Resolving Discrepancies in EU Bank Capital Instruments: Distributions, Contractual Triggers, Ranking

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Abstract

This paper examines frictions among Common Equity Tier 1 (CET1), Additional Tier 1 (AT1), and Tier 2 instruments within the European Union prudential and resolution framework across four stages: (i) distributions under going-concern conditions out of available distributable items (ADI) limited by the maximum distributable amount (MDA), (ii) contractual principal loss-absorption mechanism (PLAM) in AT1 instruments, and (iii) statutory loss-allocation at the point of non-viability (PONV), and in resolution or insolvency proceedings. The analysis identifies material divergences in the regulatory and supervisory treatment of AT1 and Tier 2 instruments across these stages and proposes targeted amendments to support a coordinated international approach, thereby promoting transparency and consistency in the capital framework.

Keywords: CET1, AT1, Tier 2, MDA, ADI, PLAM, PONV, Bail-in

JEL Classification: E44, F34, G12, G21, G28, K23

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I. Introduction

This study aims to identify discrepancies among instruments classified as Common Equity Tier 1 (CET1), Additional Tier 1 (AT1), and Tier 2 capital under European Union (EU) law (Union law), and to propose solutions for harmonisation. The primary focus, however, is on AT1 instruments, which are hybrid financial instruments that straddle the boundary between equity and debt. Contradictions are inherent in their nature: they can be declared as debt capital vis-à-vis tax authorities and investors, whereas they function as Tier 1 capital vis-à-vis

supervisory authorities and rating agencies.[1] The contradiction is evident when even implicit references to a call, redemption, or repurchase of the instruments should result in the withdrawal of their regulatory capital character,[2] whereas the German tax authorities, for instance, treat them as debt capital for tax purposes precisely because of the 'de facto market expectation to repay'.[3] Additionally, a high level of ambiguity surrounds AT1 instruments in commercial, corporate, tax, supervisory, and capital market law.

AT1 instruments have faced intense scrutiny since the banking turmoil in spring 2023, particularly after the Credit Suisse episode, where all outstanding AT1s were written down to zero, irrespective of whether they carried a high trigger (CET1 ratio of 7% of risk-weighted assets (RWA)) or the Basel III minimum trigger (5.125%), and without a prior wipe-out of CET1 instruments (notably, equity shares).[4] This has led to multiple investor lawsuits, including, in particular, state liability claims against Switzerland for allegedly wrongfully triggering execution, thereby disregarding a presumed loss absorption waterfall.

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[1] Cf. International Monetary Fund and Organisation for Economic Co-operation and Development, Financial Institutions and Instruments – Tax Challenges and Solutions (ITD Background Paper, International Tax Dialogue Conference, Beijing, Oct 2009) 10; Financial Stability Board, Corporate Funding Structures and Incentives – Final Report (28 Aug 2015) 11.

[2] Art. 52(1)(h)-(k) Regulation (EU) No 575/2013, OJ L 176, 27.6.2013, pp. 1–337 (Capital Requirements Regulation – CRR), in conjunction with Art. 20 Delegated Regulation (EU) No. 241/2014.

[3] German Federal Ministry of Finance (Bundesministerium der Finanzen - BMF), letter of 4 Nov 2021, IV C 2 – S 2742/21/10001:001 (2021/0852061); BMF letter of 25 May 2021, IV C 2 – S 2742/21/100001:001 (DOK 2021/0227797); BMF letter of 10 Apr 2014, IV C 2 – S 2741/12/10003:002 (2014/0335431).

[4] Swiss Financial Market Supervisory Authority (FINMA), 'FINMA Provides Information About the Basis for Writing Down AT1 Capital Instruments' (Press release, 23 March 2023) <https://www.finma.ch/en/news/2023/03/20230323-mm-at1-kapitalinstrumente/> accessed 12 August 2025.

Nevertheless, the European Central Bank (ECB), the European Banking Authority (EBA), and the Single Resolution Board (SRB) issued a public response reaffirming that AT1 instruments remained an important component of the capital structure of European banks.[5] The Dutch government, however, suggested a reassessment of these instruments at the Union level in a report published in March 2024.[6] The Australian Prudential Regulation Authority (APRA) decided in December 2024 to phase out the eligibility of AT1 instruments as bank capital.[7] Deutsche Bundesbank recently proposed separating capital and resolution requirements, with resolution needs met by instruments other than CET1, ensuring that CET1 remains available to absorb losses during going-concern operations while dedicated resources are held for resolution, thereby enhancing both frameworks' effectiveness.[8]

In some jurisdictions, the validity of loss-absorption mechanisms is being challenged under civil law. For example, in a recent proceeding, the Higher Regional Court of Bremen (Oberlandesgericht Bremen) took the view that certain terms of the AT1 bonds of a German Landesbank, which were based on the German banking association's model terms and

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[5] ECB Banking Supervision, Single Resolution Board (SRB) and European Banking Authority (EBA), 'Statement on the Announcement on 19 March 2023 by Swiss Authorities' (Joint press release, 20 March 2023). <https://www.bankingsupervision.europa.eu/press/pr/date/2023/html/ssm.pr230320~9f0ae34dc5.de.html> accessed 12 August 2025.

[6] Dutch Ministry of Finance, Beleidsrichtingen voor een weerbare bankensector (Policy Guidelines for a Resilient Banking Sector) (19 March 2024) 23 et seq.

[7] Australian Prudential Regulation Authority (APRA), 'APRA to Phase out AT1 as Eligible Bank Capital' (Media release, 9 December 2024) <https://www.apra.gov.au/news-and-publications/apra-to-phase-out-at1-as-eligible-bank-capital>.

[8] Michael Theurer, Europe's maze of bank regulation needs to be simplified, Guest contribution in Financial Times online (15 September 2025) <https://www.bundesbank.de/en/press/contributions/europe-s-maze-of-bank-regulation-needs-to-be-simplified-956812>.

conditions,[9] were null and void under the general terms and conditions clause-control regime on the grounds of unreasonable disadvantage and lack of transparency.[10] In doing so, the court did not treat the European Capital Requirements Regulation (CRR) or the EBA templates[11] as overriding directives that would displace clause control. The judgment – potentially affecting the validity of issuances of 20-25 billion euros under German law – remains non-final, with an appeal pending before the Federal Court of Justice (Bundesgerichtshof).[12]

Examination and analysis of Tier 2 capital instruments has largely been overshadowed by the debate surrounding AT1. This neglect is unwarranted. Although Tier 2 instruments are required to have principal loss-absorption mechanisms (PLAM) at the point of non-viability (PONV) akin to those required for AT1 instruments, their regulatory function is to absorb loss on a gone-concern basis.[13] In the Credit Suisse case, outstanding Tier 2 instruments – unlike AT1 – were left unimpaired, not least because a write-down would have triggered a default.

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[9] See Bundesverband deutscher Banken e.V. (BdB) (Hengeler Mueller), Anleihebedingungen AT1 (Typ A) (June 2019) (model terms; German text binding; English convenience translation) <https://bankenverband.de/sites/default/files/medien/4/dokumente/bdb-at1-anleihebedingungen_stand-062019_0.pdf> accessed 12 August 2025; see also BdB (Hengeler Mueller), Musterbedingungen Kapitalinstrumente: AT1-Instrument Typ B (Bedingte Pflichtwandlung) (Final version, 20 Feb 2014) <https://bankenverband.de/sites/default/files/medien/4/dokumente/at1-typb_finale-fassung_20022014_0.pdf> accessed 12 August 2025.

[10] Higher Regional Court of Bremen (OLG Bremen), Judgment of 7 May 2025, Case 1 U 15/24, ECLI:DE:OLGHB:2025:0507.1U15.24.00.

[11] European Banking Authority, EBA Standardised Templates for Additional Tier 1 (AT1) Instruments—Final (10 Oct 2016) <https://www.eba.europa.eu/sites/default/files/documents/10180/1509035/ce913725-8021-4997-958d-1428471dc837/Final%20AT1%20standard%20templates.pdf> accessed 12 August 2025.

[12] Federal Court of Justice (Bundesgerichtshof, BGH), pending, Case XI ZR 55/25.

[13] Basel Committee on Banking Supervision (BCBS), Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems (2011, various updates), Sec. 49(2), and Sec. 58.

The remainder of this paper is arranged as follows: First, the foundations of AT1 instruments and their relations to CET1 instruments, as well as the background of Tier 2 instruments and their relations to Tier 1 instruments, are presented in Section II. The three sections that follow discuss the conflicts arising due to loss sharing between the different types of instruments, depending on the situation in which the sharing of losses is required. The disparate treatment regarding distributions in an ongoing business operation is presented in Section III, while the moderating responses of the instruments upon the occurrence of a contractual trigger event are contrasted in Section IV. Finally, the different treatments available once the institution becomes non-viable or enters default are considered in Section V. Section VI concludes.

II. Foundations

The internationalisation of the prudential regulation of banks led to the recognition of hybrid financial instruments as capital components in continental Europe at the end of the 1980s. The Basel Committee of Banking Supervision (BCBS) plays a crucial role in international banking regulation. However, its international regulatory standards are intended to be non-discriminatory, meaning that they must be suitable for different types of companies, different national legal systems, and different accounting standards.[14] For this reason, the BCBS decided not to define capital instruments based on company law (common shares, etc.), but instead uses a principle-based definition ('substance over form'). The criteria of the International Financial Reporting Standards (IFRS; formerly, the International Accounting Standards (IAS)) were also taken into account.

Despite the measures taken to promote enduring institutional solvency, the 2007-09 financial crisis revealed an inadequate level of high-quality capital, divergences in the definition of

[14] BCBS, International Convergence of Capital Measurement and Capital Standards (Basel I, 1988; rev 1998) Sec. 9; BCBS, International Convergence of Capital Measurement and Capital Standards – A Revised Framework (Basel II, 2006) Sec. 12.

capital in different jurisdictions, and inadequate disclosure.[15] Hybrid bonds, which were eligible as regulatory capital, failed to achieve their purported liability effect, being allowed to do so in some cases by the supervisory authorities.[16] The BCBS's intention with the Basel III reforms was therefore to increase both the quality and quantity of the regulatory capital base in the form of CET1 capital, for which a new subcategory of Tier 1 capital was created.[17] Apart from that, the new class of 'Additional Tier 1 capital' was also introduced. Its eligibility criteria were revised, and its eligibility was limited. The goal was to improve the loss-absorbing capacity of AT1 capital instruments in ongoing business operations ('going concern').

The main innovations included, firstly, the formalisation of a distribution stop, calibrated to a potential shortfall in the newly introduced capital buffers. Secondly, a PLAM (conversion to CET1 instruments or a write-down mechanism for instruments classified as liabilities),[18] was introduced. Thirdly, the reforms provided for coordination with the new statutory intervention measures at the PONV and in resolution or insolvency proceedings.

The key distinction between Tier 2 and Tier 1 capital lies in their loss-absorption purposes: Tier 2 is required to absorb losses only in a gone-concern scenario – that is, once a negative going-concern assessment has been made. Consequently, the loss-absorption features of Tier 2 items are markedly less rigid than those applicable to Tier 1. As with AT1, there is no requirement that Tier 2 instruments qualify as equity for accounting purposes.

[15] Basel III, Sec. 48.

[16] BCBS, Press Release No 03/2011 (13 January 2011).

[17] Basel III, Sec. 7.

[18] Basel III, CAP10.11 (11).

To conclude, Tier 1 and Tier 2 together constitute 'own funds' under Articles 4(1)(118) and 72 CRR and thus 'total capital' within the meaning of Article 92(2)(c) CRR, while Tier 1 is subdivided into CET1 and AT1.

III. Distributions in ongoing business operations

1. AT1 vs. CET1 instruments

Distributions on Tier 1 instruments must be at the unrestricted discretion of the issuer and are regulated in two ways: they may only be paid out of 'distributable items' (usually referred to as 'available distributable items' (ADI)),[19] and their amount is limited to the 'maximum distributable amount' (MDA), unless the combined buffer requirement is met. ADI and MDA must be kept strictly separate.

a) Independence of distributions on capital instruments

Distributions on the various capital instruments must not be made dependent on each other through *pari passu* clauses. Clauses that require distributions to be made if distributions are paid on subordinated instruments or on instruments of equal rank ('dividend pushers') are not compatible with the required distribution discretion.[20] Furthermore, Union law does not permit features that could hinder recapitalisation or that force the suspension or limitation of distributions on CET1 or AT1 instruments if no distribution is made on the relevant instruments ('dividend stoppers').[21]

[19] Art. 28(1)(h)(ii) CRR, and Art. 52 (1)(l)(i) CRR, each in conjunction with Art. 4(1) No. 128 CRR.

[20] Art. Art. 53 (1) CRR.

[21] Art. Art. 53 (2) CRR.

b) Available distributable items

The regulatory definition of 'distribution' equates interest payments with dividends.[22] ADI is defined separately for Tier 1 (CET1 and AT1) instruments in Article 4(1) No. 128 CRR. It includes the profit determined in accordance with national accounting law at the end of the last financial year, plus any profit carried forward and reserves available for this purpose, less any losses carried forward, non-distributable profits, and non-distributable reserves.

Interest and repayments on AT1 instruments that do not qualify as equity under company law are not deemed distributions for purposes of accounting and company law, but rather operating expenses or the repayment of liabilities with no effect on (taxable) profit. Under accounting and company law, they can therefore be made even if they result in losses for which statutory reserves must be released.[23] Against this backdrop, a viable interpretation is that for AT1 instruments, all reserves recognisable under national accounting principles, such as German Commercial Code (Handelsgesetzbuch – HGB) standards, should qualify as ADI.[24] This should even include amounts barred from distribution within the meaning of Sec. 268(8) HGB or the statutory reserve to be formed in accordance with Sec. 150, ss. I, III(2) of the German Stock Corporation Act (Aktiengesetz – AktG).[25]

However, this interpretation should be qualified in an opinion presented in academic literature. The regulatory recognition of hybrid instruments as a component of own funds

[22] Art. 4(1) No. 110 CRR.

[23] In practice, the combination of an accumulated loss with a distribution is a rather theoretical case, as institutions would likely release reserves, or possibly hidden reserves, in order to avoid an accumulated loss. See Melanie Armbruster, Martin Böhringer, and Urs Lendermann, 'Ausschüttungsfähige Posten und Instrumente des Zusätzlichen Kernkapitals' (2024) Recht der Finanzinstrumente (RdF) 300.

[24] Deutsche Bundesbank, Monthly Report (June 2019) 31, 38–39.

[25] Cf. Deutsche Bundesbank, loc. cit.

differs from company law.[26] The amendment of Article 4, para. 1, No. 128 CRR by CRR II[27] has led to uncertainty due to its unclear language. Systematically, CET1 instruments and AT1 instruments are regulated in the same way with respect to ADI.[28] Therefore, all Tier 1 instruments shall be used uniformly for loss absorption in a going concern, by dividend or coupon cancellation, irrespective of their treatment under different accounting standards and company law systems. Accordingly, Article 52(1)(l)(i) CRR, in conjunction with Article 4(1) No. 128, should be interpreted in such a way that amounts that are subject to a prohibition on distributions for CET1 instruments may also not be distributed to the holders of AT1 instruments.[29]

c) Maximum distributable amount

Regarding the MDA, the term 'distribution' also includes repayments on amounts paid in and is therefore broader than the definition of distributions contained in Article 4(1) No. 110 CRR, which is limited to the payment of dividends or interest.[30] In contrast to distributable items, the calculation of the MDA is not based on balance sheet information and company law at the individual institution level, but on regulatory capital requirements[31] (and, with regard to the leverage ratio buffer for global systemically important institutions, also on the leverage

[26] Martin Böhringer and Urs Lendermann in: Beck, Samm, and Kokemoor, (eds), KWG/CRR Commentary (2024), Art. 51 CRR, para. 9 et seq.

[27] Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019, amending Regulation (EU) No 575/2013 (CRR II).

[28] Art. 28(1)(h)(ii), and Art. 52(1)(l)(i) CRR.

[29] Armbruster, Böhringer, and Lendermann, RdF 2024, 304.

[30] See national adoption example in Sec. 10i(5) No. 4 and Sec. 10j(5) No. 2 of the German Banking Act (Kreditwesengesetz – KWG).

[31] Sec. 10i KWG.

ratio[32]), or in a group context, at all levels of application (consolidated, sub-consolidated basis, and individual basis).

In the draft version of the Capital Requirements Directive (CRD V), the European Commission had proposed a priority for AT1 instruments over CET1 instruments regarding MDA.[33] However, the EBA opined against the proposed preferential treatment of distributions on AT1 instruments, referring to the improved loss absorption of these instruments in ongoing business operations.[34] A pecking order – wherein distributions on AT1 instruments would have to be the last to be restricted and the first to be paid – would restrict the discretion of institutions in cases where not all distributions can be (fully) made. Ultimately, the adopted CRD V[35] did not reflect such an order of priority. For distributions to which MDA requirements apply, there is neither an equal treatment obligation nor a prioritisation or subordination of any of the two Tier 1 capital instrument types.

In its AT1 case, OLG Bremen holds that § 10i(3) German Banking Act – implementing CRD IV Art. 141 – imposes only a temporary distribution ban: once the combined buffer is restored or a capital conservation plan is approved, distributions could resume; neither German nor EU law would contemplate a permanent ban beyond the shortfall.[36] The court rightly distinguishes statutory law from contract: Art. 52(1)(l) CRR flexibility condition 'any-time, indefinite, non-cumulative' is a contractual design requirement for regulatory eligibility.

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[32] Art. 92(1)a CRR; Sec. 10j KWG.

[33] European Commission, Proposal for a Directive amending Directive 2013/36/EU (CRD) COM(2016) 854 final (23 Nov 2016).

[34] European Banking Authority, Opinion on Own Funds in the Context of the CRR Review (EBA/Op/2017/07, 23 May 2017) Sec. 11–14.

[35] Directive (EU) 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU …, OJ L 150, 7.6.2019, pp. 253–295.

[36] Higher Regional Court of Bremen (OLG Bremen), Judgment of 7 May 2025, Case 1 U 15/24, ECLI:DE:OLGHB:2025:0507.1U15.24.00.

Yet policing AT1 via German clause-control is ill-suited: it is ex post and forum-dependent, undermines Single-Rulebook uniformity, and destabilizes capital planning. Substantively, there is no civil right to catch-up cancelled coupons; CET1 permanence would be eroded, and the narrow write-up pathway for temporary write-downs (Art. 52(1)(n), 52(2) CRR; Art. 21 Del. Reg. 241/2014) applies to principal (see below), not coupons. A regulatory fix is preferable to clarify in the CRR that cancelled AT1 coupons are final and codify a positive list of permissible discretion/non-accrual formulations, and contractual discretion, thus preserving CET1 logic, reducing forum shopping, and aligning private law practice with the Single Rulebook.

2. Tier 2 vs. Tier 1 instruments

Distributions on Tier 2 instruments are not required to be made from 'distributable items' within the meaning of Article 4(1)(128) CRR. In contrast to AT1, Tier 2 instruments are generally treated as 'must-pay' obligations;[37] failure to pay coupons may be regarded as an event of default.[38] Subject to narrow conditions, the EBA considers 'classic' dividend pushers or stoppers compatible with Tier 2, given that Articles 63 et seq. CRR do not contain a provision equivalent to Article 53 CRR.[39] A purely discretionary deferral of coupons on Tier 2 instruments following the cancellation of distributions on higher tiers does not, in the EBA's view, amount to an indirect restriction on CET1 or AT1 discretion.[40] By contrast, so-

[37] European Banking Authority, Opinion on the Prudential Treatment of Legacy Instruments EBA/Op/2020/17, Sec. 10.

[38] Art. 63 CRR contains no clause analogous to Art. 21(1)(h)(vi) and Art. 52(1)(l)(iv) CRR – namely, that 'cancellation of distributions does not constitute an event of default of the institution' (see Basel III, Sec. 53(6)).

[39] See also Articles 28(1)(h)(vii), 52(1)(l)(v), and 53 CRR (requirement of 'full flexibility of payments' for CET1/AT1).

[40] EBA/Op/2020/17, para. 10.

called ‘reverse stoppers’, that cancel distributions on Tier 2 instrument when CET1 or AT1 distributions are not made, may create an infection risk for higher capital tiers because they constrain the ‘full flexibility of payments’ required for CET1 and AT1; the consequence of their inclusion in Tier 2 instruments may be the disqualification of higher capital tiers, even where the Tier 2 instrument itself would otherwise be eligible.[41]

IV. Non-discretionary contractual principal loss absorption mechanism

1. Trigger mechanisms of AT1 instruments

Contractual principal loss absorption mechanisms (PLAM) of AT1 instruments vary fundamentally in terms of their liability rank and their impact on the losses borne by shareholders. However, all AT1 instruments issued by EU banks share common characteristics, including the non-discretionary trigger event, automatic triggering (without any activation by the issuer or the supervisor), contribution to CET1 capital in the form of a debt-to-equity swap (with or without the issuance of new CET1 instruments as compensation), as well as individual procedural elements when the trigger event occurs.[42]

a) Trigger thresholds of CET1 capital ratio

Contingent convertible (CoCo) instruments convert into CET1 instruments upon the trigger event.[43] On the threshold calibration, the Swiss Commission of Experts suggested a ‘high trigger’ (CET1) threshold of 7% of RWA) for ‘recovery CoCos’ and a ‘low trigger’ (CET1 threshold of 5% of RWA) for ‘resolution CoCos’. While AT1 capital is intended for use with a going concern, the BCBS chose the low-level resolution trigger (slightly adjusted to a CET1 ratio of 5.125% of RWA). This calibration at 5.125% (0.625 percentage points above the

[41] EBA/Op/2020/17, para. 13; see also EBA Q&A 2013 No.2112.

[42] Art. 54 Abs. 5 in conjunction with Art. 22 Abs. 1 Delegated Regulation (EU) No 241/2014.

[43] Art. 52 para. 1(n) Alt. 2 CRR.

CET1 minimum ratio requirement of 4.5%) is linked to the last of the four stages of distribution restrictions under the combined buffer requirement.[44]

A core conceptual issue is that the contractual trigger is calibrated solely to the CET1 capital ratio. In accordance with the 'better-capital' principle in the CRR, institutions may satisfy the total capital requirement by substituting AT1 with CET1 capital and Tier 2 with Tier 1 (AT1 or CET1). If, therefore, an institution meets its total capital requirement – including the combined buffer requirement – predominantly with CET1 and only marginally with AT1, a 5.125% CET1 trigger threshold will be reached only after the Pillar 1 minimum total capital ratio (8% of RWA) has already been materially breached. For prudential purposes, basing the trigger on the total capital ratio (TCR) would be more sound. The corresponding threshold would be 8.625% – i.e., the 5.125% CET1 trigger plus 1.5 percentage points for the minimum AT1 component and 2.0 percentage points for the minimum Tier 2 component (5.125 + 1.5 + 2.0 = 8.625%).

Even with a more coherent threshold implemented, a second conceptual difficulty would remain: writing down or converting AT1 into CET1 improves the quality of own funds but not their quantity. Total capital does not increase, so the implicit calibration premise – that activating AT1 would replenish the combined buffer requirement – does not hold.

More generally, the omission of a risk-insensitive trigger merits reconsideration. Because the buffer concept has been extended to the leverage ratio,[45] calibrating the trigger to the leverage ratio would be consistent with the current framework.

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[44] Basel Committee of Banking Supervision, Evaluation of the Impact and Efficacy of the Basel III Reforms (Dec 2022) rec 124; Urs Lendermann, 'Automated Bail-in: Eliminating Regulatory Restraints' (2025) Journal of Banking Regulation <https://doi.org/10.1057/s41261-024-00266-7>.

[45] See Art. 92(1a) CRR.

The CRR specifies qualitative minima for AT1 eligibility. Thereby, Union law implements a floor: although higher trigger thresholds than 5.125% and additional trigger events are permissible,[46] lower trigger levels or fewer trigger events than those required by Article 52(1)(n) CRR in conjunction with Article 54(1)(a)(i) CRR at the relevant level of consolidation render instruments ineligible as AT1. During the banking crisis, certain national competent authorities (such as those in Spain, Ireland, Portugal, and Greece) required several banks to hold AT1 capital with write-down triggers set at levels up to and even above 7% of the CET1 capital ratio. At present, the EU Single Rulebook bars member states from introducing generally applicable deviations from the CRR or CRD IV standards, irrespective of stringency.[47] By contrast, institution-specific measures under Pillar 2 (e.g., pursuant to Article 104 CRD IV and related ECB and EBA guidance) may require firms to maintain higher trigger thresholds so long as such measures do not undermine CRR eligibility and are applied proportionately.

Given the doubts about the effectiveness and timeliness of existing triggers and loss-absorption mechanisms,[48] the literature advocates incorporating a market-based trigger – e.g., a share-price trigger set at a penny-stock threshold[49] – to complement the PONV trigger, as discussed below.

b) Fundamental differences between the instruments

In regulatory terms, three stylised forms of loss-absorption are observed with AT1 instruments: (1) conversion into CET1 at a pre-specified or formula-based rate; (2) permanent

[46] Art. 54(1)(a)(ii), (b) CRR.
[47] EBA Q&A 2013 No. 39 (31 October 2013).
[48] Bank of England, Financial Stability Report (June 2014) 34–35; Deutsche Bundesbank Monthly Report (March 2018) Vol. 70 No. 3, 61.
[49] Cf. Urs Lendermann, 'Automated Bail-in: Eliminating Regulatory Restraints' (2025) Journal of Banking Regulation <https://doi.org/10.1057/s41261-024-00266-7>.

write-down; and (3) temporary write-down with the contractual possibility of subsequent write-up. These forms differ not in the quantum of loss borne at the trigger but in their post-trigger treatment – namely, whether holders receive compensation (shares) and, consequently, whether their position improves in the creditor hierarchy and scope for value recovery (potential upside) under the instrument's contractual terms.[50]

(1) Contingent convertible instruments

The conversion ratio of a CoCo determines the amount of its initial liability participation as well as the dilution of value and voting rights of its existing shareholders. The former CoCo holders are automatically held liable for future losses as new holders of CET1 instruments. However, they will also participate in recovery, based on potential future profits.

(2) Permanent write-off instruments

In contrast to CoCos, permanent write-off instruments ('write-offs') are not related to corporate law (e.g., in Germany, they are not subject to the German Stock Corporation Act), and there is no issuance of new shares that could cause technical and legal issues.[51] The banks' preference for write-offs over CoCos can be attributed to their anticipation of shareholder resistance against dilution caused by the conversion of CoCos into new shares. Essentially, shareholders strive to avoid erosion of their control, while management is cautious about the complexities associated with contingent capital through shareholder resolutions.[52] From a regulatory perspective, the main concern lies in the efficacy of loss

[50] Deutsche Bundesbank, 'Contingent Convertible Bonds: Design, Regulation, Usefulness' (March 2018) Vol. 70 No. 3 Monthly Report, 60.

[51] Urs Lendermann, 'Automated Bail-in: Eliminating Regulatory Restraints' (2025) Journal of Banking Regulation.

[52] See Deutsche Bundesbank, (March 2018) 70 Monthly Report, 60; Stefan Avdjiev et al., 'CoCo Issuance and Bank Fragility' (2017) BIS Working Paper 678.

absorption of AT1 instruments in a going-concern, while restrained regulation is favoured by those who argue for more flexibility in the contractual arrangements between banks and investors.[53]

In contrast to holders of CoCos, holders of write-offs do not participate in a future financial recovery. The write-down of the receivable is imposed without compensation.[54] If the contractual liability mechanisms are viewed in isolation and the statutory liability cascade is disregarded, the following applies: write-offs rank junior to CET1 instruments. When the contractual trigger event occurs and the write-offs are written down (in full), the bank still has a CET1 capital ratio of close to 5.125%. The contractual loss-absorbing mechanism does not provide for the deletion of any instruments subordinated to them, i.e., CET1 instruments (unlike in resolution, pursuant to Art. 47(1)(a) Bank Recovery and Resolution Directive – BRRD). As this contradicts the eligibility criterion for CET1 instruments set forth in Article 28(1)(i) CRR, i.e. that CET1 instruments shall bear the first and proportionally largest share of losses, an explicit exception was included for write-offs in Article 28(2) CRR. The loss participation of write-offs therefore benefits not only the creditors, but also the shareholders. Write-offs essentially insure the shareholders.[55]

(3) Temporary write-down instruments

In order to mitigate the conceptual liability asymmetry of write-offs vis-à-vis shareholders, and to increase marketing opportunities, a temporary write-down with a subsequent write-up

[53] Edoardo D. Martino, Casimiro Antonio Nigro, and Tom Vos, in 'CoCos in Europe: What Is Wrong – and How to Fix It?' (29 April 2024) European Banking Institute Working Paper Series 169, Amsterdam Law School Research Paper 18/2024, Amsterdam Center for Law & Economics Working Paper 09/2024 <https://ssrn.com/abstract=4810761>.

[54] Art. 52(1)(n), second alternative CRR.

[55] Böhringer, Ihme, and Lendermann in: Beck, Samm, and Kokemoor, KWG/CRR Commentary (2024), Art. 52 CRR para. 157.

feature was permitted for write-down instruments[56] after several discussions.[57] The write-up involves a repayment of the CET1 items (to the benefit of (former) AT1 holders) to which the write-down of the instruments previously led. To address the issue of permanence of CET1 instruments[58] on the one hand and (in the case of corporations) the issue of capital maintenance[59] on the other, an exception was created in Article 52(1)(n) Alt 1, second alternative CRR. A bank must have full flexibility with regard to write-ups. A write-up is considered a distribution and shall therefore be fully discretionary and subject to ADI and MDA restrictions, as set forth in Article 21 Delegated Regulation (EU) No. 241/2014.

In short, the post-trigger treatment specified in the contractual terms places CoCos, write-offs, and temporary write-downs in very different positions in the creditor hierarchy and thus yields distinct recovery profiles.

2. Debate on trigger mechanisms in Tier 2 instruments

In contrast with AT1 instruments, the Union law does not require Tier 2 instruments to be embedded with a specific, contractual, and non-discretionary PLAM.[60] This raises the question of whether institutions may voluntarily incorporate such a mechanism into Tier 2. Market practice has also shown experimentation with so-called 'Risk-Adjusted Capital Tier 2'

[56] Art 52(1)(n), second alternative CRR, in conjunction with Art. 21 Delegated Regulation (EU) No. 241/2014.

[57] The draft initially envisaged only a permanent write-down. BCBS, Consultative Document, Proposal to ensure the loss absorbency of regulatory capital at the point of non-viability (August 2010). It was noted that the word 'permanent' was dropped in the final PONV press release because many consultation responses had objected to it.

[58] Art. 28(1)(f) CRR.

[59] E.g., Secs. 57, 71 AktG.

[60] Art. 62 et seq. CRR contain no provision comparable to Art. 52(1)(n) in conjunction with Article 54 CRR.

(RAC Tier 2) instruments that include a contractual 'trigger event' and a 'rating methodology event' to achieve equitable treatment in certain rating methodologies.[61]

From a prudential perspective, contractual loss-absorption features in Tier 2 should not create an 'infection risk' for higher capital tiers. If the activation of a contractual Tier 2 write-down were itself treated as an event of default, outstanding AT1 instruments – whose PLAM might trigger at the same or even a lower CET1 threshold – would cease to function as going-concern loss-absorbing capital. Just as the EBA has cautioned regarding reverse stoppers in Tier 2, such designs risk 'infecting' CET1 and AT1; *a fortiori*, a Tier 2 trigger that could precipitate default warrants even stricter scrutiny.

Article 28(1)(i) CRR reflects the Basel III, para. 53, criterion 8 standard, under which CET1 shall absorb the first and proportionately greatest share of losses. The exception in Article 28(2), first subparagraph, CRR was introduced primarily with AT1 in mind (to implement Basel III, fn 13). In structures involving write-offs, the AT1 trigger may be hit while the CET1 ratio remains at 5.125% of RWA (or higher), meaning that the AT1 absorbs losses ahead of residual CET1; by contrast, AT1 contingent convertibles (genuine CoCos), once converted, rank *pari passu* with CET1 thereafter. In these scenarios, common shares are still deemed to meet the criterion. Accordingly, Article 28(2) CRR should be construed narrowly and confined to those permanent write-down cases. Any application of this article to Tier 2 should be exceptional, as it could lead to normalisation of *pari passu* loss-sharing between Tier 2 and CET1 in a going-concern setting.

[61] See EBA, Report on the Monitoring of Additional Tier 1 (AT1), Tier 2, and TLAC/MREL-Eligible Liability Instruments of European Union (EU) Institutions – Update (EBA/Rep/2023/23), para. 214, 218. Eee e.g. BPCE, Tier 2 Contingent Write-down (Prospectus, 2021–13/2021–14; 7%(!) trigger) <https://www.groupebpce.com/app/uploads/2023/11/Prospectus-BPCE-Tier-2-contingent.pdf> accessed 12 August 2025.

Under Article 52(1)(d) CRR, Article 21, para. 10 SRMR, and Article 60, para. 1 BRRD, AT1 ranks below Tier 2 in insolvency. Allowing Tier 2 instruments to absorb losses before AT1 (via a contractual Tier 2 trigger) would invert this hierarchy. Consistent with its gone-concern role, Tier 2 shall thus not include the AT1-style contractual mechanism set out in Articles 52(1)(n) and 54 CRR. The EBA has flagged eligibility risks and discourages their use.[62]

V. Discretionary loss absorption at the point of non-viability or in resolution or insolvency proceedings

1. PONV vs. Bail-in

This section distinguishes the loss absorbency of regulatory capital at the point of non-viability (PONV) from that in the application of a bail-in, in resolution, insolvency proceedings, and liquidation, by timing and purpose – going-concern stabilisation versus gone-concern resolution versus insolvency proceedings – and by their implications on the triggering of an event of default.

Tier 2 instruments rank senior to AT1 in the creditor hierarchy[63] and, unlike AT1, are not typically embedded with a contractual, non-discretionary loss-absorption mechanism.[64] Instead, Tier 2 is only subject to statutory write-down or conversion powers exercised by the resolution authority under Article 21 SRMR and Article 59 BRRD.[65] These powers adopt the

[62] EBA/Rep/2023/23 para. 218.

[63] Art. 52 (1)(d) CRR and Art. 21(10) Regulation (EU) No. 806/2014 of the European Parliament and of the Council (15 July 2014) establishing a Single Resolution Mechanism (Single Resolution Mechanism Regulation, SRMR); Art. 60 Abs. 1 Directive 2014/59/EU of the European Parliament and of the Council (15 May 2014) establishing a framework for the recovery and resolution of credit institutions and investment firms (Bank Recovery and Resolution Directive, BRRD), according to the national transposition in the EU member states.

[64] Art. 62 CRR lacks a rule equivalent to that in Art. 52(1)(p) in conjunction with Art. 54 CRR.

[65] Art. 21 SRMR; Art. 59 BRRD (and national transposition).

BCBS requirement to ensure loss absorption at the PONV[66] to address concerns about the timeliness of contractual loss-absorption,[67] as well as the Financial Stability Board's (FSB) concept of using the bail-in as a resolution tool.[68]

The BCBS language regarding the PONV demonstrated particular relevance in the Credit Suisse case. It provides:

> The trigger event is the earlier of:
> (1) a decision that a write-off, **without which the firm would become non-viable**, is necessary, as determined by the relevant authority; and
> (2) the decision to make a public sector injection of capital, or equivalent support, **without which the firm would have become non-viable**, as determined by the relevant authority.[69] (emphasis added)

Functionally, the PONV write-down/conversion power resembles the bail-in tool. According to the FSB Key Attributes, the bail-in tool is intended to be applicable to CoCos and other contractual bail-in instruments that have not already absorbed losses prior to resolution through any PLAM.[70] The FSB further envisages that regulatory capital may count toward

[66] Sec. 49, Basel III, fn 9 and BCBS, Press release, Ref no. 03/2011 (13 January 2011) Annex: 'Minimum Requirements to Ensure Loss Absorbency at the Point of Non-Viability'; see also BCBS, Consultative Document: Proposal to Ensure the Loss Absorbency of Regulatory Capital at the Point of Non-Viability (2010).

[67] Bank of England, Financial Stability Report (June 2014) 34–35; Deutsche Bundesbank Monthly Report (March 2018) Vol. 70 No. 3, 61.

[68] Financial Stability Board, Key Attributes of Effective Resolution Regimes for Financial Institutions (Oct 2011; update Oct 2014) Key Attributes 3.1, 3.2(ix), 3.5.

[69] Recital 49, Basel III fn 9 iVm, Press release no. 03/2011 (13 January 2011) Annex: 'Minimum requirements to ensure loss absorbency at the point of non-viability'.

[70] FSB, Key Attributes 3.2 (ix), 3.5.

total loss-absorbing capacity (TLAC), provided the bail-in tool can be applied to such instruments with legal certainty.[71]

At least with respect to AT1, the PONV requirement properly functions as an early-intervention measure for stabilisation: AT1 is designed to absorb losses on a going-concern basis, and its activation under the BCBS standard is intended to preserve or restore the institution's viability ('*without which* the firm would become non-viable' [72]).

By contrast, the bail-in is a resolution tool exercised by the resolution authority in formal resolution proceedings. It is applied 'when a firm is no longer viable or likely to be no longer viable, and has no reasonable prospect of becoming so'[73] (under EU law: 'failing or likely to fail – FOLTF'[74]). The general role and scope of the different standard-setting bodies responsible for each – the BCBS for PONV and the FSB for bail-in – also provide some explanation for the divergence in timing and purpose.

Irrespective of the differentiation in the objective and the stage of application (going-concern stabilisation vs. gone-concern resolution) and timing, EU law places both interventions within the purview of the resolution authorities:[75] the general write-down/conversion power (Art. 21 SRMR; Art. 59 BRRD) and the bail-in tool (Art. 27 SRMR; Art. 44 BRRD). The PONV is not a supervisory early-intervention power and does not appear in the CRD catalogue (Art. 104 CRD IV). In EU terminology, 'bail-in' designates the resolution tool applied to liabilities,[76] while for 'write-down or conversion of capital instruments and eligible

[71] FSB, Total Loss-absorbing Capacity (TLAC) Term Sheet (9 Nov 2015) rec. 6, 13, 14.

[72] BCBS, Press release, Ref no. 03/2011 (13 January 2011) Annex: 'Trigger event', No. 4 and 5.

[73] FSB, Key Attribute 3.1.

[74] Art. 18(4) SRMR; Art. 32(4) BRRD.

[75] See Rec. 45 of the CRR. In this regard, and with regard to the inconsistent terminology, crit. Binder, Glos, and Riepe (eds.), Handbuch Bankenaufsichtsrecht, Sec. 18, para. 71 et seq.

[76] Art. 27 SRMR; Art. 44 BRRD.

liabilities', the legislation uses the distinct heading.[77] Under Article 59(1), first subparagraph, BRRD (mirrored by Art. 21 SRMR), the resolution authority may exercise the power to write down or convert capital instruments and eligible liabilities, either as a stand-alone measure outside resolution or in conjunction with a resolution action.

2. AT1 and Tier 2 instruments at the PONV

At the PONV, both AT1 and Tier 2 instruments may be required to absorb losses to forestall a 'failing or likely to fail' (FOLTF) determination – or, if a public bailout averts failure, to ensure proportionate burden-sharing by those instruments. The policy rationale for calling Tier 2 instruments at the PONV is to avoid a windfall for its holders; absent state aid, the firm would likely enter a gone-concern scenario in which Tier 2 holders would bear losses in any event. Accordingly, the effective point of liability (loss absorption) is now the same for AT1 and Tier 2 instruments, even if a hierarchical order of loss allocation may still apply upon trigger. However, requiring Tier 2 to absorb losses in a going concern runs counter to its intended gone-concern role. Worse, doing so would typically trigger an event of default, potentially precipitating the very gone-concern scenario with uncertain system-wide effects that the PONV determination is meant to avert. This provides some insight as to why, in the Credit Suisse episode, PONV measures were applied to AT1 but not to Tier 2 instruments.

Against this background, the conventional divide between going-concern capital (Tier 1) and gone-concern capital (Tier 2 and TLAC-eligible liabilities) appears increasingly artificial, unless and until the orderly resolvability of G-SIBs (global systemically important banks) is demonstrably assured. Accordingly, this paper advocates introducing a rule (on a basis analogous to AT1[78]) that calling Tier 2 capital to absorb losses at the PONV shall not, in

[77] Art. 21 SRMR; Art. 59 BRRD.

[78] Basel III, Sec. 53.6 and Sec. 55.7, s (b).

itself, constitute an event of default and, in particular, should not trigger early-termination rights under financial contracts or credit events under credit default swaps (CDS).[79] Excluding Tier 2 instruments from the PONV regime would not be an appropriate alternative, as it would call into question their status as regulatory own funds.

3. EU statutory waterfall vs. contractual PLAM

This section contrasts the order of loss allocation that results from the respective type of contractual PLAM of AT1 instruments (as noted above) with the statutory order of loss allocation under Union law, which applies uniformly across three scenarios: (i) at the PONV (Art. 21(10) SRMR; Art. 60 BRRD, with national transposition); (ii) upon application of the bail-in tool, when the institution is FOLTF (Art. 27 SRMR; Art. 44 BRRD); and (iii) in insolvency (Art. 48(7) BRRD, and national implementation).

Following the idea that debt instruments should be held liable only after equity instruments, and based on the equity-first principle set forth in Article 28(1)(i) CRR, AT1 instruments shall always take precedence over CET1 instruments at the PONV, in resolution, or in insolvency cases under Union law. This statutory ordering does not, by itself, ensure that AT1 instruments effectively deliver going-concern loss absorption or fully align with the role of CET1 capital; nor does it accommodate the contractual heterogeneity of AT1 (CoCos, permanent write-downs, and temporary write-downs). There is no general normative basis for subordinating CET1 to AT1 (or vice versa) outside the legislated sequence. However, transparent, predictable, and impartial application of the statutory waterfall increases acceptance of loss allocation, reduces litigation risk, and mitigates post-crisis market-access frictions.

[79] Urs Lendermann, 'Automated Bail-in: Eliminating Regulatory Restraints' (2025) Journal of Banking Regulation.

In Switzerland, the BCBS's PONV standard was implemented not by statute but contractually, via the terms and conditions of the AT1 (and Tier 2) instruments. When Credit Suisse received extraordinary emergency liquidity assistance from the Swiss National Bank, backed by a federal guarantee, the Swiss Financial Market Supervisory Authority (FINMA) gave effect to the contractual AT1 write-off provisions through an early intervention measure[80] based on an emergency ordinance adopted by the Federal Council as an early-intervention measure.[81] Under that (now-repealed) ordinance, AT1 instruments were to be written down in full, without compensation, without a prior wipe-out of outstanding CET1 instruments, and irrespective of whether the AT1 carried a 7% or 5.125% trigger.

While the EBA had previously cautioned against features that could privilege AT1 distributions in a going concern, it issued a joint press release together with the ECB and the SRB on 20 March 2023 in response to the announcement by Swiss authorities on 19 March 2023 regarding the uncompensated write-down of the AT1 instruments issued by Credit Suisse.[82] In that joint statement, the three EU authorities explicitly highlighted the following points:

> The **resolution framework** implementing in the European Union the reforms recommended by the Financial Stability Board after the Great Financial Crisis has

[80] See Swiss Financial Market Supervisory Authority (FINMA), Casuistry, Authorized, No. 2023-02; see also Federal Administrative Court, Press release on the write-off decision B-2254/2023 (15 May 2023).

[81] Art. 5(a) of the Ordinance on Additional Liquidity Support Loans and the Granting of Default Guarantees by the Confederation for Liquidity Support Loans by the Swiss National Bank to Systemically Important Banks, inserted by No. I of the Ordinance of 19.3.2023 (RO 2023 136), Repealed by No. I of the Ordinance of 6.9.2023, with effect from 15.9.2023 (RO 2023 495).

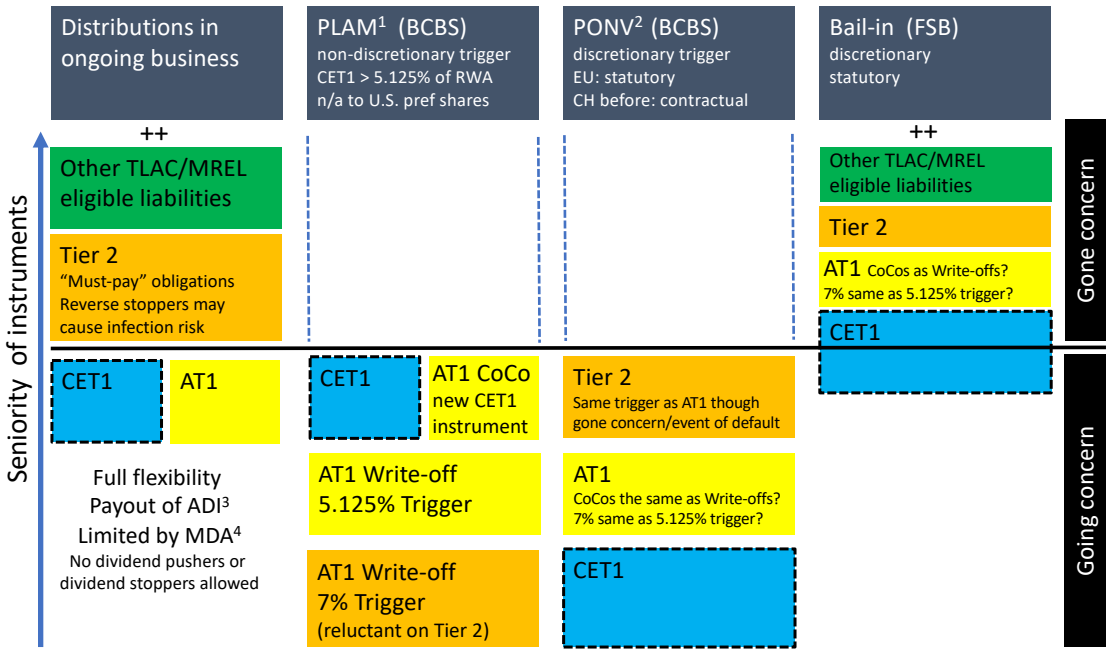
[82] ECB, SRB, and EBA Statement on the Announcement on 19 March 2023 by Swiss Authorities in the Joint Press Release dated 20 March 2023.

established, among others, **the order** according to which shareholders and creditors of a troubled bank should bear losses.

In particular, **common equity instruments are the first ones to absorb losses**, and **only after their full use would Additional Tier 1** [instruments] **be required to be written down**. This approach has been consistently applied in past cases and will continue to guide the actions of the SRB and ECB banking supervision in crisis interventions.[83] (emphasis and amendment added)

A contradiction in policies thus persists not only in relation to the Swiss framework but also within Union law regarding the different stages of application as shown on the table below.

Table: Discrepancies in the hierarchy of CET1, AT1, and Tier 2 instruments



Notes:
[1]Principal loss-absorbing mechanism
[2]Loss absorption at the point of non-viability to avoid a gone-concern scenario
[3]Available distributable items
[4]Maximum distributable amount

[83] Statement by ECB, SRB, and EBA, ibid.

Thus, it is crucial to increase the consistency, transparency, and simplicity of the trigger event and the ranking of AT1 and Tier 2 instruments. This can be accomplished by aligning trigger mechanisms so that instrument seniority remains consistent across all trigger types. The analysis advocates an equity-converting contingent convertible (CoCo) design and an explicit prohibition of write-offs[84] – for AT1 instruments under the contractual PLAM, and for both AT1 and Tier 2 at the PONV. Existing CET1 would be diluted through the conversion of these instruments into new CET1. Greater weight is placed on (i) stronger governance by AT1 holders anticipating a potential role as future shareholders, (ii) incentives for bank management to avoid a change of control, (iii) reduced wealth transfers from debt to equity – and the avoidance of windfall gains for CET1 holders – with any residual transfer governed by a pre-agreed conversion rate, and (iv) lower litigation risk by eschewing perceived one-sided write-offs that impose losses without upside. These advantages are assessed to outweigh concerns about operational complexity and potential shareholder resistance to dilution. Institutions that are not organised as stock corporations, or that cannot or do not wish to issue instruments convertible into CET1, should replace AT1 directly with CET1.

VI. Conclusion

This paper discusses the conflicts arising through loss-sharing by holders of CET1 instruments and those of AT1 and tier 2 instruments, under different scenarios. In the event of insufficient profits, distributions on AT1 instruments are not privileged over distributions on CET1 instruments. Rather, distributions on both types must be at the full discretion of the issuer. Additionally, amounts that are subject to a prohibition on distribution for CET1 instruments due to mandatory reserves under commercial and company law may not be distributed to holders of AT1 instruments. Tier 2 instruments are 'must-pay' obligations,

[84] Cf. Urs Lendermann, 'Automated Bail-in: Eliminating Regulatory Restraints' (2025) Journal of Banking Regulation <https://doi.org/10.1057/s41261-024-00266-7>.

while ‘reverse stoppers’ or *pari passu* clauses might cause an ‘infection’ risk on higher capital tiers.

Currently, the ranking of AT1 and CET1 instruments when the contractual trigger event occurs, namely reaching a CET1 RWA ratio of 5.125% or higher, is determined by the respective contractual terms and conditions. In the case of genuine CoCos, the conversion ratio determines the amount of the AT1 instrument’s initial liability participation. Write-offs are ranked below CET1 instruments, whereas temporary write-downs (with a subsequent write-up) can reach their original ranking before CET1 instruments in the event of a financial recovery. Tier 2 instruments shall not incorporate any contractual PLAM design that might change the seniority in resolution and insolvency.

However, in a realistic scenario, the institution would reach the PONV or become insolvent or default via other means, before the contractual PLAM trigger event is determined, and the capital instruments would necessarily be used to absorb loss by virtue of a statutory order from the resolution authorities. In a PONV event, Tier 2 should be held to be loss-absorbing, while at the same time, a gone-concern scenario shall be avoided. Under Union law, in a PONV scenario, and in resolution or insolvency proceedings, Tier 2 instruments should always be senior to AT1 instruments, and AT1 instruments should always take precedence over CET1 instruments.

This paper shows that the conflicts in loss sharing between holders of AT1 instruments and holders of CET1 instruments are regulated very differently in various scenarios. This makes risk assessment for rating agencies and investors, with regard to both AT1 and CET1 instruments, a challenge that is almost impossible to resolve.[85] Therefore, this study advocates

[85] Cf. European Securities and Markets Authority (ESMA) ‘Potential Risks Associated with Investing in Contingent Convertible’ ESMA/2014/944 (31 July 2014).

for any regulatory adjustments to the Tier 1 regulatory capital concept to first define the purpose of AT1 and Tier 2, and the relationship of each to CET1. The next crucial step would be to make the trigger event and the ranking of AT1 instruments more consistent, transparent, and simpler by promoting a CoCo design and explicitly prohibiting write-offs. A market trigger design, such as a share price trigger at the penny stock level, is also advocated for. Finally, finding Tier 2 instruments to be loss-absorbing at the PONV should not be considered an event of default and, in particular, it should not trigger early termination rights or any credit default swaps.

Appendix

Overview of Findings

SEQUENCE	INSTRUMENT, MEASURE	ORDER, PRIORITY, DEPENDENCY
OCCURRENCE OF LOSSES DURING ONGOING BUSINESS OPERATIONS	Distributions	**CET1 and AT1 instruments** Distributions on any of both capital instruments shall not be made dependent on each other to maintain **full flexibility**: • No *pari passu* clause • No dividend pushers • No dividend stoppers
		Tier 2 instruments 'Must-pay' obligations. In general, dividend pushers and dividend stoppers are allowed. However, reverse stoppers and *pari passu* clauses may cause infection risk on CET1 and AT1.
	Available distributable items (ADI) (applicable accounting standards, on solo entity basis)	**CET1 and AT1 instruments** (According to the opinion represented here): Amounts that are subject to a prohibition on distributions for CET1 instruments **shall not be distributed to holders of AT1 instruments** (unclear language of Art. 4 para. 1 No. 128 CRR).
		Tier 2 instruments Not applicable
	Maximum distributable amount (MDA) (combined buffer requirement, regulatory capital standards, on (sub) consolidated basis and on solo basis)	**CET1 and AT1 instruments** For distributions under the application of an MDA, **full flexibility** shall be warranted: • No *pari passu* • No prioritisation • No subordination
		Tier 2 instruments Not applicable

<table>
<tr><td rowspan="5">PRINCIPAL LOSS-ABSORBENCY MECHANISM (PLAM) ON A CONTRACTUAL TRIGGERING EVENT</td><td colspan="2">AT1 INSTRUMENTS</td></tr>
<tr><td>Contingent convertible bonds (CoCos)</td><td>Upon conversion into CET1 instruments, AT1 CoCos rank pari passu with CET1 instruments, with the conversion rate determining the extent of dilution</td></tr>
<tr><td>Permanent write-off bonds</td><td>Upon conversion into CET1 instruments, AT1 write-offs rank junior to CET1 instruments. This study advocates for prohibiting write-offs.</td></tr>
<tr><td>Temporary write-down bonds</td><td>Write-down: as write-offs, see before.
Write-up: considered as distributions (Art. 21 Del. Reg. (EU) No. 241/2014), therefore the following applies as above:
Independence and full flexibility
ADI
MDA
This study advocates for prohibiting temporary write-downs.</td></tr>
<tr><td colspan="2">TIER 2 INSTRUMENTS</td></tr>
<tr><td colspan="2">Incorporating contractual PLAM are neither required nor prohibited. However, EBA discourages their use, as it creates ‘infection’ risks for higher capital tiers.</td></tr>
<tr><td rowspan="2">POINT OF NON-VIABILITY (PONV)</td><td rowspan="2">Statutory loss-absorbing measures by the competent authority.
Trigger events:
a write-off, without which the firm would become non-viable, is necessary; or
a public sector injection of capital, or equivalent support, without which the firm would have become non-viable</td><td>AT1 instruments
Shall always rank senior to CET1 instruments according to:
Art. 21(10) SRMR,
Art. 60 BRRD, and
Art. 48(7) BRRD (For directives, the respective national adoption applies).</td></tr>
<tr><td>Tier 2 instruments
Though designed for gone-concern loss absorption, are deployed at PONV to preserve going-concern viability and should, as argued in this study, be expressly deemed not to trigger an event of default.
Shall rank senior to Tier 1 (AT1 and CET1) instruments according to the Union laws quoted above.</td></tr>
<tr><td rowspan="2">FAILING OR LIKELY TO FAIL (FOLTF), OR INSOLVENCY</td><td rowspan="2">bail-in in resolution
statutory insolvency and liquidation measures</td><td>AT1 instruments
Shall always rank senior to CET1 instruments.</td></tr>
<tr><td>Tier 2 instruments
Shall rank senior to Tier 1 (AT1 and CET1) instruments according to the same Union laws as quoted above.</td></tr>
</table>

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