

POSITION PAPER



ESBG response to the EBA consultation on the Regulatory Technical Standards (RTS) on the indirect subscription of MREL instruments within groups (“daisy chains”)

ESBG (European Savings and Retail Banking Group)

Rue Marie-Thérèse, 11 - B-1000 Brussels

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We welcome the opportunity to comment on the Regulatory Technical Standards (RTS) on own funds and eligible liabilities. We would like the EBA to consider the following reflections.

A. General Remarks

- ✓ **Timeline:** The finalization of the draft RTS and submission to the EU Commission is planned for the year end 2020. Considering the usual legislative process, it can be expected that the respective delegated regulation will not be adopted & published sooner than beginning of Q2 2021. Nevertheless, the banks are expected to receive their MREL (incl. iMREL) targets in Q1 2021. As the RTS will impact the iMREL capacity of entities subject to the requirement, it will impact the (possible) iMREL shortfalls and thus the linear build-up including the transitional (intermediate) targets. This would then result in the voidness (or at least voidability) of the MREL decisions and the connected need to re-calculate and re-issue the MREL decisions.

Due to the abovementioned, **we propose to shift the application date of the RTS until 1st January 2022**. This option would allow for valid MREL planning as well as valid MREL decisions, since the resolution entities cannot legally apply the RTS in its non-binding state when determining the (i)MREL targets.

- ✓ **Subsidiaries:** The draft RTS does not sufficiently clarify the terms “subsidiaries” or “entities subject to internal MREL requirement”. In order to achieve sufficient level of legal certainty, it is necessary to clarify what constellations and cases fall within the scope of this RTS:
 - Is the RTS applicable to subsidiaries under control (consolidated) of the direct parent subsidiary? (e.g. Subsidiaries 3 and 4 as 100% subsidiaries of Subsidiary 1 of the Parent Entity (Resolution Entity));
 - Is the RTS also applicable to “participations” regardless of ownership rights/consolidation rights? (e.g. Subsidiary 3 as a 25% subsidiary of Intermediate Subsidiary 1 of the Parent Entity (Resolution Entity));

Please clarify **whether this RTS is applicable also for banking groups with Institutional Protection Scheme (IPS)**, especially in the light of the Art. 49 CRR (3). We believe that due to the specificities of the IPS, **it would not be appropriate to include the IPS banking groups under the “general” regime of the RTS**. Should an exception not be possible, a **specific treatment reflecting the IPS and its specificities** should be foreseen in the RTS.

- ✓ **Reporting:** Due to the impact of this draft RTS on the available MREL capacity of the institutions in scope, what will be the implications on Reporting (and disclosure)? Is this RTS already covered by the newly introduced reporting framework 3.0 (and mostly the ITS on MREL/TLAC reporting and disclosure)?
- ✓ **Risk Weighted Assets Adjustment and Deduction:** due to the RTS specifying the need for the RA to consult the Competent Authority and request the allocation of a 0% risk weight to all exposures to be deducted, the following points shall be clarified in the RTS:
 - Clarify that until the decision for the application of a 0% RW is granted, the institutions shall not undertake any deductions, **i.e. the deduction itself and the 0% RW shall be implemented simultaneously** in order to prevent an asymmetrically negative hit on the MREL capacity of the “intermediate entity”.



- Clarify until when the 0% risk weight application shall be considered as granted, e.g. until further notice, until the deduction is necessary, until the NRA requests otherwise?
 - Clarify that the 0% risk weight application to a particular deduction item shall be considered as granted also when the book value of this deduction fluctuates
 - Clarify what the process shall be in case of new deduction items, e.g. a new participation in an entity with iMREL requirement.
 - Provide further clarification on the alignment process between the RA and the CA.
- ✓ **Definition of the deduction:** what shall be the amount of the deduction? Shall it be the exposure value of the deduction item (e.g. the book value of the participation) in the “intermediate entity” balance sheet (e.g. booked according to local GAAP), or shall it be the liability value on the recipient’s entity side, e.g. deduction = book value of equity participation in a non-resolution entity subject to iMREL or deduction = regulatory capital (e.g. CET1) value on the recipient’s entity side.
Proposal: we consider that the methodologically correct value shall be the book value of the iMREL eligible asset as booked in the “intermediate entity’s” balance sheet.



B. Question for consultation

- 1. Do you have any views on the merits of the approach analysed by the EBA to implement the mandate or regarding other options considered under paragraph 14?**
- 2. Could you describe the possible cases of daisy chains 17 in the institutions you represent, taking into account the BRRD2 MREL conditions (but without considering waiver possibilities)?**
- 3. In the institutions you represent, how would you deal with daisy chain situations? Do you plan to issue eligible liabilities directly from subsidiaries to the resolution entity, or rather indirectly through the intermediate subsidiaries?**

We plan to issue both directly and indirectly to the resolution entity

- 4. The deduction regime increases in general 18 the issuance needs of intermediate entities. What could be the financial impact(s) of such increase of issuances? (allocation of profits/distribution of dividends, capital of subsidiaries, buffers redistribution across the group, tax, etc.). Please answer qualitatively, and if possible, also quantitatively regarding the institution you represent.**

The main negative impact stems from the fact that the envisaged deductions will lead to a higher internal MREL issuance at the level of the intermediate entity. For liquidity-rich, deposit funded intermediate entities, this means an artificial balance sheet inflation, as the surplus liquidity out of the iMREL issuance will be placed back to the Resolution Entity, thereby inflating also its balance sheet. Albeit those transactions being intra-group, there could be significant negative P&L impacts due to:

- ✓ **Banking taxes** being levied on the solo-unconsolidated balance sheet of local banks
- ✓ **Resolution Fund Contribution Fees**, which are also levied on the solo-unconsolidated balance sheet of banks. In order to mitigate the negative impact on this, we suggest that EBA re-consider the definition of the contribution base on which Resolution Fund Contributions are based and also include a deduction item for all iMREL eligible instruments, instead of Own Funds only.

In addition, and as pointed out above under point 1) the functioning of institutional protection schemes is not properly reflected in the current RTS. Such IPS are set-up and also approved by competent authorities in a way which enables the efficient up- and/or side-streaming of losses and ensures re-capitalization in case of need. Not reflecting the IPS within the RTS can result in a deviating treatment both for regulatory capital and internal MREL purposes.

- 5. In the institutions you represent, how many cases are there where an intermediate subsidiary is not regulated, or located in a non-EU jurisdiction (and therefore not subject to banking capital requirements resp. MREL requirements), or where the CA has only set sub-consolidated (and no individual) own funds requirements to an intermediate subsidiary (therefore no individual P2R or CBR applies to it)?**
- 6. Are there any circumstances, including, but not limited to, the complexity of the Group, in which you would foresee significant issues with the implementation of this RTS? If so, please provide further details of the circumstances and the issues that would be faced.**



About ESBG (European Savings and Retail Banking Group)

ESBG represents the locally focused European banking sector, helping savings and retail banks in 21 European countries strengthen their unique approach that focuses on providing service to local communities and boosting SMEs. An advocate for a proportionate approach to banking rules, ESBG unites at EU level some 900 banks, which together employ more than 650,000 people driven to innovate at roughly 50,000 outlets. ESBG members have total assets of €5.3 trillion, provide €1 trillion in corporate loans (including to SMEs), and serve 150 million Europeans seeking retail banking services. ESBG members are committed to further unleash the promise of sustainable, responsible 21st century banking. Our transparency ID is 8765978796-80.



European Savings and Retail Banking Group – aisbl
Rue Marie-Thérèse, 11 ■ B-1000 Brussels ■ Tel: +32 2 211 11 11 ■ Fax: +32 2 211 11 99
Info@wsbi-esbg.org ■ www.wsbi-esbg.org

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