EFBS – FINANCIAL AFFAIRS COMMITTEE

SRB MREL Policy under the Banking Package

Single Resolution Board

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Agenda

SRB MREL POLICY UNDER THE BANKING PACKAGE

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Banking package: New regulatory classifications

Type of institution	Description
G-SIIs	CRR-CRD designation in line with FSB methodology; (Pillar) 1 MREL
Top-tier (> € 100bn assets)	Banks with total assets above EUR 100 bn with a minimum (Pillar 1) MREL, including subordination
Other Pillar 1 banks (selected by NRAs)	Banks that are neither G-SIIs nor Top-tier banks which the NRAs have assessed as reasonably likely to pose a systemic risk in the event of failure (Art. 12d(5) SRMR); the SRB will apply the same regime as for top-tier banks
Others (those not covered above)	Other banks which do not fall in the previous classifications which might have subordination requirements based on the assessment of NCWO risk

Banking package: MREL calibration

- MREL continues to be composed of:
  - Loss absorption amount (LAA)
  - Recapitalisation amount (RCA)
- New: the MREL expressed in LRE applies in parallel to MREL-TREA
- Both have to be met in parallel at all times

LAA *(CBR is removed from the formula)*

$$LAA_{TREA} = \left(TREA \text{ x } (Pillar\ 1 + Pillar\ 2)\right)$$

$$LAA_{LRE} = (LRE \text{ x } Leverage\ Ratio)$$

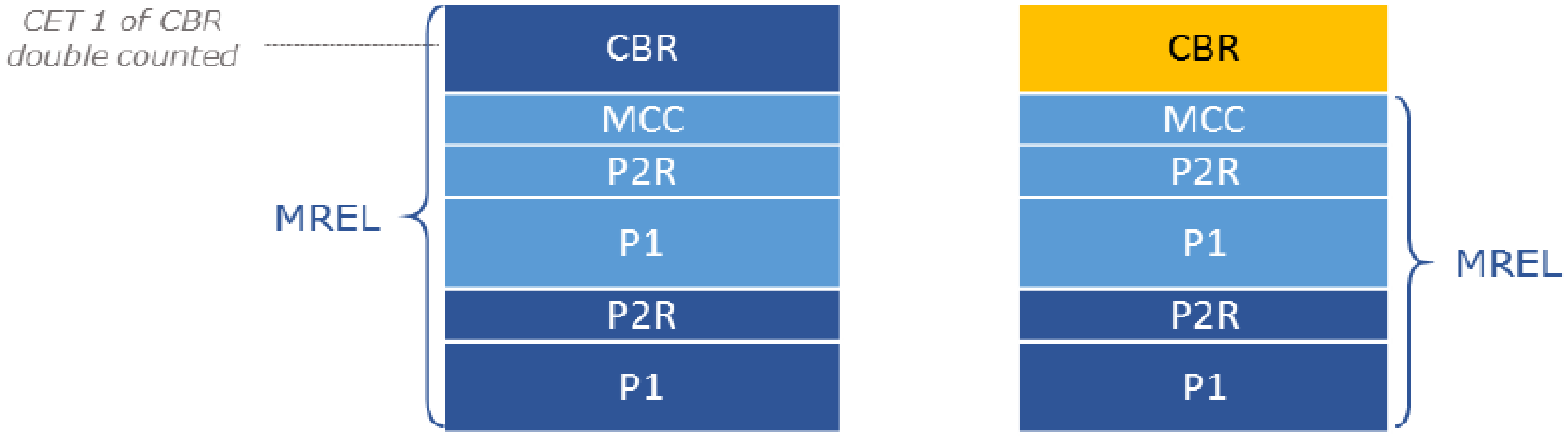
RCA

$$RCA_{TREA} = \left(TREA \text{ x } (Pillar\ 1 + Pillar\ 2)\right)$$

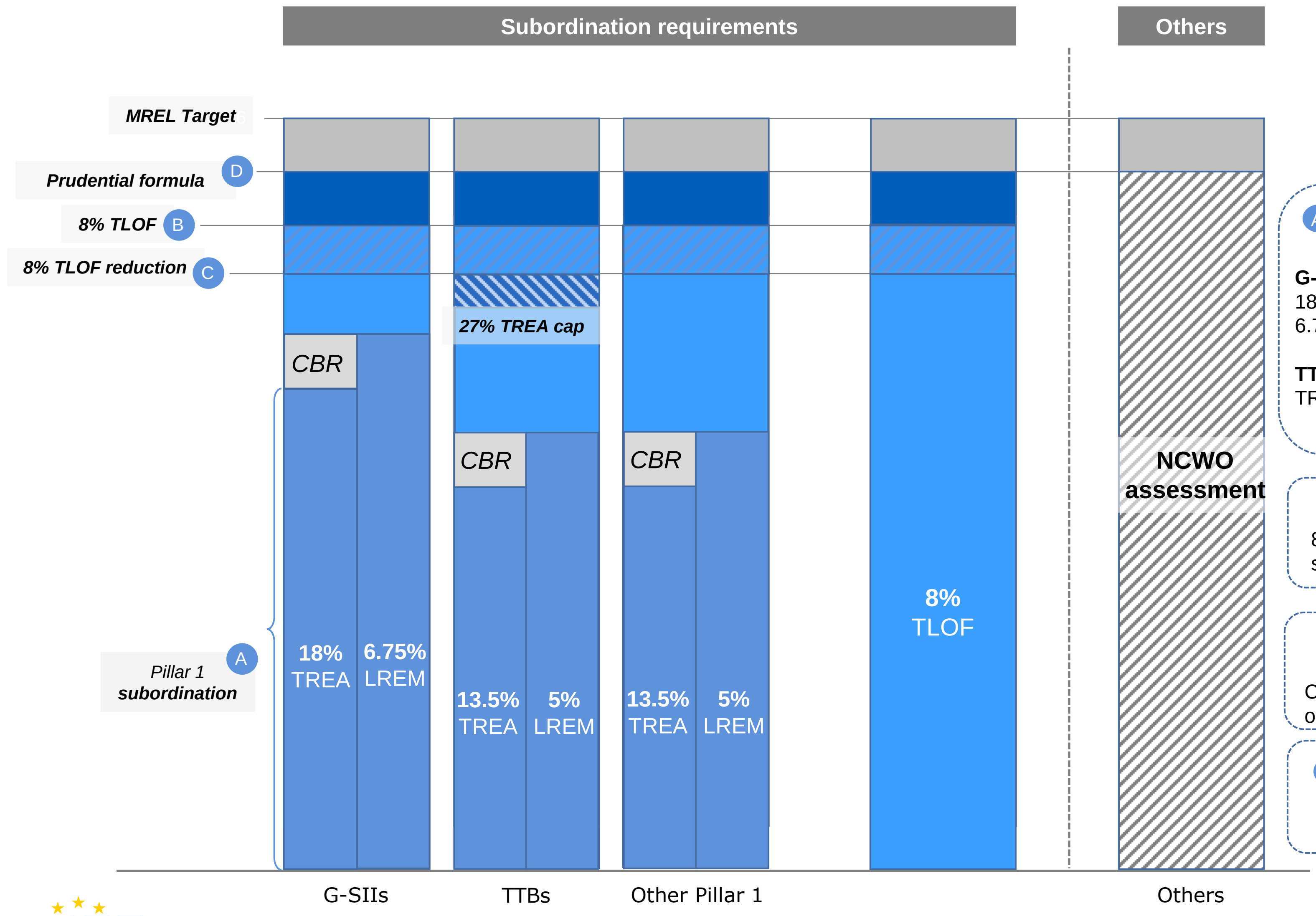
$$RCA_{LRE} = (LRE \text{ x } Leverage\ ratio)$$

Banking package: MREL calibration

- **Interplay with capital buffers**
  - In RWA framework, no counting of CET1 used for CBR
  - In LRE framework, buffer capital can be used for MREL



Banking package: Overview of MREL Subordination



A *Pillar 1 subordination*

G-SIIs:
18% TREA (add. CBR) or 6.75% LREM

TTBs / Other Pillar 1: 13.5% TREA (add. CBR) or 5% LREM

B ***8% TLOF target***

8% TLOF additional subordination requirement

C ***potential 8% TLOF reduction***

Case-by-case decision based on NCWO

D *potential **increase of 8% TLOF***

up to the "prudential formula": 2x P1 + 2x P2R + CBR

MREL Subordination: NCWO assessment

A value-based assessment of NCWO risk

- The NCWO methodology seeks to quantify NCWO risk by comparing the value of instruments held by different creditors in resolution with their value in insolvency using a dedicated **quantitative tool**.

Parameters of the quantitative tool:

Insolvency scenario: In order to assume losses associated with asset realisation (asset haircut) or the extent to which assets will be liquidated below their book value in insolvency proceedings → hc_{Assets} = 10% is applied to the remaining balance sheet after LAA absorption of initial losses.

Resolution scenario: Part of claims converted into shares (RCA) partially compensates the creditor for the loss of the debt claim → $PtB_{OF\_from\_Senior}$ = 25% is applied to obtain the market value (opposed to the book value) to the received shares by the creditors.

Internal MREL

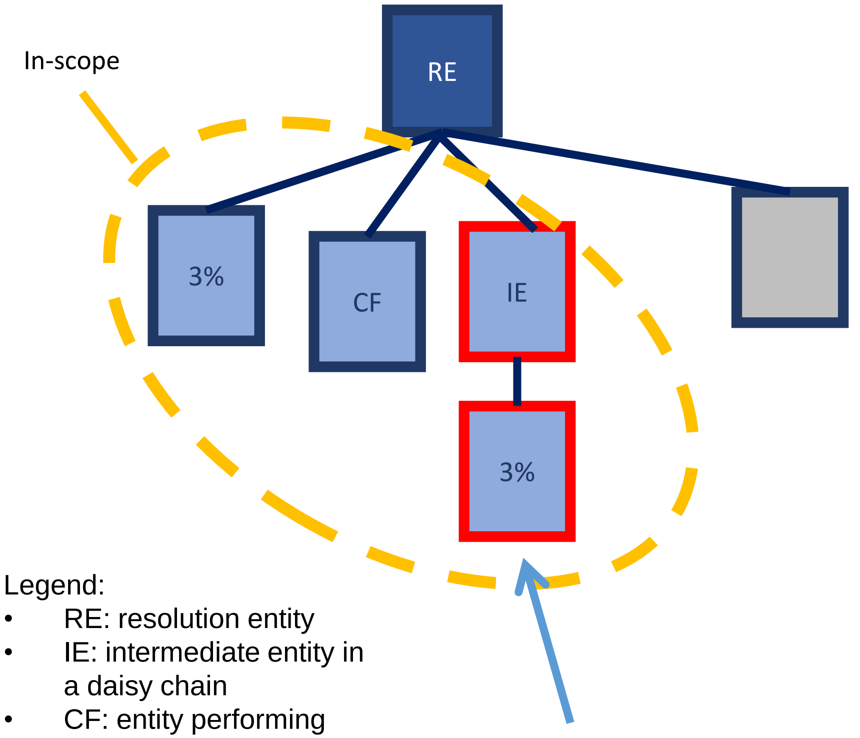
- **Calibration** before adjustments:
  MRELTREA = LAA(P1+P2)+RCA(P1+P2)
  MRELLRE = LAA(3% LRE)+RCA(3% LRE)

- The **2021 MREL policy expands the scope of non-resolution entities** subject to iMREL.

- The threshold for being determined as Relevant Legal Entity (RLE) is reduced **from 4% to 3%.**

- **iMREL applies to credit institutions and financial holding companies subject to prudential requirements (CRR).**

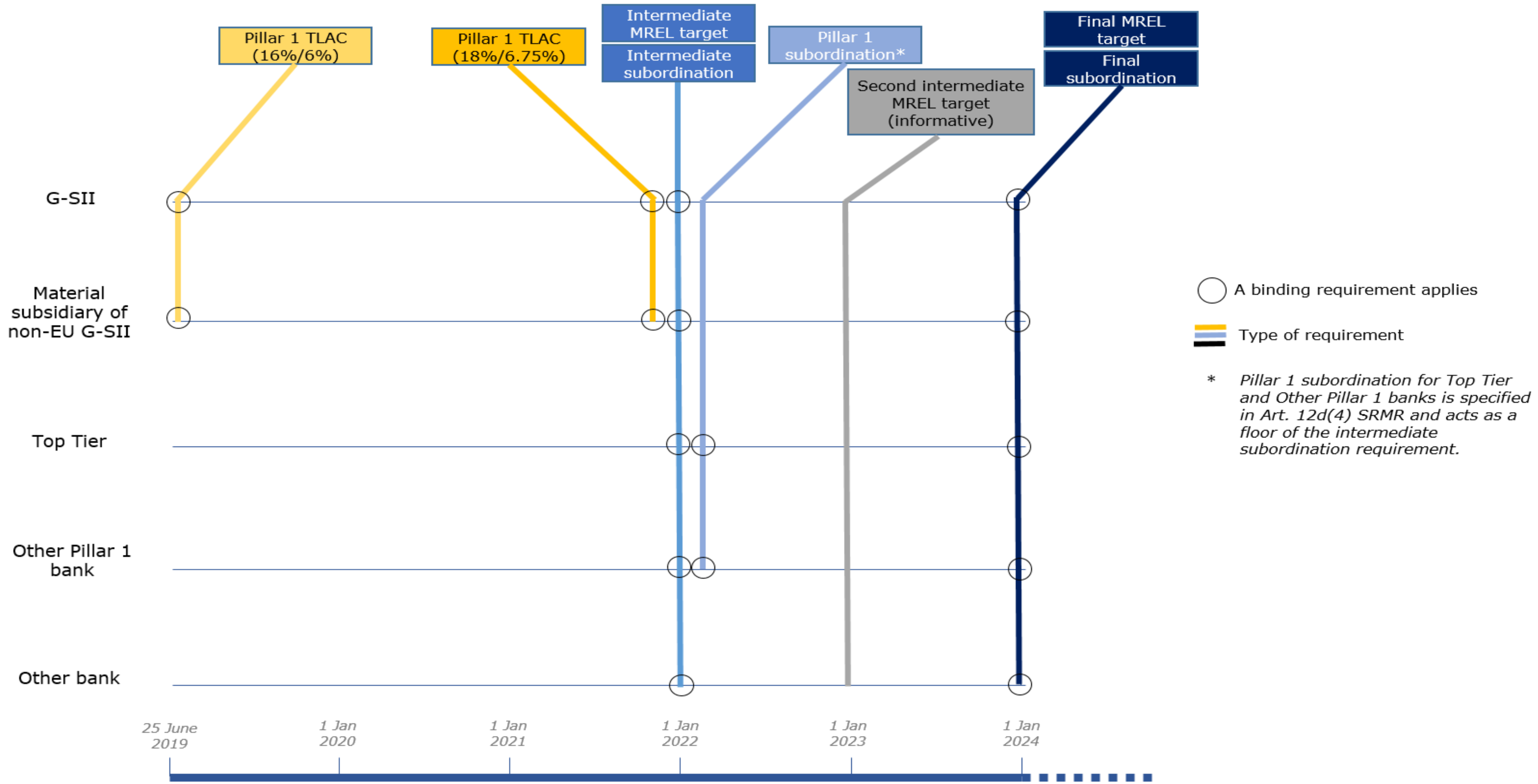
- In addition, the **SRB sets internal MREL to intermediate entities**: an intermediate entity is defined as a subsidiary of a resolution entity that is a parent entity of at least one RLE.



Legend:
- RE: resolution entity
- IE: intermediate entity in a daisy chain
- CF: entity performing critical functions
- 3%: entity above the 3% threshold for RLE

Lowest entity meeting any of the RLE criteria

Transition periods



SRB MREL policy: what was already in place?

In May 2020, **the SRB published its MREL policy** implementing the vast majority of changes introduced by the applicable **SRMR2, BRRD2 and CRR2 rules.**

- The policy covered the following aspects:
  - MREL requirements for Global Systemically Important institutions (G-SIIs);
  - Changes to the calibration of MREL, including introducing MREL based on leverage ratio exposure (LRE) and based on risk-weighted exposure (TREA);
  - Changes to the quality of MREL (subordination);
  - Dedicated rules for certain business models, such as cooperatives, and for resolution strategies, such as multiple point of entry (MPE);
  - Provisions on internal MREL;
  - Clarifications on third-country issuances; and
  - Phasing-in provisions.

SRB MREL Policy: 2021 policy update

- The update refines the 2020 MREL Policy and introduces new elements:
  - Internal MREL: Revised thresholds (from 4% to 3%) for relevant legal entities
  - Waivers from internal MREL: Criteria for systemic subsidiaries for which no internal MREL waiver is possible
  - P2R post-resolution: Based on SREP score and further adjusted based on bank risk profile
  - MREL calibration on preferred vs variant strategy: Based exclusively on the preferred resolution strategy
  - MREL calibration for liquidation entities: Can increase LAA beyond the default adjustment proportionately to financial stability concerns
  - MREL eligibility: New chapter on MREL eligibility conditions and management sign-off form
  - MREL maximum distributable amount (M-MDA): New chapter on M-MDA restrictions that may be applied in cases of MREL breaches

SRB Permission Regime to reduce eligible liabilities under Art. 78a CRR

- On 26 May, the EBA published its Final Report on the draft RTS on the Permission Regime.
- On 28 July, the SRB published an Information Notice that it will apply the RTS on the Permission Regime as of 1 January 2022.
- Exceptionally, banks can submit permission applications to the SRB until end September 2021 (instead of end August 2021) to be authorized for 1 January 2022.
- Communication on the SRB website to assist banks in understanding the contents of the RTS.

MREL Maximum Distributable Amount (M-MDA)

- In accordance with **Article 10a SRMR**, the SRB may set restrictions preventing entities from distributing more than the MDA related to MREL (M-MDA) via various actions (incl. dividend payments on CET1, variable remuneration and payments on AT1 instruments).
- The M-MDA may be applied where:
  - ✓ the entity **meets the combined buffer requirement (CBR) in addition to the own funds requirements** (i.e. no prudential MDA),
  - ✓ but **fails to meet the CBR in addition to the external and internal MREL (including subordination), a well as external and internal TLAC, expressed in risk exposure amount (TREA)**.

What is expected from the banks in case of a shortfall on CBR?

- Once the entity is in shortfall, it shall immediately notify the national resolution authority and the SRB.
- Banks should not wait until breaches occur and should signal expected breaches.
- Banks are expected to provide all the necessary data to the SRB to perform the monthly assessments.
- The M-MDA may also be applied in case of MREL breaches.

MREL Maximum Distributable Amount (M-MDA)

Interplay with prudential MDA

- **Common features:** The M-MDA shares many features with the prudential MDA-regime (where the CBR has to be met in addition to Pillar 1 and Pillar 2 requirements), e.g. the computation methodology.
- **No automaticity:** Unlike the prudential MDA, the M-MDA regime is not automatic and its application is subject to a discretionary decision of the resolution authority, which needs to follow specific procedural steps and assessment criteria.
- **Precedence of prudential MDA**

How will the SRB assess whether to impose M-MDA?

Notification by the bank

Stage I:
SRB assesses whether to exercise the M-MDA power, taking into account all of the elements set out in Article **10a(2) SRMR**

9 months later

Stage II:
SRB in principle exercises the M-MDA power, except where it finds that at least two of the conditions set out in Article **10a(3) SRMR** are fulfilled

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A formal consultation with the ECB will run during each stage.

Outlook for next Resolution Planning Cycles

The SRB will continue completing and refining the MREL policy, in particular in the following areas:

- **NCWO approach:** the SRB will assess the possibility to reflect more elements in the NCWO methodology, notably the evolution of the bank's balance sheet and the potential impact of the discretionary exclusions.
- **Further work on transfer strategies:** the SRB will enhance the MREL policy for these resolution strategies.
- **Implementing new EBA RTS into the SRB policy:** the SRB will revise the MREL policy once new EBA RTSs will be endorsed, e.g. on prior permissions and on daisy-chains.

THANK YOU!

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