28 November 2014

EBA/CP/2014/41

Consultation Paper

Draft Regulatory Technical Standards on criteria for determining the minimum requirement for own funds and eligible liabilities under Directive 2014/59/EU

Contents

1. Responding to this Consultation

The EBA invites comments on all proposals put forward in this paper and in particular on the specific questions summarised in 5.2.

Comments are most helpful if they:

- respond to the question stated;
- indicate the specific point to which a comment relates;
- contain a clear rationale;
- provide evidence to support the views expressed/ rationale proposed; and
- describe any alternative regulatory choices the EBA should consider.

Submission of responses

To submit your comments, click on the 'send your comments' button on the consultation page by 27.02.2015. Please note that comments submitted after this deadline, or submitted via other means may not be processed.

Publication of responses

Please clearly indicate in the consultation form if you wish your comments to be disclosed or to be treated as confidential. A confidential response may be requested from us in accordance with the EBA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the EBA's Board of Appeal and the European Ombudsman.

Data protection

The protection of individuals with regard to the processing of personal data by the EBA is based on Regulation (EC) N° 45/2001 of the European Parliament and of the Council of 18 December 2000 as implemented by the EBA in its implementing rules adopted by its Management Board. Further information on data protection can be found under the Legal notice section of the EBA website.

2. Executive Summary

Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms (the BRRD) provides a common resolution regime in the Union that allows authorities to deal with failing institutions as well as ensuring cooperation between home and host authorities. In the future, shareholders and creditors will have to internalise the burden of bank failure, minimizing moral hazard and risks to taxpayers.

To avoid institutions structuring their liabilities in a way that impedes the effectiveness of the bail-in or other resolution tools, and to avoid the risk of contagion or a bank run, the Directive requires that institutions meet at all times a robust minimum requirement for own funds and eligible liabilities (MREL). This is to be set on a case-by-case basis by resolution authorities, based on at least six common criteria set out in the BRRD.

These technical standards further specify these minimum criteria in order to achieve an appropriate degree of convergence in how they are applied and interpreted across Member States, and ensure that similar levels of MREL are set for institutions with similar risk profiles, resolvability, and other characteristics regardless of their domicile. Differences in the application of the criteria would result in similar banks facing different requirements and thus different costs of financing their activities.

Setting a level of MREL based on the minimum criteria also requires resolution authorities to assess matters which are also considered either in the calibration of prudential regulatory requirements or in the case-by-case judgements made by supervisory authorities, such as the degree of losses which institutions or groups should be able to absorb, or their risk profile, business model, and systemic importance. These technical standards therefore also seek to describe how these two sets of judgements should be related to each other.

The draft RTS first seeks to clarify how the resolution authority's assessment of the amount of MREL needed to absorb losses and, where necessary, recapitalise a firm after resolution, should be linked to the institution's going concern capital requirements. They provide that resolution authorities should, as a default, seek to rely on supervisory assessments of the degree of loss that a bank needs to be able to absorb and the capital it needs to operate.

In addition, resolution authorities should consider any additional MREL needed to successfully implement the resolution plan. In particular, where the resolution plan identifies that some liabilities would be unlikely to contribute to loss absorption or recapitalisation in resolution, resolution authorities may need to increase the MREL or take alternative measures. If the resolution authority considers that in resolution a contribution to the costs of resolution from the Deposit Guarantee Scheme would be possible, after considering the strict limits on such contributions, they may also take this into account in setting the MREL.

Lastly, the draft RTS proposes that for the assessment of systemic risk, resolution authorities should identify as systemic at least those institutions which are identified as Globally Systemically Important Institutions (G-SIIs) or Other Systemically Important Institutions (O-SIIs) for the purposes of the CRR/CRD IV. For systemic institutions, resolution authorities should consider the potential need to be able to access the resolution financing arrangement in the event that it is not possible to implement a resolution plan relying solely on the institution's own resources, and assess whether the MREL would be sufficient to enable the preconditions in the BRRD for access to these arrangements to be met.

The EBA expects these RTS to be compatible with the proposed FSB term sheet for Total Loss Absorbing Capacity (TLAC) for Globally Systemically Important Banks (G-SIBs). Where there are differences resulting from the nature of the EBA's mandate under the BRRD, as well as the fact that the BRRD MREL requirement applies to banks which are not G-SIBs, these differences do not prevent resolution authorities from implementing the MREL for G-SIBs consistently with the international framework.

3. Background and rationale

Section 1: The MREL provisions of the Bank Recovery and Resolution Directive

The recent financial crisis forced governments around the world to rescue banks. The subsequent impact on public finances as well as the undesirable incentive effects of socializing the costs of bank failure have underscored that a different approach is needed.

Significant steps have been taken to address the potential spill overs between banks and sovereigns, and thereby reduce the systemic risks of failing banks. Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms (the BRRD) provides a common resolution regime in the Union that allows authorities to deal with failing institutions as well as ensuring cooperation between home and host authorities. In the future, shareholders and creditors will have to bear the burden of bank failure, minimizing moral hazard and risks to taxpayers. Removing the implicit subsidy of large banks by governments will avoid the build-up of excessive risk and leverage within banks and the banking system as a whole.

To avoid institutions structuring their liabilities in a way that impedes the effectiveness of the bail-in or other resolution tools, and to avoid the risk of contagion or a bank run, the Directive requires that institutions meet at all times a robust minimum requirement for own funds and eligible liabilities (MREL) expressed as a percentage of the total liabilities and own funds of the institutions[1]. Hence, MREL should ensure that shareholders and creditors primarily bear losses in situations regardless of which resolution tool (e.g. the bail-in or bridge bank tools) is applied. In this way MREL ensures sufficient loss absorbing capacity that should enable an orderly resolution, ensuring continuity of critical functions without recourse to public funds.

According to Article 45(2), the EBA is mandated to develop draft regulatory technical standards to specify further the six criteria which resolution authorities are expected to apply when setting MREL. The EBA's work interacts considerably with the work of the Financial Stability Board ('FSB') to develop a related global standard on Total Loss Absorbing Capacity (TLAC) for globally systemically important banks (G-SIBs). The EBA aims to implement the MREL as required by the BRRD, and in a way that is consistent with the developing international framework, while ensuring proportionality in its application to institutions other than G-SIBs.

[1] See Recital 80 and Article 45 of Directive 2014/59/EU

Section 2: General approach

Article 45 of the BRRD provides for a case-by-case assessment of the MREL for each institution or group, against a minimum set of criteria described in Article 45, paragraph 6. The BRRD does not establish a common minimum MREL; while the impact assessment for the BRRD estimated the impact of the requirement on the assumption of a reference level of MREL of 10% of total liabilities, the actual level should be adapted to reflect the resolvability, risk profile, systemic importance and other characteristics of each institution.

These technical standards aim to further specify these minimum criteria in order to achieve an appropriate degree of convergence in how they are applied and interpreted across Member States, and ensure that similar levels of MREL can be set for institutions with similar risk profiles, resolvability, and other characteristics regardless of their domicile. Differences in the application of the criteria would result in similar banks facing different requirements and thus potentially different costs of financing their activities.

Setting a level of MREL based on the minimum criteria also requires resolution authorities to assess matters which are also considered either in the calibration of prudential regulatory requirements or in the case-by-case judgements made by supervisory authorities, such as the degree of losses which institutions or groups should be able to absorb, or their risk profile, business model, and systemic importance. These technical standards therefore also seek to describe how these two sets of judgements should be related to each other.

Resolution authorities also need to consider, when setting an appropriate MREL, the interaction with other conditions set by the BRRD, in particular for resolution planning and the requirements for use of the resolution fund to indirectly absorb losses.

Both CRR regulatory capital requirements and the BRRD preconditions for use of the resolution fund (in Article 44(5) and (8) of the BRRD) do establish common minimum requirements, whereas the BRRD does not establish a common minimum for MREL. The EBA is seeking comments on the requirement in the draft text for resolution authorities to assess whether systemically relevant banks respect conditions for accessing the resolution fund (i.e., have MREL al least equal to 8% of total liabilities), and will continue to consider whether and how this issue falls within the scope of the RTS. Comments from stakeholders are invited on whether the draft RTS strikes the appropriate balance between the need to adapt the MREL to the circumstances of individual institutions and promoting consistency across resolution authorities in the setting of adequate levels of MREL.

The EBA is additionally required to submit a report to the Commission by 31 October 2016 reviewing the implementation of MREL at national level and several aspects of the framework for MREL set out in the BRRD.

Section 3: Specific criteria

This section explains how the RTS specifies further the assessment criteria of Article 45(5).

3.1 Resolvability and capital adequacy

The first two criteria cater to the need to meet the resolution objectives when an institution is resolved using the resolution tools, including bail-in. The main means by which MREL contributes to ensuring that firms can be resolved in a way which meets resolution objectives is to ensure that there are enough own funds and eligible liabilities available to absorb losses and contribute to recapitalisation. This in turn will mean that extraordinary public financial support is not needed to absorb losses or contribute to recapitalisation, and the use of resolution funds is only required in extraordinary circumstances and when other preconditions in the BRRD are met. As such, it is proposed to further specify this criterion in the same way as the following criterion (relating to capital adequacy following bail-in), but noting that it applies to all resolution tools.

The capital adequacy criterion has two elements: loss absorption and recapitalisation. The RTS proposes how resolution authorities should assess the amount necessary for each.

The first is the need to ensure losses are absorbed. The regulatory capital requirements (both pillar 1 and 2) and buffers already reflect a judgement of the supervisor and regulatory community about the level of unexpected losses an institution should be able to absorb. It is therefore proposed that as a baseline the resolution authority should seek to ensure that losses equal to capital requirements (including buffers) can be absorbed. The EBA is seeking comment from stakeholders as to whether a) some components of capital requirements are not suitable for inclusion in this assessment of required loss absorbency and b) whether there are specific circumstances in which resolution authorities should assume that capital requirements are not fully consumed by losses in resolution.

Differences in judgement between the competent and resolution authority may be appropriate, but should be clearly reasoned. The draft RTS aims to avoid requiring the resolution authority needing to maintain the capacity to act as a 'shadow' supervisor. For this purpose, the resolution authority shall request from the competent authority a summary of the institutions capital requirements. Subsequently, the resolution authority may, if they wish, assess whether the information provided by the competent authority justifies an adjustment of the loss absorption amount. It may only do so in consultation with the competent authority and based on a reasoned explanation, referring as far as is feasible (given the information available to the resolution authority) to CRR/CRD IV and the guidelines adopted by the EBA pursuant to article 107 (3) of Directive 2013/36/EU for the supervisory review and evaluation of risks.

The resolution authority may additionally assess that a higher loss absorption amount is required if the resolvability assessment process concludes that this is necessary to reduce or remove an impediment to resolvability. Alternative benchmarks for determining the loss absorption amount have been considered, but are difficult to make workable and/or have already been considered in calibration of supervisory requirements. A notable example is historical loss experience. This has been already been considered in the course of the overall calibration of capital requirements in the CRR/CRD IV. Using historical loss experience to calibrate MREL on a case-by-case basis would require potentially inconsistent choices by resolution authorities about how to select a sample of historical loss episodes and the definition of loss. Estimating historical loss experience in a robust way which is consistent across Member States would therefore be challenging. In any case problems of data availability and quality may make identification of a sufficiently large sample difficult. Capital requirements provide a benchmark which is more likely to be applied consistently across institutions and Member States.

The second element of the capital adequacy criterion is for the resolution authority to determine the amount of recapitalisation which would be required to implement the preferred resolution strategy identified in the resolution planning process. This recapitalisation amount is only necessary for those institutions for which liquidation under normal insolvency processes is assessed not to be feasible and credible. Hence, for those banks that can be liquidated, the recapitalisation amount may be zero.

The recapitalisation criterion consists of two parts. The first creates a link between MREL and the capital ratio (including any leverage ratio requirement that has been applied) necessary to comply with conditions for authorisation for the institution after resolution. According to the CRR and CRD framework, the competent authority may withdraw the authorisation if an institution no longer meets the prudential requirements that it needs to satisfy at all times. This means that an institution, immediately after resolution, would have to comply, at a minimum, with the 8% total capital ratio requirement and any Pillar 2 capital requirement that the authorities have set (and potentially any leverage ratio requirement). Capital requirements are likely to need to be met through CET1 capital instruments only, at least in the immediate post-resolution period.

When estimating capital needs after implementation of the preferred resolution strategy, the resolution authority should as a starting point use as denominators for capital ratios the most recent reported values (for risk-weighted exposure amounts, and, if relevant, leverage exposure measures). Authorities may adjust these denominators if the resolution plan identifies, explains, and quantifies a change in these measures. This change should be assessed in the resolvability assessment process to be both feasible and credible, without extraordinary financial support or adversely affecting the provision of critical functions by the institution

The second part of the recapitalisation amount is to ensure sufficient market confidence in the institution. The draft RTS proposes that this should be assessed by considering how much is needed to restore the capital buffers established by CRD IV, and, for Globally Systemically Important Institutions, to reach similar capital levels to the firm’s peer group. Sustaining market confidence is likely to require that the institution is not operating under a capital conservation plan and so that capital buffers would need to be restored. The peer group approach takes the lesson learned during the crisis that market confidence is likely to depend on capital levels relative to peers. In addition, the proposed capital levels are also needed to avoid reliance on extraordinary public financial support, which resolution plans cannot assume. The EBA is seeking comment on whether a similar peer group approach is also appropriate for other types of institution.

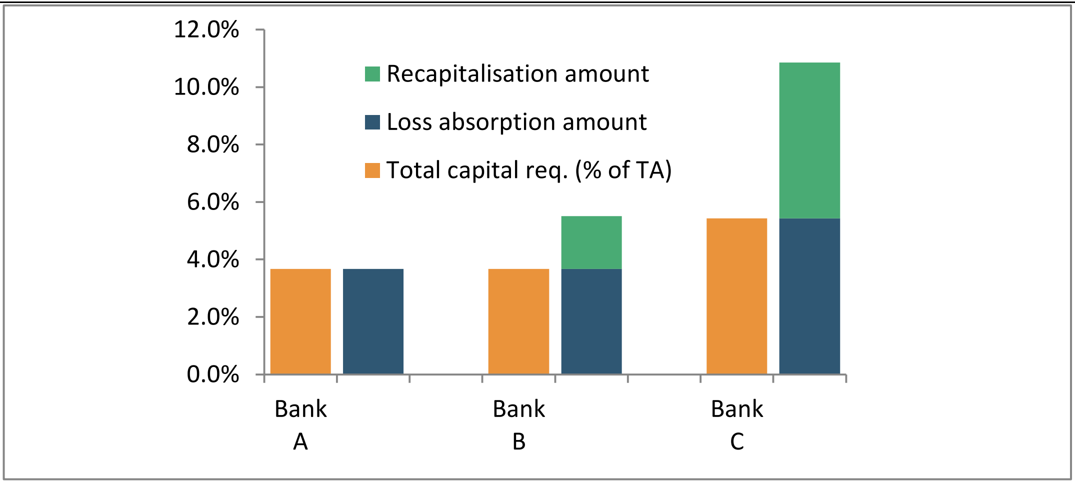
Box 1: Stylised examples of application of the capital and resolvability criteria

This box provides three examples of how resolution authorities might apply these criteria to simple hypothetical banks with different resolution plans. Note that these examples assume that the resolution authority relies wholly on the institutions' capital requirements to determine the required degree of loss absorbency and does not make any additional adjustments envisaged by the draft RTS on the basis of the resolvability assessment or other considerations.

Bank A is a small bank, assumed to have a minimum total capital requirement of 8% of RWAs and a combined buffer requirement of 2.5% (i.e. no pillar 2 or discretionary buffer requirements), and total RWAs equal to 35% of total liabilities and own funds. The resolvability assessment process concludes that it is both feasible and credible to liquidate the bank. The resolution authority therefore determines a loss absorption amount by translating the overall capital requirement of 10.5% of RWAs into the equivalent percentage of total liabilities and own funds – in this case, 3.7%. The recapitalisation amount is zero, as the bank would be liquidated.

Bank B is a medium-sized bank, again with an overall capital requirement of 10.5% and RWAs equal to 35% of total liabilities and own funds. The loss absorption amount determined by the resolution authority is therefore also 3.7% of total liabilities and own funds. However the resolution authority assesses that liquidation is not credible because the bank carries out some critical functions that need to be preserved. The resolution plan adopted is to transfer assets and liabilities associated with the critical functions to a bridge bank, and liquidate the remaining assets and liabilities. The planned bridge bank accounts for half of the RWAs of Bank B, so the resolution authority sets a recapitalisation amount of 1.8% of total liabilities and own funds. This gives a total MREL of 5.5%. If a leverage ratio requirement had been applied, this would also need to be considered and could lead to a higher level of MREL.

Bank C is a large, systemically important bank with a capital conservation buffer requirement of 2.5%, a G-SII buffer requirement of 2.5%, and a pillar 2 capital requirement of 2% of RWAs, giving an overall capital requirement of 15% of RWAs. Again RWAs are 35% of total liabilities and own funds. If the pillar 2 and G-SII buffers are included in the resolution authority's assessment of the required loss absorption amount, it would be 5.4% of total liabilities and own funds. The resolution authority determines that the only feasible and credible resolution strategy is a bail-in, and so resolution will not result in any immediate reduction in RWAs. The resolution authority therefore sets a recapitalisation amount also equal to 5.4% of total liabilities, and a total MREL of 10.8%. If a leverage ratio requirement had been applied, this would also need to be considered and could lead to a higher level of MREL.



3.2 Exclusions and deposit guarantee scheme contributions

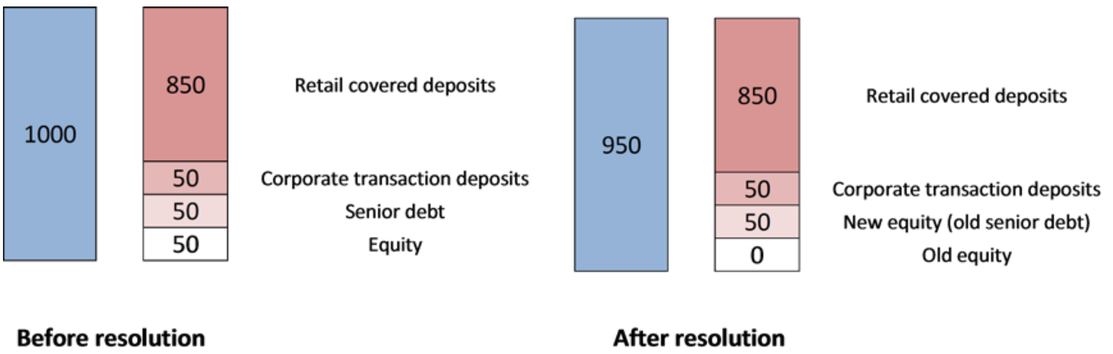
The third criterion is the need to ensure that the MREL is sufficient even if the resolution plan envisages that certain classes of liabilities are excluded from contributing to loss absorption or recapitalisation by the resolution authority in order to ensure a successful resolution. There are three ways in which such exclusions from loss might occur: in a bail-in, some liabilities are not eligible under Article 44(2) of the BRRD or resolution authorities may make use of their power under Article 44(3) of the BRRD to exclude some classes of liabilities on an ad-hoc basis, or they may be transferred in full under a partial transfer.

Bail-inable liabilities (i.e. those which meet the conditions for inclusion in the amount of own funds or eligible liabilities) may be excluded from loss in this way and so not able to contribute to the absorption of losses or recapitalisation. If this contingency is envisaged in the resolution plan the MREL needs to be increased to account for their exclusion.

Additionally, exclusion of liabilities from loss increases the amount of loss or recapitalisation which must be borne by other liabilities. If a sufficiently large amount of excluded liabilities rank equal to or junior to in insolvency any liabilities which are bailed in, this could result in holders of bailed-in liabilities receiving worse treatment than in insolvency, and so being eligible for compensation. The draft RTS proposes a principle that MREL should be set to avoid such a risk of compensation arising, but leaves the resolution authority to determine whether this is best done by increasing the MREL, requiring part of the MREL to be met through contractual bail-in instruments as permitted under Article 45(13) of the BRRD, or through alternative measures to remove impediments to resolvability.

Box 2: Stylised example of the impact of exclusions

A failing bank has assets of 1,000 (RWA of 500); equity of 50 (CET1 10%); senior debt of 50; large corporate transaction deposits of 50, that rank "pari passu" with senior debt; and 850 in preferred retail deposits. The resolution authority concludes that bailing in corporate transaction accounts would interrupt the operation of a critical function, and so they should excluded from bail-in under the resolution plan.



A loss of 50 would require writedown of all of the old equity. Conversion of 100% of the senior debt would, assuming the average risk weight of assets does not change, restore the CET1 capital ratio to 10.5%. If the economic value of the equity after resolution is 80% of book value, the economic loss to the former senior creditors would be 10.

Under insolvency, half of this loss would have been borne by the corporate transaction deposits. If the ex post insolvency valuation concludes that total losses in insolvency would have been 70 or less, then senior debt holders would be worse off than in insolvency. To reduce this, the MREL requirement could be raised (provided this is met through liabilities which can be feasible and credibly bailed in) or part of the MREL requirement could be met through subordinated bail-in able liabilities, in both cases increasing the proportion of losses in insolvency that are borne by MREL holders.

The fourth criterion requires the resolution authority to take account of the extent to which the Deposit Guarantee Scheme could contribute to the financing of resolution in accordance with Article 109 of the BRRD. Article 109 permits the use of deposit guarantee funds in resolution, but limits their contribution to the lesser of a) the amount of losses covered depositors would have borne in insolvency, or b) 50% (or a higher percentage set by the member state) of the target level of the deposit guarantee fund. The RTS proposes that resolution authorities should be required to set MREL to ensure that these limits would be respected if losses equal to the amount determined for purposes of the first criteria were incurred.

Additionally, for institutions for which the resolvability assessment process concludes that liquidation under normal insolvency processes is both feasible and credible, the RTS proposes that resolution authorities may reduce the MREL to take account of the estimated contribution from the DGS.

3.3 Risks and systemic risks

The fifth criterion requires resolution authorities to take account of the size, business model, funding model, and risk profile of the institution. As noted above, these factors also affect the setting of prudential requirements for the institution, and in particular the Supervisory Review and Evaluation Process (SREP). In order to ensure that any differences of judgement between the supervisory and resolution authorities are clearly articulated and discussed, and to avoid unnecessary duplication of resources between authorities, resolution authorities are required to request a summary of these factors from the competent supervisory authority, and how risks arising from them are mitigated by capital requirements or other supervisory risk mitigants. Subsequently, the resolution authority may assess whether these factors are adequately addressed by these mitigants, or by measures adopted to remove or reduce impediments to resolvability. If it assesses that this is not the case, the resolution authority may adjust the MREL. It may only do so in consultation with the competent authority and based on a reasoned explanation, referring as far as possible to the CRR/CRD IV and any guidelines adopted by the EBA pursuant to article 107 (3) of Directive 2013/36/EU adopted by the competent authority for the supervisory review and evaluation of risks.

The sixth and final criterion requires resolution authorities to take account of the potential adverse effects on financial stability of the failure of the institution. The draft RTS proposes that the resolution authority should identify institutions whose failure is reasonably likely to pose systemic risk, including at least any Globally Systemically Important Institutions (G-SIIs) or Other Systemically Important Institutions (O-SIIs) identified pursuant to the CRD. For these institutions MREL should continue be set to ensure that the first five criteria are adequately addressed.

But in addition, given the high potential social costs of their failure, it is important to ensure that additional funding from the resolution financing arrangements established pursuant to the BRRD is also available if needed. Resolution authorities are therefore required to assess whether the level of MREL is sufficient to ensure that the conditions for use of the resolution fund described in Article 44 of the BRRD could be met. That article requires that a contribution to loss absorption and recapitalisation of not less than 8% of the total liabilities including own funds of the institution (or, under certain conditions, 20% of risk-weighted assets) has been made by the holders of relevant capital instruments and other eligible liabilities.

Lastly, the RTS propose that the resolution authority should, in assessing an institution or group against these criteria, consider the appropriate timetable for institution to meet the MREL and provide the institution with a planned MREL for each 12 month period during this transitional period. This planned level may however be revised subsequently.

Section 4: Comparison with FSB proposals

The EBA expects these RTS to be compatible with the proposed FSB term sheet for Total Loss Absorbing Capacity (TLAC) for Globally Systemically Important Banks (G-SIBs). While there are differences resulting from the nature of the EBA's mandate under the BRRD, as well as the fact that the BRRD MREL requirement applies to banks which are not G-SIBs, these differences do not prevent resolution authorities from implementing the MREL for G-SIBs consistently with the international framework. Below is a summary of some of the differences between the BRRD MREL framework and the FSB proposals:

1. **Pillar 1, Pillar 2 and capital buffers.** The FSB term sheet proposes a predetermined pillar 1 minimum TLAC requirement of between 16% and 20% of risk-weighted assets (RWAs), and an additional, discretionary, pillar 2 TLAC requirement set on a bank by bank basis. Basel III capital buffers must be met on top of the TLAC requirements. The BRRD requires MREL to be set on a case by case basis, and does not include a common minimum requirement. Accordingly, if resolution authorities choose to aim to meet the FSB standards, this should be consistent with setting a single MREL requirement which covers both the pillar 1 and pillar 2 components of the proposed TLAC term sheet.

2. **Eligibility of instruments.** The FSB term sheet sets a number of requirements for instruments to be eligible for TLAC (e.g. subordination), some of which differ from the criteria to be counted towards MREL in the BRRD. Eligibility of instruments is set by the BRRD and is outside the scope of this RTS. However the BRRD and the draft RTS do require resolution authorities to take into account the risk of exclusions from bail-in, and the need for the institution to be feasibly and credibly resolvable.

3. **Implementation date.** The FSB proposes a lag before implementation of TLAC (not before 1 Jan 2019), whereas the requirement to set MREL applies from the date of national implementation of Article 45 of the BRRD (i.e. 1 Jan 2016 at the latest). However the approach adopted in the draft RTS would not prevent resolution authorities from setting an MREL requirement which increases over time to reflect the need for an adequate transition period.

4. **Denominator.** The FSB pillar 1 requirement is set as a percentage of RWAs (or, if the leverage ratio backstop binds, of the leverage ratio exposure measure). The BRRD requires the MREL to be set as a percentage of own funds and total liabilities (after full recognition of counterparty netting rights). The draft RTS enables resolution authorities to consider RWA-based capital requirements or leverage ratio requirements when setting MREL, but the final requirement must be set as a percentage of own funds and total liabilities.

5. **Other differences in scope.** The TLAC proposal of the FSB also addresses a number of other issues which are outside the scope of these RTS, including the prudential treatment of holdings of TLAC instruments and a requirement for a minimum percentage of TLAC to consist of non-capital instruments.

4. Draft regulatory TS on criteria for determining the minimum requirement for own funds and eligible liabilities

COMMISSION DELEGATED REGULATION (EU) No …/..

supplementing Directive xx/XX/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodology for assessing the value of assets and liabilities of institutions or entities referred to in points (b), (c) or (d) of Article 1(1)

of xx.x.2014

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to 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[2], and in particular article 45(2) thereof.

Whereas:

(1) Effective resolution can only be feasible and credible if adequate internal financial resources are available to an institution to absorb losses and for recapitalisation purposes without affecting certain liabilities, in particular those excluded from bail-in. To avoid that institutions excessively resort to a form of funding that is excluded from bail-in, which would impinge on the institution's loss absorption and recapitalisation capacity and utlimately on the overall effectiveness of resolution, Directive 2014/59/EU provides that institutions should meet a minimum requirement for own funds and eligible liabilities ('MREL').

(2) According to the Directive above the MREL should be set by resolution authorities, in consultation with the competent authority, on a case-by-case basis. In order to promote a uniform approach across the Union ensuring that resolution authorities set similar requirements for similar institutions, the Directive requires that the minimum requirement is set on the basis of at least a number of common criteria, to be further specified by the EBA.

(3) According to the Directive, when determining MREL, the resolution authority should consider the need, in case of application of the bail-in tool, to ensure that the institution

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is capable of absorbing losses and having its Common Equity Tier 1 ratio restored to a level sufficent to meet the capital requirements for authorisation and at the same time to sustain sufficient market confidence. The close relationship with supervisory decisions requires that such assessments are elaborated by the resolution authority in close consultation with the competent authorities as required by the Directive. In particular, the assessment of the necessary capacity to absorb losses should be closely linked to the institution's current capital requirements, and the assessment of the necessary capacity to restore capital should be closely linked to likely capital requirements after application of the resolution strategy, unless there are clear reasons which justify differences in assessment. The same kind of assessement should be carried out when the resolution authority determines the minimum requirements to ensure the resolvability of an insitution when resolution tools other than bail-in are applied.

(4) Resolution authorities should also consider the possibility that certain classes of liabilities, to be identified in resolution plans and in the resolvability assessment, might be excluded from bail-in and therefore should not be taken into account for purposes of meeting the MREL. Resolution authorities should also ensure that when significant amounts of any insolvency class of liabilities are excluded from bail-in, this exclusion would not result in liabilities of the same or a more senior class bearing greater losses than they would in insolvency. Resolution authorities can achieve this result by requiring part of the minimum requirement to be met in subordinated contractual bail-in instruments, or by setting a higher minimum requirement, or by alternative measures to address impediments to resolution.

(5) Resolution authorities should assess the potential size of contributions to the cost of resolution from the deposit guarantee scheme by determining whether exhausting the required capacity to absorb losses as determined by the resolution authority would be sufficient to writedown all liabilities which are junior in insolvency to covered deposits. If this assessment reveals the likelihood of such a contribution, resolution authorities may opt to set a lower minimum requirement.

(6) In order to ensure supervisory consistency the resolution authority's assessment of the size, business model, funding model, and risk profile of the institution should be closely linked to that carried out by the competent authority unless clear reasons justify a different assessment.

(7) Resolution authorities should consider the potential adverse impact of the failure of an institution failure on financial stability. In the case of systemically important institutions, resolution authorities should pay particular attention to ensuring that in case resolution costs exceed the resolution authority's assessment of the amount of loss absorption and recapitalisation required, resolution financing arrangments are able if necessary to contribute to the full range of costs of resolution while respecting the conditions set out in Directive 2014/59/EU. This would require in particular that the holders of the institution's capital instruments and other eligible liabilites, at the time of resolution and after absorbing any losses before that time, should be capable of contributing to loss absorption and recapitalisation an amount at least equal to 8% of the total liabilities including own funds. This should not however result in any reduction or replacement of the need to ensure sufficient loss absorption and

recapitalisation capacity through writedown and conversion of eligible liabilities, or imply that use of the resolution financing arrangement should be assumed as part of a resolution plan.

(10) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority to the Commission.

(11) The European Banking Authority has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with article 37 of Regulation (EU) No 1093/2010.

HAS ADOPTED THIS REGULATION:

PART I

GENERAL PROVISIONS

Article 1

Definitions

For the purposes of this Regulation the following definitions apply:

(a) 'preferred resolution strategy' shall mean the preferred resolution strategy identified pursuant to Article 3 paragraph 3 of the [EBA Technical Standards on the contents of resolution plans and the assessment of resolvability].
(b) 'capital requirements' shall be defined in accordance with the transitional provisions laid down in Part Ten of Regulation (EU) nº 575/2013 and national legislation exercising the options granted for competent authorities in that Regulation.
(c) 'Qualifying eligible liabilities' means eligible liabilities which satisfy the conditions in Article 45(4) of Directive 2014/59/EU necessary to be included in the amount of own funds and eligible liabilities referred to in Article 45(1).

PART II

RESOLVABILITY AND CAPITAL CRITERIA

Article 2

Determining the amount necessary to ensure loss absorption

1. Resolution authorities shall determine the amount of loss which the institution should be capable of absorbing in and before resolution ('loss absorption amount').
2. For the purpose of of determining the loss absorption amount in accordance with this Article and of the contribution of the deposit guarantee scheme to the resolution costs pursuant to Article 4, the resolution authority shall, consistently with Article 45(6) of Directive 2014/59/EU, request from the competent authority a summary of the capital requirements applicable to an institution, in particular:
    a. own funds requirements pursuant to Article 92 and 458 of Regulation (EU) No 575/2013, which include:
        i. CET1 capital ratio of 4.5% of the total risk exposure amount;
        ii. a Tier 1 capital ratio of 6% of the total risk exposure amount;
        iii. a total capital ratio of 8% of the total risk exposure amount;

b. any requirement to hold own funds in excess of these requirements pursuant to Article 104(1) letter (a) of Directive 2013/36/EU;
c. combined buffer requirements as defined in point 6 of paragraph 1 of Article 128 of Directive 2013/36/EU;
d. the Basel I floor according to article 500 of Regulation (EU) No 575/2013;
e. any leverage ratio requirement

Question 1

The draft text above describes comprehensively capital requirements under the CRR/CRD IV framework, which includes minimum CET1, AT1 and total capital requirements, capital buffers required by CRD IV, Pillar 2 capital requirements set on a case-by-case basis, and backstop capital measures (Basel I floor and leverage ratio). The EBA is seeking comments on whether all elements of these capital requirements should be considered for the assessment of the loss absorption amount. Do you consider that any of these components of the overall capital requirement (other than the minimum CET1 requirement) are not appropriate indicators of loss in resolution, and if so why?

3. The default loss absorption amount determined by the resolution authority shall be the sum of the requirements referred to in paragraph 2, letters (a), (b) and (c), or any higher amount necessary to comply with the requirements referred to in paragraph 2 letters (d) or (e).

4. The resolution authority may assess whether the need for loss absorption in resolution is adequately reflected in the institution's capital requirements, taking into account the assessment of business model, funding model, and risk profile pursuant to Article 6.
5. If the resolution authority assesses that the need for loss absorption is not adequately reflected in the institution's capital requirements, the resolution authority may adjust the loss absorption amount. The resolution authority shall provide the competent authority with a reasoned explanation of any such assessment, making reference where appropriate to Regulation 575/2013/EU and Directive 36/2013/EU and any guidelines adopted by the EBA pursuant to article 107 (3) of Directive 2013/36/EU for the supervisory review and evaluation process.

Question 2

Should paragraph 5 refer only to the resolution authority *increasing* the loss absorption amount, rather than *adjusting* it? Are there specific circumstances under which resolution authorities should allow a smaller need to be able to absorb losses before entry into resolution and in the resolution process than indicated by the capital requirements (for example, due to the use of national discretions in setting capital requirements)?

6. The resolution authority may determine that a higher loss absorption amount is required if the resolvability assessment concludes that this is necessary to reduce or remove an impediment to resolvability.

Question 3
Should any additional benchmarks be used to assess the necessary degree of loss absorbency? If yes, how should these be defined and how should they be used in combination with the capital requirements benchmark? Should such benchmarks also allow for a decrease of the loss absorption amount compared to the institution’s capital requirements?

Article 3

Determination of the amount necessary to continue comply with conditions for authorisation and to carry out activities and sustain market confidence in the institution

1. Resolution authorities shall determine an amount of recapitalisation which would be necessary to implement the preferred resolution strategy identified in the resolution planning process (recapitalisation amount).
2. If the resolvability assessment concludes that liquidation of the institution under normal insolvency processes is feasible and credible, and no alternative preferred resolution strategy is identified, the recapitalisation amount determined shall be zero, unless the resolution authority determines that a positive amount is necessary on grounds that liquidation would not achieve the resolution objectives in all circumstances.
3. When estimating regulatory capital needs after implementation of the preferred resolution strategy, the resolution authority shall use the most recent reported values for the relevant capital ratio denominator, unless all of the following circumstances are met:

a. the resolution plan identifies, explains, and quantifies a change in the denominator; and

b. the above change is considered in the resolvability assessment to be both feasible and credible without adversely affecting the provision of critical functions by the institutio, and without recourse to extraordinary financial support other than contributions from resolution financing arrangements consistent with Article 101 (2) and the principles governing use of the resolution financing arrangement set out in Article 44 of Directive 2014/59/EU; and

c. for systemic institutions identified pursuant to Article 7(1), that the conditions provided in Article 7 paragraph (3) are met

4. The resolution authority shall identify, explain and quantify any such changes. In particular where such changes are dependent on the actions of a purchaser of assets or business lines of the institution under resolution, or of other third parties, the resolution authority shall prepare a reasoned explanation of the feasibility and credibility of this change.

5. The recapitalisation amount shall be at least equal to the capital requirements necessary to comply with the conditions for authorisation after the implementation of the preferred resolution strategy.

6. The capital requirements referred to in paragraph 5 are in particular the following:

   a. own funds requirements pursuant to Articles 92 and 458 of Regulation (EU) No 575/2013, which include:

      - a CET1 capital ratio of 4.5% of the total risk exposure amount
      - a Tier 1 capital ratio of 6% of the total risk exposure amount
      - a total capital ratio of 8% of the total risk exposure amount

   b. any requirement to hold own funds in excess of these requirements pursuant to Article 104(1) letter (a) of Directive 2013/36/EU

   c. the Basel I floor according to article 500 of Regulation 575/2013/EU.

   d. any leverage ratio requirement

7. The recapitalisation amount shall also include any additional amount that the resolution authority considers necessary to maintain sufficient market confidence after resolution. This additional amount shall be at least equal to the higher of:

   a. the combined buffer requirement as specified in Chapter 4, Section 1 of Directive 2013/36/EU which would apply to the institution after the application of resolution tools; or

   b. in case the institution is a Globally Systemically Important Institution (G-SII), the amount necessary to make the CET1 capital ratio of the institution after application of resolution tools at least equal to the median of the CET1 capital ratio of a peer group consisting of all designated G-SIIs established in the Union.

Question 4

Do you consider that any of these components of the overall capital requirement are not appropriate indicators of the capital required after resolution, and if so why?

Question 5

Is it appropriate to have a single peer group of G-SIIs, or should this be subdivided by the level of the G-SII capital buffer?

Should the peer group approach be extended to Other Systemically Important Institutions (O-SIIs), at the option of resolution authorities? If yes, would the appropriate peer group be the group of O-SIIs established in the same jurisdiction?

Should the peer group approach be further extended to other types of institution?

Question 6

The approach outlined in Articles 2 and 3 will reflect differences between consolidated and subsidiary capital requirements. Are there additional ways in which specific features of subsidiaries within a banking group should be reflected?

8. If the assets, liabilities, or business lines of the institution would be split between more than one entity following implementation of the preferred resolution strategy, references to risk exposure amounts and capital requirements in this Article should be understood as the aggregate amounts across these entities.

PART III

DEPOSIT GUARANTEE SCHEME CONTRIBUTION AND EXCLUSION CRITERIA

Article 4

Contributions by the deposit guarantee scheme to the financing of resolution

1. The resolution authority shall determine an estimate of the potential losses to the deposit guarantee scheme if the institution were liquidated under normal

insolvency proceedings. This potential contribution from the deposit guarantee shall be considered to be the loss absorption amount less the sum of liabilities which rank junior to covered deposits in insolvency, namely:

a. the institution's own funds and eligible liabilities;
b. any other outstanding subordinated liability
c. any ordinary unsecured, non-preferred liability
d. any liability which is not excluded from bail in pursuant to article 44 (2) of Directive 2014/59/EU,
e. any deposits which meet the conditions set out in letter (a) of Article 108 of Directive 2014/59/EU
f. any other liability which ranks lower in the creditor hierarchy than deposits covered by the deposit guarantee scheme.

2. The resolution authority shall ensure that the MREL is set at a sufficient level to ensure that, if met, the estimated contribution would be lower than 50% of the target level of the deposit guarantee scheme pursuant to Article 10 of Directive 2014/49/EU, or another percentage as determined by a Member State pursuant to Article 109(5) of Directive 2014/59/EU.
3. When the resolvability assessment concludes that liquidation of an institution under normal insolvency proceedings would be feasible and credible, the resolution authority may reduce the MREL in order to take into account any estimated contribution.
4. Any reduction in MREL determined by the resolution authority pursuant to paragraph 3 shall take into account the overall risk of exhausting the available financial means of the deposit guarantee scheme. The resolution authority shall document how this element has been given consideration and any reductions made pursuant to paragraph 3.

Article 5

Exclusions from bail-in or partial transfer

1. The resolution authority shall identify any class of liability which are reasonably likely to be fully or partially excluded from bail-in under Article 44 (2) or (3) of Directive 2014/59/EU, or transferred to a recipient in full using other resolution tools based on the resolution plan.
2. If any liability which qualifies for inclusion in MREL is identified as being potentially fully or partially excluded pursuant to paragraph 1, the resolution authority shall ensure that the MREL is sufficient to absorb the loss amount determined pursuant to Article 1 and achieve the amount of recapitalisation determined Pursuant to article 2 without writedown or conversion of these liabilities.
3. If any liability is identified in accordance with paragraph 1 and:

a. rank equally to or junior to any class of liability which qualifies for inclusion in MREL; and

b. the amount of liabilities identified totals more than [10%] of any one class of liabilities which ranks equally in insolvency;

the resolution authority shall estimate the amount of the loss absorption amount and of the recapitalisation amount would be borne by these liabilties should they not be excluded.

Question 7

Do you agree that there should be a *de minimis* derogation from this provision for excluded liabilities which account for less than 10% of a given insolvency class?

4. The resolution authority shall assess whether the MREL is sufficient to ensure that the amount identified pursuant to paragraph 3 can be absorbed by instruments which (i) qualify for inclusion in MREL and (ii) are not excluded from loss absorption or recapitalisation, without breaching the creditor safeguards provided in Article 73 of Directive 2014/59/EU (the NCWO safeguard).

5. The resolution authority shall document any assumptions, valuations, or other information used to determine that the MREL meets the conditions set out in paragraph 4

PART IV

RISK AND SYSTEMIC RISK

Article 6

Business model, funding model, and risk profile

1. The resolution authority shall request from the competent authority, as part of the consultaiton required by Article 45 (6) of Directive 2014/59/EU, a summary and explanation of the outcomes of the supervisory review and evaluation process conducted pursuant to Article 97 of Directive 2013/36/EU and taking into account Guidelines adopted pursuant to Article 109 of that Directive, and in particular:

   a. A summary of the assessment of each of the business model, funding model, and overall risk profile of the institution

   b. A summary of the assessment of whether capital and liquidity held by an institution ensure sound coverage of the risks to which the institution is or might be exposed;

   c. Information on how risks and vulnerabilities identified in the supervisory review and evaluation process are reflected, directly or indirectly, in the additional own fund requirements applied to an the institution pursuant to letter (a) of paragraph 1 of Article 10 of Directive 2013/36/EU based on the outcomes of the supervisory review and evaluation process.

   d. Information on other supervisory measures and powers pursuant to Articl 102 and letters (b) to (l) of paragraph (1) of Article 104 of Directive 2013/36/EU applied to an institution to address risks and vulnerabilities identified inthe supervisory review and evaluation process

2. The resolution authority may assess whether these risks and vulnerabilities are adequately reflected in the capital requirements, addressed by other supervisory measures, or by measures to remove impediments to resolvability pursuant to Articles 17 or18 of Directive 2014/59/EU.
3. If the resolution authority assesses that they are not adequately reflected or addressed, it should adjust the MREL. The resolution authority shall provide the competent authority with a reasoned explanation of any such assessment, taking into account where appropriate any EBA guidelines adopted pursuant to Article 107 (3) of Directive 2013/36/EU.

Article 7

Size and systemic risk

1. For institutions and groups which have been designated as G-SIIs or O-SIIs by the relevant competent authorities, and for any other institution which the competent authority or the resolution authority considers reasonably likely to pose a systemic risk in case of failure, the resolution authority shall assess whether the MREL is sufficient to permit the requirements set out in Article 44 of Directive 2014/59/EU governing a contribution to loss absorption by the resolution financing arrangement to be met. In this regard, consideration shall be given in particular to the requirement that in resolution a minimum contribution to loss absorption and recapitalisation of 8% of total liabilities and own funds, or of 20% of the total risk exposure amount if additional conditions under paragraph 8 of Article 44 of Directive 2014/59/EU are met, is made by shareholders and holders of capital instruments and eligible liabilities at the time of resolution.
2. Resolution authorities may choose not to assess whether the MREL meets the condition of paragraph 1 if the resolvability assessment concludes that:
   a. there are no impediments to a feasible and credible resolution without a contribution to loss absorption from the resolution financing arrangement; and
   b. there are no plausible circumstances in which a contribution from the resolution financing arrangement would be necessary to avoid a breach of the safeguards provided in Title IV Chapter VII of Directive 2014/59/EU; and
   c. the preferred resolution strategy assumes that losses are absorbed only by

liabilities which meet the conditions of Article 45(4) of Directive 2014/59/EU and are assessed as feasibly and credibly able to contribute to loss absorption.

3. For institutions and groups which have been designated as G-SIIs or O-SIIs by the relevant competent authorities, and for any other institution which the competent authority or the resolution authority considers reasonably likely to pose a systemic risk in case of failure, downwards adjustments to estimated capital requirements after resolution for regulatory capital ratios pursuant to Article 3(3) shall only be applied if the conditions of paragraph 2 are met. Where a joint decision on MREL by a resolution college is required pursuant to Article 45 of Directive 2014/59/EU, any such adjustment shall be documented and explained in the information provided to members of the resolution college.

Question 8

Do you agree that resolution authorities should seek to ensure that systemic institutions have sufficient MREL to make it possible to access resolution funds for the full range of financing purposes specified in the BRRD?

PART V

AGGREGATION AND TRANSITION

Article 8

Combined assessment of MREL

1. Resolution authorities shall ensure that MREL is sufficient to allow the writedown or conversion of an amount of own funds and qualifying eligible liabilities at least equal to the sum of loss absorption amount and the recapitalisation amount as determined by resolution authorities following Articles 2 and 3, and to meet the other requirements provided for in this Regulation.
2. Resolution authorities shall express the calculated MREL as a percentage of total liabilities and own funds of the institution.

Article 9

Transitional arrangements

1. By way of derogation from Article 8, resolution authorities may determine a lower level of MREL to enable an appropriate transitional period.

2. For the purposes of paragraph (1), resolution authorities shall determine an appropriate transitional period and communicate to the institution a planned MREL for each 12 month period during the transitional period. At the end of the transitional period, the final MREL shall be equal to the amount determined under Article 8. This shall not prevent resolution authorities from subsequently revising either the transitional period or any planned MREL.
3. The transitional period shall not be longer than 48 months

Question 9:

Is this limit on the transition period appropriate?

Question 10:

Should the resolution authority also set a transitional period for the MREL of banks which are undergoing or have undergone a resolution process?

Question 11:

Overall, do you consider that the draft RTS strikes the appropriate balance between the need to adapt the MREL to the circumstances of individual institutions and promoting consistency in the setting of adequate levels of MREL across resolution authorities?

Article 10

Final provisions

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Commission
The President

[For the Commission
On behalf of the President

[Position]

5. Accompanying documents

5.1 Draft Cost- Benefit Analysis / Impact Assessment

Introduction

Article 45(2)of Directive 2014/59/EU mandates the EBA to develop draft RTS to specify further the criteria which resolution authorities are expected to apply when setting MREL.

As per Article 10(1) of the EBA regulation (Regulation (EU) No 1093/2010 of the European Parliament and of the Council), any draft RTS developed by the EBA shall be accompanied by a cost and benefit analysis. Such annex shall provide the reader with an overview of the findings as regards the problem identification, the options identified to remove the problem and their potential impacts.

This annex presents a draft assessment of the issues which will be considered by the EBA in its final impact assessment. The EBA will continue to refine its assessment of these issues before finalising a draft RTS for submission to the Commission. In particular, we intend to undertake further data collection to permit a more detailed assessment of the possible quantitative impact on institutions.

Question 12:

Are there additional issues, not identified in this section, which should be considered in the final impact assessment?

Policy background and problem identification

As described in the main body of the consultation paper, Directive 2014/59/EU (the BRRD) provides a framework of resolution powers that is intended to make sure that institutions themselves, along with their shareholders, creditors, and other stakeholders, bear the costs of bank failure. But in the interests of preserving financial stability and the continuity of the critical economic functions of institutions, certain types of liability are excluded from the scope of application of the bail-in tool or are otherwise protected from absorbing losses in resolution. This creates a potential incentive for institutions to seek to raise a greater proportion of their funding from these classes of liabilities. To guard against this the BRRD requires institutions to maintain at all times a minimum amount of own funds and other liabilities which are a) within the scope of the bail-in tool and b) meet certain other criteria specified in Article 48.

This minimum requirement for own funds and eligible liabilities (MREL) must be set by resolution authorities on a case-by-case basis. The case-by-case assessment allows for the MREL to take account of the specific features of each institution, but to ensure a sufficient degree of harmonisation across the Union the BRRD requires resolution authorities to set the MREL on the basis of six common criteria, and for these criteria to be further specified in technical standards developed by the EBA. This draft impact assessment therefore does not seek to assess the impact of introducing an MREL requirement, as this has already been done in the BRRD. Instead it seeks to identify the marginal impact of different approaches which could be taken to developing these technical standards.

Baseline

There are two major challenges in establishing a baseline for assessing the impact of these Technical Standards, which arise because the requirement to set an MREL is a new requirement introduced by the BRRD. Member States do not currently set similar requirements and so a) do not systematically collect data on the amount of outstanding liabilities which satisfy the criteria for inclusion in MREL; and b) have no established practices for setting requirements against which to compare the impact of the RTS.

Objectives

The general objective of these Technical Standards is to ensure that the MREL provisions of the BRRD operate effectively to ensure that institutions can be resolved in a way that meets the resolution objectives.

The specific objectives of the RTS are to:

1. Enable similar MREL requirements to be set for institutions with similar risk profiles, resolvability, and other characteristics regardless of their domicile. ;

2. Provide sufficient scope to take into account the specific characteristics of different institutions, and in particular to ensure that the principle of proportionality is respected;

3. Enable, as far as is consistent with the aims and text of the BRRD, requirements to be set for G-SIIs which are consistent with the FSB's TLAC proposals.

Policy options

Determination of loss absorption and recapitalisation amounts, and assessment of risk profile, funding profile and business model.

1. ***Loss absorption and risk assessments***

Option 1: Option 1 would be for an independent assessment to be performed by the resolution authority to determine a) the required degree of loss absorption; b) the business model, funding and risk profile of the resolved entity.

Option 2: Option 2 would require that the resolution authority takes the supervisory authorities' assessments, as expressed in a) capital requirements as a measure of required loss absorbency and b) supervisory review assessments as regards business model, risk profile, and funding model as a starting point, and provides a reasoned explanation of any departures from these.

Area	Policy options	Pros	Cons
1. **Relationship between resolution authority and competent authority assessments**	Option 1: Independent assessment to be performed by the resolution authority	• Enables resolution authority to consider factors other than capital requirements (e.g. historical loss experience) • Permits full independence of resolution authority judgement	• Increases potential for conflict and possible regulatory arbitrage between supervisor and resolution authority • Unclear how to constrain this discretion other than by replicating supervisory standards • Resource cost of maintaining capacity to perform analysis
	Option 2: Competent authority assessment as default	• Promotes coherence between supervisory and resolution authority assessments • Optional for resolution authority to maintain additional analytical capacity • Consultation with competent authority required by level 1 • Provides framework for	• Requires good communication between competent and resolution authorities • 'Soft' limit on independence of resolution authority judgement

		discussion between competent and resolution authorities	

Preferred option: Option 2 is preferred to Option 1, provided that option 2 is implemented in a way which is consistent with the BRRD provision for resolution authorities to retain the final say on setting of MREL.

2. *Extent of recapitalisation to maintain sufficient market confidence*

Option 1: The level of CET1 capital after resolution would be benchmarked to the CET1 levels of peer institutions.

Option 2: The level of CET1 capital after resolution should be at least sufficient to meet anticipated capital buffer requirements, after allowing for any estimated reductions in capital requirements due to the resolution.

Option 3: The level of CET1 capital after resolution should be at least sufficient to meet anticipated capital buffer requirements, after allowing for any estimated reductions in capital requirements due to the resolution *and* the post-resolution business reorganisation.

Area	Policy options	Pros	Cons
1. Extent of recapitalisation to maintain sufficient market confidence	Option 1 : CET1 capital after resolution should be benchmarked to the CET1 levels of peer institutions	• Easy to implement (data would be directly available through the peer review). • Simple and straight forward approach that would ensure maximum transparency • Crisis experience indicates confidence does depend on peer comparisons • No additional cost.	• Static approach (does not take into account the outcome of the resolution as well banks' specific developments) • Not tailored and does not consider bank's specific risks.

	Option 2: CET1 capital after resolution should be at least sufficient to meet anticipated capital buffer requirements, after allowing for any estimated reductions in capital requirements due to the resolution.	• More forward looking approach than option 1 as it would consider the up to date situation of the institution when determining capital needed.	• More costly and time consuming than option 1 as it would require the competent authority or resolution authority to perform a specific assessment of a bank capital need after resolution.
	Option 3: CET1 capital after resolution should be at least sufficient to meet anticipated capital buffer requirements, after allowing for any estimated reductions in capital requirements due to the resolution *and* the post-resolution business reorganisation.	• Enable an accurate and comprehensive assessment of capital need.	• More complex and time consuming as it adds a new ladder for the determining the level of CET1 capital. • Reductions in capital requirements due to business reorganisation are less certain and take longer to implement, whereas market confidence is needed from day 1 to enable a prompt return to private sector financing

Preferred option: Option 2, is preferred to option 3, given the importance as a policy objective of the BRRD of ensuring that banks do not need to rely on public sector financial support during or after resolution. G-SIIs tend to rely on market financing to a greater extent and to be subject to a greater degree of market scrutiny and comparison with peers; therefore Option 1 is included in parallel for these firms.

Impact of resolution authority assessment of exclusions

Resolution authority assessments of whether instruments will be excluded from contributing to loss absorption or recapitalisation in resolution are likely to have a significant effect on the MREL set for different institutions. As resolvability assessments have not yet been conducted for most EU banks, it is not possible to observe resolution authorities' assessments. However, some information is available on factors which resolution authorities may be expected to consider. The EBA's draft technical standards on the content of resolution plans and the assessment of resolvability identify a number of factors which resolution authorities should consider in assessing the risk of such exclusions, which include maturity, subordination ranking, identity of the holders of liabilities, legal impediments such as the existence of set-off rights, and other factors (such as risk of needing to compensate creditors for breaches of property rights safeguards, or role in performing critical functions).

The instruments least likely to be excluded from loss absorption or recapitalisation as a result of these factors are equity, own funds instruments, and other subordinated debt. Publicly available data for a sample of 128 EU banks[3] shows outstanding equity and subordinated debt (at consolidated level) totalling approximately €2450bn as of end-December 2013.

Other instruments which meet the criteria of Article 45(4) of the BRRD count towards the MREL but are, to varying degrees, at a greater risk of exclusion. Senior unsecured bonds with a residual maturity of more than 1 year could be excluded from loss absorption or recapitalisation if holders would have made high recoveries in insolvency (for instance, because they rank pari passu to a large amount of liabilities which are not exposed to loss in resolution, or because their holders benefit from set-off rights against the institution).

Combining publicly available data on total outstanding senior bonds for the same sample of 128 EU banks, with data at the level of each member state banking system on the split between secured and unsecured bonds and on their maturity structure[4], shows estimated outstanding senior unsecured debt of approximately €3875bn at end-December 2013. This is the largest component of MREL qualifying liabilities, and resolution authority assessments of whether or not these liabilities are likely to be excluded from loss absorption or recapitalisation will therefore be a critical input into setting the MREL.

Lastly, senior unsecured instruments other than bonds, in particular large corporate deposits with residual maturity of more than one year, may also qualify for inclusion in MREL. Such instruments may be excluded from loss absorption or recapitalisation for the same reasons as senior unsecured bonds. They may in addition be excluded if the resolution authority concludes that they are essential to the provision of critical functions. Data on corporate deposits with residual maturity over 1 year are publicly reported by many banks, but breakdowns between large and small corporate deposits are not.

[3] see Annex 1 for further detail on sample selection and data sources

[4] See Annex 2 for details of proxies used

The most important part of the resolution authority's assessment of the risk of exclusions is therefore the identification of senior unsecured debt which may be excluded from bail-in. This may be especially likely for certain types of liabilities issued by operating entities of banking groups, if bailing these in increases the risk that critical functions provided by the operating entity would be interrupted.

This impact will not be distributed evenly across banks. Generally speaking large banks tend to hold more senior unsecured debt and more large corporate deposits relative to their total assets than small banks.

Table 1: Outstanding amount of qualifying liabilities (Dec-13)

A: Total equity + Total subordinated debt.	2450 EUR Billion
B: A + estimated senior unsecured debt with a residual maturity above 1yr.	6325 EUR Billion

Source: SNL

Annex 1 provides an overview of the proxies used.

Resolution authority assessment of the risk of exclusions will therefore have a significant impact on the MREL shortfalls of individual banks, as well as decisions about. For illustrative purposes, using the same dataset as above shortfalls to illustrative benchmark levels of MREL can be estimated. Note that actual MREL requirements will be set by resolution authorities taking into account resolution strategies and other factors that may affect loss absorption amounts and recapitalisation needed after resolution.

Table 2: Benchmarks levels of MREL

Scenario 1	MREL threshold equal to double the minimum capital requirement including buffers (8% minimum total capital requirement + 2.5% capital conservation buffer + G-SII buffers where relevant).
Scenario 2	MREL threshold at 8 % of total liabilities and equity.

If resolution authorities assessed that only equity and subordinated debt could be feasibly and credibly loss-absorbing under scenario 1 80 of the banks in the sample would have a shortfall to their MREL, totaling €332bn. Under scenario 2 66 banks would have a shortfall, totaling €464bn. However, if resolution authorities assessed that all senior unsecured debt with maturities greater than 1 year was feasibly and credibly loss-absorbing, under scenario 1 only 15 banks would have a shortfall, totaling €36bn, and under scenario 2 only 6 banks would, totaling €12bn. These estimates are illustrative, but indicate the importance of this assessment.

Table 3: Aggregate MREL shortfall (billion euros)

	Scenario 1		Scenario 2	
	Amount	% of assets*	Amount	% of assets*
A: Equity & sub debt only	332	0.98	464	1.37
B: A + senior unsecured debt with residual maturity > 1 year	36	0.11	12	0.04

** Total banking assets of the whole sample*

Source: SNL

Option 1: Develop a formula or formulas for assessing the impact of exclusions on MREL

Option 2: Describe principle for identifying the impact of exclusions on MREL

Area	Policy options	Pros	Cons
2. **Assessment of impact of exclusions from loss/recapitalisation on MREL**	Option 1: Develop a formula or formulas for assessing the impact of exclusions on MREL	• Greater transparency and certainty for authorities and institutions (although assessment of risk of exclusion is done case-by-case)	• Formula would need to be appropriate to all possible circumstances • Impact of inappropriate formula on MREL possibly very large, given importance of decisions on exclusions
	Option 2: Describe principles for identifying the impact	• Allows resolution authorities to ensure impact of	• Less transparency and certainty

	of exclusions on MREL	exclusions is properly considered in all circumstances • Allows resolution authorities to use measures to reduce need for exclusion as well as/instead of MREL	

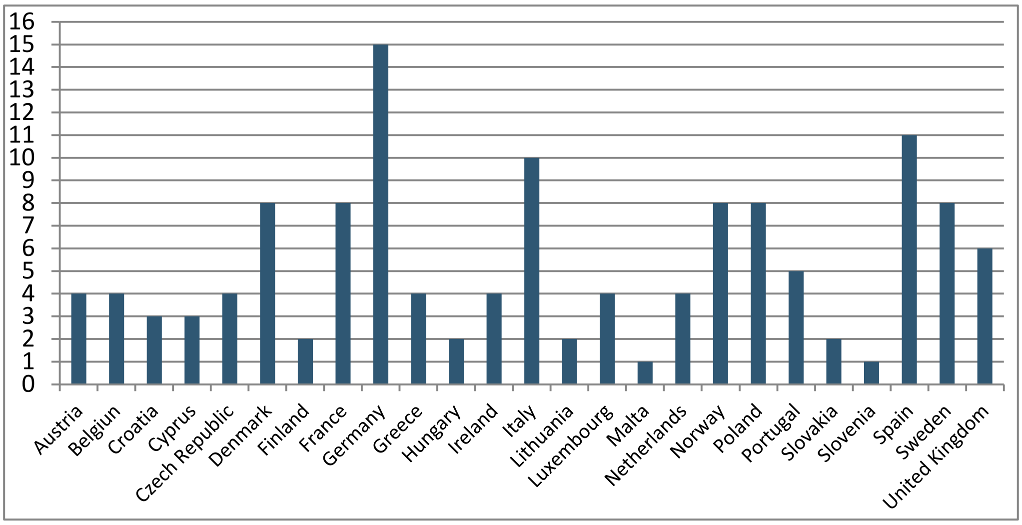
Preferred option: Option 2 is preferred, given the importance of resolution authority decisions on exclusions in setting MREL and the risk that any formula would not adequately take account of the range of liability and legal entity structures of institutions and groups.

Annex 1 of the impact assessment: Sample selection and data sources

To establish an estimate of the amount and distribution of institutions' own funds and liabilities which qualify for inclusion in MREL, EBA staff conducted an analysis based on publicly available data on bank balance sheet (published account data accessed via SNL and aggregated data on Member State banking systems from the ECB). To allow an adequate analysis of the impact of MREL on the EU banking sector the sample has to cover a large number of EU countries and a diversified sample of banking models.

The SNL database covers a sample of 672 EU banks from which the most relevant banks need to be selected. The aim is first to select a representative sample for the analysis, and secondly to avoid double counting in the sample so that the analysis does not overestimate MREL shortfall, i.e. excluding sub-entities when parent company is already available in the sample. The initial criterion for the selection is the size of the institution in terms of its asset value and therefore the analysis selected the largest banks in each jurisdiction. The selection also excluded from the sample the subsidiaries when the parent company is included. 128 EU banks have been included in the sample for the analysis (See Chart 1).

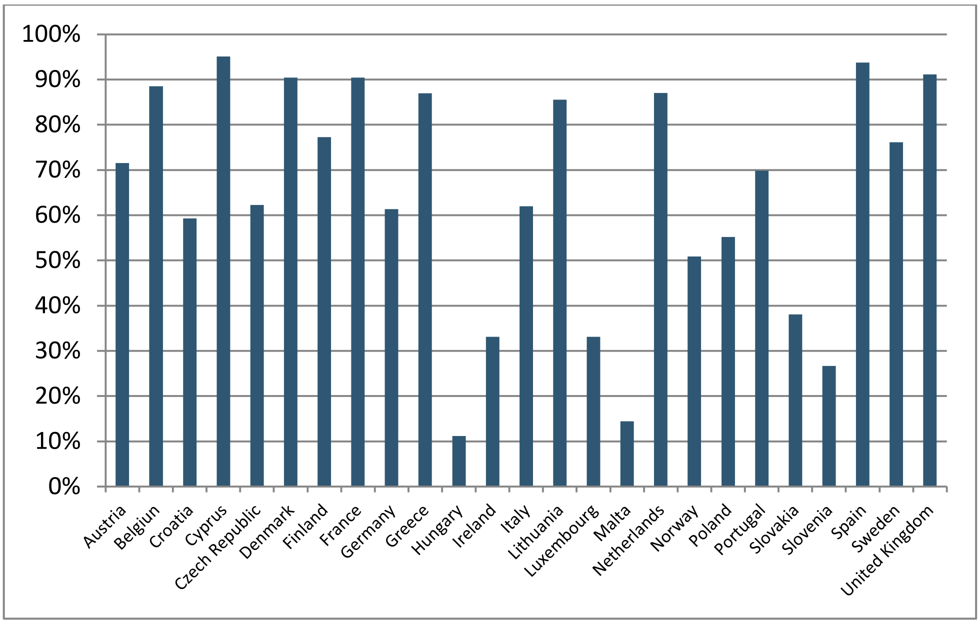
Chart 1: Number of banks included in the selected sample per country



Source: SNL

The sample is broadly representative: in most countries the sample covers more than 50% of the total assets of the banking sector. In the jurisdictions where the selected sample is below is 50% (i.e. Hungary, Slovenia, Slovakia, Malta) the lower level of representativeness is caused by the lack of data in the SNL for these specific countries (and not due to the selection process) (See Chart 2).

Chart. 2: Share of the selected banks in the total banking asset of the country



Source: SNL/ECB

Annex 2 of the impact assessment: Proxies used

Data needed		Availability in SNL	Suggested Proxies
Regulatory capital requirements		0%	Assume equal to: - 10.5% of RWA for other banks (8% of capital requirement + 2.5% of pillar 2 capital requirement - Plus G-SIB buffers for G-SIBs
Debt securities	Share of senior debt maturing >1yr in total debt(H)	0%	This data is not available in SNL on an individual basis. However, the share of senior debt maturing >1yr relative to total debt is available on a country basis. The analysis will assume that this ratio (country average) is constant across institutions in a jurisdiction.
	Total unsecured senior debt (I)	0%	This data is not available in SNL on an individual basis or on a country basis. However, the share of unsecured debt relative to total debt can be computed from NSFR data for each

			country with a distinction between big banks (equity > 3BN EUR) and small banks. The analysis will then assume that these ratios (country average for small and big banks) are constant across institutions in a jurisdiction.
	Total unsecured senior debt >1y (J= IxH)	0%	Once the total unsecured senior funding (I) is estimated, Total unsecured senior debt >1y for each individual can be computed using the country average identified above (point H).

5.2 Overview of questions for Consultation

Question 1	The draft text describes comprehensively capital requirements under the CRR/CRD IV framework, which includes minimum CET1, AT1 and total capital requirements, capital buffers required by CRD IV, Pillar 2 capital requirements set on a case-by-case basis, and alternative backstop capital measures. The EBA is seeking comments on whether all elements of these capital requirements should be considered for the assessment of the loss absorption amount. Do you consider that any of these components of the overall capital requirement (other than the minimum CET1 requirement) are not appropriate indicators of loss in resolution, and if so why?
Question 2	Should the resolution authority be allowed to adjust downwards? What are the specific circumstances under which resolution authorities should allow a smaller need to be able to absorb losses before entry into resolution and in the resolution process than indicated by the capital requirements?
Question 3	Should any additional benchmarks be used to assess the necessary degree of loss absorbency? If yes, how should these be defined and how should they be used in combination with the capital requirements benchmark? Should such benchmarks also allow for a decrease of the loss absorption amount compared to the institution's capital requirements?
Question 4	Do you consider that any of these components of the overall capital requirement are not appropriate indicators of the capital required after resolution, and if so why?
Question 5	Is it appropriate to have a single peer group of G-SIIs, or should this be subdivided by the level of the G-SII capital buffer? Should the peer group approach be extended to Other Systemically Important Institutions (O-SIIs), at the option of resolution authorities? If yes, would the appropriate peer group be the group of O-SIIs established in the same jurisdiction? Should the peer group approach be further extended to other types of institution?
Question 6	The approach outlined in Articles 2 and 3 will reflect differences between consolidated and subsidiary capital requirements. Are there additional ways in which specific

	features of subsidiaries within a banking group should be reflected?
Question 7	Do you agree that there should be a de minimis derogation from this provision for excluded liabilities which account for less than 10% of a given insolvency class?
Question 8	Do you agree that resolution authorities should seek to ensure that systemic institutions have sufficient MREL to make it possible to access resolution funds for the full range of financing purposes specified in the BRRD?
Question 9	Is this limit on the transition period appropriate?
Question 10	Should the resolution authority also set a transitional period for the MREL of banks which are undergoing or have undergone a resolution process?
Question 11	Overall, do you consider that the draft RTS strikes the appropriate balance between the need to adapt the MREL to the circumstances of individual institutions and promoting consistency in the setting of adequate levels of MREL across resolution authorities?
Question 12	Are there additional issues, not identified in this section, which should be considered in the final impact assessment?