



Minimum Requirement for Own Funds and Eligible Liabilities (MREL)

2018 SRB Policy for the second wave of resolution plans

Published on 16 January 2019





MREL Policy – second wave of resolution plans

Disclaimer: The SRB MREL policy is subject to further potential revisions, including as a result of changes in the applicable European Union (EU) legislation. This public document aims to make the public in general, and institutions in particular, aware of the SRB MREL policy as well as the process currently being followed to determine MREL targets in the SRB 2018 resolution planning cycle for institutions included in the second wave. The SRB MREL policy has been elaborated with national resolution authorities of the Banking Union and represents a common approach to ensure consistency and a level playing field within the Banking Union, and takes into account where necessary any bank-specific features. The SRB may deviate from the content of this document if it considers it necessary and in line with bank-specific features and the applicable legislative framework.

EXECUTIVE SUMMARY

- 1 The Single Resolution Board (SRB) hereby publishes its policy statement on minimum requirement for own funds and eligible liabilities (MREL) for the second wave of resolution plans of the 2018 cycle, following the publication of the SRB policy statement for the first wave of resolution plans on 20 November 2018. The SRB has split the cycle for resolution planning in 2018 into two waves and has followed a transitional two-step approach to the MREL-setting process. This policy applies to the second wave of resolution plans which are those of the most complex groups.

Interaction with the "Banking Package" – preparing the transition to future requirements

- 2 While this policy on MREL is based on the current legislative framework, the SRB is raising the bar in terms of banks' resolvability and MREL targets to prepare the ground for future regulatory changes in the context of the "Banking Package" (CRR2/BRRD2/SRMR2), recently agreed upon but not yet formally adopted by the co-legislators.
- 3 The SRB will therefore review its policy for MREL setting for further updates in 2019 on the basis of the publication of the Banking Package in the Official Journal of the EU, with the aim of charting a consistent path and preparing banks to transition to the new regime, as well as to reflect any change necessary due to those requirements potentially coming into force in 2019.

MREL at consolidated level – completing the framework

- 4 While the 2018 SRB policy follows a number of the elements defined in the 2017 policy, some new elements are added.

Location of eligible resources

- 5 Progressing from the consolidated approach counting all liabilities issued from entities of the same resolution group in the 2017 policy, a Point-of-Entry approach will now apply for liabilities other than own funds instruments. Only liabilities issued directly by the resolution entity will be considered eligible to meet consolidated targets on the ground that resolution tools will be applied only to this entity as the point of entry for the resolution strategy. The amount of own funds instruments issued by the resolution entity or the subsidiaries within the resolution group that are recognised for meeting the consolidated CRR prudential requirements will continue to be included in MREL calculations taking into account the loss-absorbing capacity of own funds instruments located outside the resolution entity.

Subordination

- 6 Subordination is instrumental for making resolution strategies more credible and feasible. In order to improve resolvability by addressing NCWO risk and to support banks in effectively planning their funding needs, the SRB now moves from informative benchmarks in previous policy towards determining binding subordination requirements for all banks with a consolidated target, at increased levels.
- 7 Subordination levels will be set based on a combination of a general level, applicable buffer requirements and a metric, taking account of the bank-specific nature of the assessment of NCWO risk in the senior layer. A floor of 16% RWA plus CBR will apply for G-SIIs, and of 14% RWA plus CBR for O-SIIs and other resolution entities.

Calibration

- 8 The SRB allows for adjustments of the RCA, including the MCC, to reflect the transfer of assets. When the strategy relies primarily on a transfer tool (sale of business – share or asset deal, bridge institution and/or asset separation), the SRB will adjust the RCA by applying a scaling factor of minus 20% of total assets, as a proxy to reflect the change in recapitalisation needs, in particular due to assets that would be transferred and/or liquidated under normal insolvency proceedings. This scaling factor applies to the RWA basis as well, and can be added to other bank-specific adjustments applied to the RCA, including the MCC, where relevant. It represents an interim step towards a more tailored, bank-specific approach.
- 9 When considering the appropriate resolution tools and the need for a variant strategy, MREL targets should be set at a level ensuring that the implementation of both strategies is credible and feasible. Where transfer strategies rely on a third party and market conditions to be implemented, the SRB requests a variant strategy. Therefore, the MREL needs to be calibrated prudently to reflect the most stringent strategy (baseline or variant). When the resolution plan envisages a variant strategy relying on an open-bank bail-in approach, the MREL target is based on the bail-in tool.

Introducing MREL at individual level

- 10 With a view to ensuring a sufficient quantum of loss absorbing capacity in all parts of the resolution group, the SRB will start issuing binding targets at the individual level to subsidiaries of banking groups, prioritising the most relevant entities. Calibration of individual targets generally follows the methodology for consolidated targets, taking into account the applicability of individual components of prudential requirements of the default formula (P2R, buffer components) at individual level, as well as specificities in subsequent adjustments.



- 11 While standard BRRD eligibility criteria apply, supplementary informative guidance on achieving internal MREL, aligned as closely as possible with eligibility for internal MREL as foreseen in the forthcoming Banking Package, is given to banks to enhance the internal loss absorbing capacity within the resolution groups and preparing banks for the future legal framework.

CONTENT

| | |
|--|-----------|
| EXECUTIVE SUMMARY | 4 |
| ABBREVIATIONS | 8 |
| METHODOLOGY | 9 |
| A – TARGETS AT CONSOLIDATED LEVEL - CALIBRATION | 9 |
| B – TARGETS AT CONSOLIDATED LEVEL - ELIGIBILITY | 13 |
| C – TARGETS AT INDIVIDUAL LEVEL - CALIBRATION | 19 |
| D – TRANSITION PERIODS | 21 |
| CONCLUSION AND NEXT STEPS | 22 |

ABBREVIATIONS

| | |
|-------|--|
| BRRD | Bank Recovery and Resolution Directive |
| CBR | combined buffer requirement |
| DGS | deposit guarantee scheme |
| DR | Commission Delegated Regulation |
| EU | European Union |
| FSB | Financial Stability Board |
| G-SII | Global Systemically Important Institution |
| LAA | loss-absorbing amount |
| MCC | market confidence charge |
| MPE | multiple points of entry |
| MREL | minimum requirement for own funds and eligible liabilities |
| NCWO | no creditor worse off |
| P1 | Pillar 1 requirement |
| P2R | Pillar 2 requirement |
| RC | resolution college |
| RCA | recapitalisation amount |
| RWA | risk-weighted assets |
| SPE | single point of entry |
| SRB | Single Resolution Board |
| SREP | supervisory review and evaluation process |
| TLAC | total loss-absorbing capacity |

METHODOLOGY

A – TARGETS AT CONSOLIDATED LEVEL - CALIBRATION

- 12 **The MREL policy builds on the delegated regulation (DR) ⁽¹⁾ default formula**, made up of two components: (i) a loss absorbing amount (LAA), which reflects the losses that the bank will incur in resolution, and (ii) a recapitalisation amount (RCA), which reflects the amount needed to ensure that ongoing prudential requirements are met after resolution. The latter component is complemented by a market confidence charge (MCC), necessary to ensure market confidence post-resolution. MREL targets are based on fully loaded risk weighted assets (RWAs) and fully loaded capital requirements.
- 13 **The Basel I floor has been removed from the MREL formula, while the leverage ratio remains excluded from the MREL formula.** The Basel I floor has been removed from the MREL formula because it is no longer applicable (Article 500 of the Capital Requirements Regulation expired on 31 December 2017). The leverage ratio is not included in the computation because it remains non-binding under the legal framework as of the date of this publication. The SRB reserves the right to update this element following the publication of any binding leverage ratio requirement in the Official Journal of the EU.
- 14 **MREL targets will be set using supervisory and resolution reporting data.** MREL targets will be set using the final supervisory review and evaluation process (SREP) decisions and Pillar 2 requirements approved in 2017, and based on end-2017 balance sheet data.

The SRB uses the default LAA

- 15 **The SRB uses the default LAA without adjustments.** In accordance with the DR, the SRB considers the default LAA ⁽²⁾ the sum of a bank's minimum capital requirement (Pillar 1 requirement), its Pillar 2 requirement (P2R), and its fully loaded combined buffer requirement (CBR).

$$\text{SRB default LAA} = \text{P1} + \text{P2R} + \text{CBR}$$

The SRB considers bank-specific adjustments for the RCA

- 16 **The default formula remains the starting point for determining the RCA.** Under the DR, there are two components of the RCA: the minimum requirement for

⁽¹⁾ Commission Delegated Regulation (EU) 2016/1450.

⁽²⁾ For the specificities of MPE adjustments, see *infra* para. 24.

authorisation (P1 and P2R), and an amount intended to regain market confidence, the MCC. In line with the 2017 MREL policy, the SRB has decided to set the default MCC at the level of the CBR minus 125 basis points.

$$\text{SRB default RCA} = \text{P1} + \text{P2R}$$

$$\text{SRB default MCC} = \text{CBR} - 125 \text{ basis points}$$

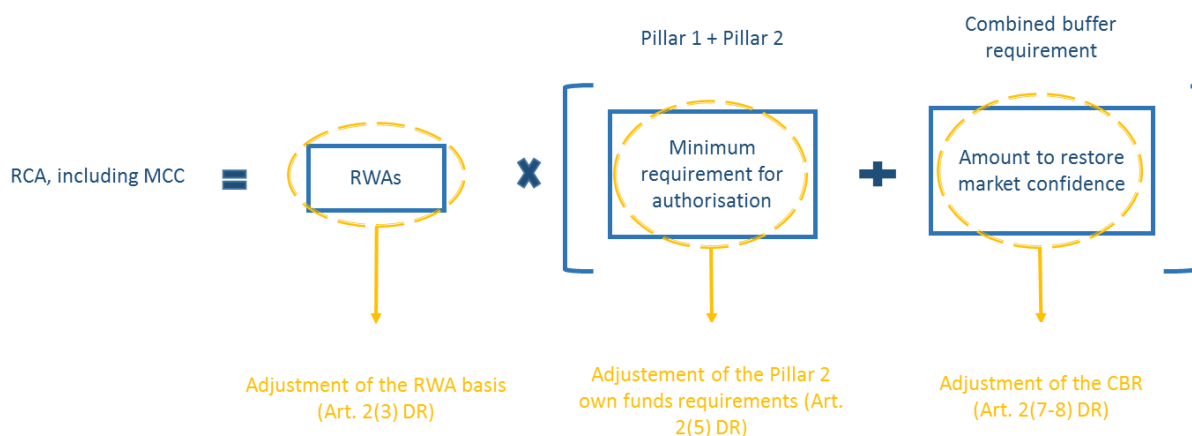
17 Banking groups for which liquidation is the preferred resolution strategy have no RCA. Where the preferred strategy at the level of the group is liquidation, MREL will be set at the level of the LAA, with no RCA and no MCC.

18 Bank-specific adjustments are considered on the basis of the DR. The DR enables resolution authorities to make bank-specific adjustments to three components of the RCA, including the MCC. These adjustments relate to the following (see also Figure 1):

- 1) The RWA basis for the calculation of the RCA and MCC: resolution authorities may use a different RWA basis from the reported RWA to calculate the RCA and the MCC ⁽³⁾.
- 2) The Pillar 2 own funds requirements used for the default RCA: these can be adjusted to define the amount required to comply with the conditions for authorisation after the implementation of the preferred resolution strategy.
- 3) The level of the CBR used for the default MCC: this can be adjusted to tailor the amount required to maintain sufficient market confidence after resolution.

⁽³⁾ In particular, when the resolution plan identifies, explains and quantifies any change in regulatory capital needs immediately as a result of resolution action, and when this change is considered in the resolvability assessment to be both feasible and credible without adversely affecting the provision of critical functions by the institution and without recourse to extraordinary public financial support.

Figure 1: Bank-specific adjustments under the DR for the RCA, including the MCC



19 The SRB may allow, on a bank-by-bank basis with due justification, three adjustments to the RWA basis. These adjustments relate to:

- 1) **The effect of balance sheet depletion:** the failure of a banking group may result in the banking group having a smaller balance sheet directly following resolution, particularly if the failure was due to credit risk losses. The SRB considers that, on a group-by-group basis, a maximum balance sheet depletion of up to 10% of total assets may be used to adjust the RWA basis ⁽⁴⁾.
- 2) **The use of recovery options and other measures:** the SRB may consider those recovery options and other measures which can be actionable immediately in resolution, provided the SRB foresees these options as a credible and feasible resolution action in the respective resolution plan. Adjustments on the basis of one or more recovery options would be capped at the level of 5% of RWAs.
- 3) **Restructuring plan divestments and sales:** if actions as formulated in restructuring plans ⁽⁵⁾ are legally binding and time-bound, the SRB may take into account the possible impact on the bank's RWA basis. These plans aim to restore the long-term viability of the bank by achieving sustainable profitability and reducing risk, among other goals. This includes the removal of riskier assets with

⁽⁴⁾ The SRB assumes that the incurred losses would equal the LAA, and that these losses would reduce the total asset amount of the balance sheet accordingly under the assumption that the risk density of the assets would remain stable post-resolution in comparison with its *ex ante* resolution level.

⁽⁵⁾ When restructuring plans have been agreed upon between a Member State and the EU Commission.

associated higher risk weighting from the balance sheet through mandatory deleveraging actions embedded in the restructuring plan.

20 The SRB does not envisage any further adjustments to the default RCA and MCC.

Other bank-specific adjustments taken into account for the overall MREL target

21 The SRB maintains the reference to an 8% total liabilities and own funds benchmark. MREL should be set at a sufficiently prudent level to allow access, if necessary, to financing arrangements such as the Single Resolution Fund. In line with the approach taken in 2017, the SRB will analyse on a case-by-case basis any deviation from this benchmark.

22 In line with the general 2017 MREL policy, the SRB does not envisage any other adjustments to MREL targets for the second wave of resolution plans. This relates in particular to (i) liabilities that are likely to be excluded in exceptional circumstances under Article 44(3) of the BRRD and (ii) deposit guarantee scheme (DGS) contributions. The SRB considers that taking into account DGS contributions would not be consistent with the preferred resolution strategy for most of the banking groups under its direct responsibility.

Specificities of multiple-points-of-entry strategies are addressed

23 SRB is applying a dedicated formula for MPE strategies. In an MPE strategy, the banking group is resolved through the application of resolution powers to the resolution group where losses materialise. A resolution group comprises a resolution entity (i.e. a point of entry) and its subsidiaries that are intended to be resolved jointly through the upstreaming of losses to the resolution entity. It is essential that a credible and feasible MPE strategy can be executed without undermining the viability and resolvability of other resolution groups. Therefore, contagion risk is minimised where one resolution group within a bank can be resolved without causing the failure of the other resolution groups.

24 The SRB MREL policy identifies the requirement for a consolidated MREL target at the level of each resolution entity, within the MPE group. MREL targets will be based on the applicable total capital requirement and the applicable total RWA of the resolution group (i.e. excluding the RWA of other resolution groups in the same banking group); and specific adjustments to take into account potential expected LAA stemming from participations in other resolution groups as well as the RCA needs related to residual exposures to those resolution groups following expected loss absorption.

Calibration for transfer strategies

- 25 **In order to use transfer strategies ⁽⁶⁾, resolution plans have to analyse the market and ensure that banks meet high standards in terms of separability and data availability.** Among other requirements, the planning and operationalisation of transfer strategies have to (i) achieve a certain degree of separability, (ii) ensure a fair and precise analysis of market depth, and (iii) confirm the availability of adequate management information systems and data to support these strategies.
- 26 **The SRB allows for adjustments to the RCA, including the MCC, to reflect the transfer of assets.** When the strategy relies primarily on a transfer tool (sale of business – share or asset deal, bridge institution and/or asset separation), the SRB will apply a scaling factor of minus 20% of total assets, as a proxy to reflect the recapitalisation needs post resolution or the assets that would be transferred and/or liquidated under normal insolvency proceedings. This scaling factor applies to the RWA basis as well, and can be aggregated with other bank-specific adjustments applied to the RCA, including the MCC, where relevant. It represents an interim step towards a more detailed methodology.
- 27 When considering the appropriate resolution tools and the need for a variant strategy, MREL targets should be set at a level ensuring that the implementation of both strategies is credible and feasible. Where transfer strategies rely on a third party and market conditions to be implemented, the SRB requests a variant strategy. Therefore the MREL needs to be calibrated prudently in line with the most stringent strategy (baseline or variant). When the resolution plan envisages a variant strategy relying on an open-bank bail-in approach, the MREL target is based on the bail-in tool.

B – TARGETS AT CONSOLIDATED LEVEL - ELIGIBILITY

Subordination

- 28 **Subordination improves resolvability and reduces the risk of breaching the NCWO principle.** Subordination can be considered a tool to improve resolvability by making the implementation of the bail-in tool feasible and credible. In particular, subordination addresses risks stemming from (i) having bail-in-able instruments ranking *pari passu* with operational liabilities and any other excluded liabilities prescribed by Article 44(2) of the BRRD and (ii) the exercise of the discretionary power

⁽⁶⁾ Transfer strategies are resolution strategies that do not rely on the use of the bail-in tool (open-bank bail-in), but envisage the use of the sale of business tool, the bridge institution tool and/or the asset separation tool, in accordance with the legal framework.

of the resolution authority to exclude some liabilities from bail-in under exceptional circumstances (Article 44(3) of the BRRD).

- 29 **Subordination requirements will be determined on the basis of two elements:** a general level depending on the systemic importance of banks and a potential bank-specific add-on to address NCWO risks based on mandatory exclusions. The determined overall subordination requirement cannot be higher than the consolidated target, or lower than overall capital requirements. The assessment of compliance with the relevant subordination levels will take into account all forms of subordination, including 'senior non-preferred' instruments, where they exist, subject to analysis in line with national laws, and structural subordination. The SRB reserves the right to adjust this policy at a later stage in the light of the future design of the BRRD/SRMR and further development of the MREL policy.
- 30 **The SRB requires a minimum level of subordinated instruments, depending on the size and systemic importance of banks.** In adherence to global TLAC standards, banks which have been identified as global systemically important institutions (G-SIIs) will be required to maintain a minimum percentage of subordinated instruments equal to 16% of RWA plus the CBR; banks identified as other systemically important institutions (O-SIIs) and other resolution entities will be expected to fulfil a minimum percentage of subordinated instruments equal to 14% of RWA plus the CBR. This reference point acts as a proxy to improve resolvability and addresses potential NCWO issues.
- 31 **The SRB may also set a NCWO add-on related to mandatory exclusions from bail-in.** In line with the DR, each time the mandatorily excluded liabilities as specified in Article 44(2) of the BRRD exceed a threshold of 10% of the relevant liability class, an assessment has to be performed regarding the possible risk of breaching the NCWO principle when applying the bail-in tool. Pending the availability of sufficient data and of a reliable method enabling the SRB to reach final bank-by-bank determinations on such risk, the SRB considers this threshold as an indicator highlighting the presence of bank-specific NCWO risk in the senior layer, obliging the SRB to take action to address risks to resolvability. The SRB determines a bank-specific subordination add-on equal to the difference between the exclusion ratio and the threshold of 10 percent, multiplied by the size of the senior layer and expressed in RWA. In addition, the SRB will also start identifying liabilities that may be excluded under Article 44(3) of the BRRD from a resolvability perspective.
- 32 In light of the TLAC Term Sheet, the SRB may grant a 2.5% allowance for senior instruments where the minimum percentage is 16%, or 2.2% where it is 14% under strict conditions ensuring that this does not have a material adverse impact on resolvability, and in all cases only where the proportion of mandatory excluded liabilities that rank *pari passu* with senior liabilities is less than 10%.

Eligible liabilities are included at Point-of-entry level

- 33 **Compliance with binding targets will be assessed against own funds at consolidated resolution group level, but eligible liabilities at point-of-entry level only.** The SRB considers a computation at the level of the point of entry, taking into account own funds instruments eligible for the group's consolidated own funds requirement issued either by the resolution entity itself or by subsidiaries within the resolution group. Eligible liabilities other than own funds are only counted towards the MREL if issued by the resolution entity to entities outside the resolution group. This approach, included for monitoring purposes in the previous statement of policy, is instrumental in ensuring a credible allocation of MREL resources within the group, in line with the application of resolution actions at the level of the point-of-entry.
- 34 **The SRB will specifically assess on a case-by-case basis the application of this approach to cooperative groups ⁽⁷⁾.** MREL-eligible liabilities issued by the central body but also by any of the entities contributing to the solidarity mechanism or similar mutual support schemes may count for the compliance with the binding targets under strict conditions. In addition, the SRB expects cooperative groups to consider issuing MREL-eligible instruments from the central body in order to ease the operationalization of bail-in.

Structured notes are mostly excluded

- 35 **Structured notes.** The SRB excludes structured notes by default. However, the SRB will assess on a case-by-case basis the eligibility of such liabilities:
- 1) where a given amount of the principal of the liability arising from the instrument is known in advance at the time of issuance, is fixed and is not affected by a derivative feature;
 - 2) if the instrument, including its derivative feature, is not subject to any netting agreement and its valuation is not subject to Article 49(3) of the BRRD; and
 - 3) only up to the amount of the liability that complies with point 1 (i.e. for the fixed floor of the liability that would have to be paid).

Liabilities issued to SPVs

- 36 **Banks should decrease their reliance on MREL funding through SPVs due to additional complexity for the implementation of bail-in.** The bail-in of intra-group liabilities between the resolution entity and the SPVs may be more complex than in a funding structure where instruments are issued by the resolution entity directly to external investors. This is particularly the case where a significant part of the MREL

⁽⁷⁾ Cooperatives are defined as a network or group or other credit institutions affiliated to a central body, in which the members are subject to a solidarity mechanism or similar mutual support scheme, as defined by national legislation or Regulation (EU) No 575/2013.

capacity is issued via SPVs. Banks should progressively decrease their reliance on these structures.

- 37 Therefore, liabilities of the resolution entity to the SPV shall not be MREL-eligible, except where the bank demonstrates to the satisfaction of the SRB that the specific features of the funding structure do not impair the credibility and feasibility of the operationalisation of the resolution strategy. All the other MREL eligibility criteria must also be met; in particular, the liabilities must not arise from a derivative and must not be owed to, secured by or guaranteed by the institution itself.

Non-covered non-preferred deposits breakable below one year are excluded

- 38 **The SRB will exclude non-covered non-preferred deposits if they can be withdrawn within a one-year period.** Some term deposits may have an early redemption clause that would have to be taken into account in the maturity assessment (Article 45(4) of the BRRD). In addition, according to the European Banking Authority, a 'deposit which is deposited for at least a year's period but which confers upon its owner a right to early reimbursement with less than one year's notice shall not be included in the amount of own funds and eligible liabilities meeting MREL ⁽⁸⁾. As a result, the SRB is asking banks to conduct credible analyses of these deposits and will review them to exclude from the eligible instruments all non-preferred non-covered deposits above one year that have a redemption clause below one year, even if penalties, whatever their magnitude, apply, or for which there is no sufficient evidence that they cannot be withdrawn.

Liabilities held by retail investors are MREL-eligible

- 39 **The SRB does not see any legal basis for resolution authorities to exclude ex ante and uniformly eligible liabilities held by natural persons or small and medium-sized enterprises from MREL or from bail-in.** The SRB is required to bail in retail investors in line with their ranking in the applicable creditor hierarchy, other than in exceptional circumstances, and cannot exclude instruments from MREL for the sole reason that they are held by retail investors should they otherwise meet the requirements for MREL. European Union (EU) legislation includes many safeguards to ensure financial products are sold to suitable investors only. The implementation and supervision of such rules is the responsibility of Member States' market authorities; therefore, any possible failure to comply with investor protection rules is not an argument to exclude these liabilities from the computation of MREL targets or, finally, bail-in.
- 40 **However, holdings of subordinated or senior instruments by retail investors could prove to be an impediment to resolution.** As part of the resolvability assessment, the SRB will analyse the bank's exposure to retail bondholders to assess

⁽⁸⁾ EBA Q&A 2015/2267.

whether the bail-in of these counterparties might be an impediment to resolvability. While acknowledging the benefits of diversification for funding purposes, large holdings of liabilities sold to retail investors could make banks difficult to resolve for various reasons, including (i) the potential loss of a bank's customer base and the risk of withdrawals and (ii) potential litigation brought by retail investors upon or after resolution, which might endanger the bank's future viability.

Liabilities issued under third country law

- 41 **The SRB excludes liabilities other than own funds governed by the laws of a country outside the EU, unless banks can demonstrate that write-down or conversion would be effective under the laws of that third country.** When liabilities are not governed by EU law, resolution authorities face the risk that the courts of the country with legal jurisdiction over the liabilities may not recognise the resolution actions of an EU resolution authority. In accordance with Article 45(5) BRRD, the SRB will not count towards the MREL any liability governed by the law of a third country unless a bank is able to demonstrate that the exercise of the write-down or conversion powers by the SRB and relevant NRAs of the Banking Union would be effective under the laws of that third country.
- 42 **Minimum conditions for demonstrating the effectiveness of contractual recognition.** In the absence of binding international agreements with third countries or statutory recognition ⁽⁹⁾ of the effect of a bail-in decision under the law of that third country, banks need (a) to demonstrate that the contract governing the liability contains a contractual recognition clause which, at a minimum, fully meets the requirements of Article 55 BRRD, and Commission Delegated Regulation 2016/1075, and that no other contractual term or arrangement impairs the effectiveness and enforceability of the clause; and (b) to provide a legal opinion confirming the former, and otherwise meeting the minimum criteria as defined in Annex I ⁽¹⁰⁾, which will inform the SRB's assessment, paying due attention to horizontal consistency to ensure a level playing field. The SRB reserves the right not to request a legal opinion, for instance, where it deems that the proportion of issuances governed by the laws of third countries of the MREL-eligible stock of a bank is not significant and the SRB has sufficient elements to conclude for the eligibility of such liabilities.
- 43 **Exogenous risks to resolvability may impact eligibility.** The SRB will include these liabilities in MREL calculations only if and as long it is satisfied that exogenous circumstances of the third country legal order which cannot be remedied through contractual arrangements do not put the effective exercise of the write-down and

⁽⁹⁾ Powers granting discretion to an authority as whether to grant recognition to foreign resolution proceedings at the point of resolution do not ensure resolvability ex ante.

⁽¹⁰⁾ For new issuances. With regard to legal opinions already provided to the SRB not fully meeting the minimum criteria, the SRB will decide on a case-by-case basis.

conversion powers in respect of these instruments at risk. Such circumstances may for example arise from court rulings denying recognition on grounds of public policy, or securities laws making conversion infeasible; their existence will not be assumed by the SRB *ex ante* without concrete indication, but may lead the SRB to exclude all liabilities under a given governing law from MREL calculations following a change in the SRB's assessment of exogenous risks to resolvability.

- 44 **The responsibility for ensuring that liabilities preserve their eligibility rests with banks, which should also consider issuing under the governing law of an "EU27" ⁽¹¹⁾ country.** With a view to mitigate exogenous risks to resolvability which may lead to an exclusion of liabilities from MREL calculations, banks are encouraged to adhere to market practices for new issuances such as variation or substitution clauses, or subjecting the recognition clause to "EU27" law, all of which are able to increase the level of comfort on the effective enforceability of the bail-in clause. To achieve legal certainty, banks should also consider issuing under the governing laws of a "EU27" country.
- 45 **The SRB will evaluate liabilities governed by the law of a third country that qualify as own funds instruments from a resolvability perspective.** For the purpose of the MREL computation, the SRB treats own fund instruments governed by the law of a third country in alignment with their eligibility under the current CRR. Nonetheless, the SRB recalls the obligation for banks under Article 55 BRRD to include contractual clauses into AT1 and T2 instruments governed by third country law. The significant presence of such instruments without a clause may cause difficulties in resolution where they impact the total loss-absorbing capacity of the institution, and NCWO risks could be of particular concern if present in this part of the capital structure. Therefore, the SRB will assess any such risk in its resolvability assessment, and request to take corrective action if required.

MREL in the context of Brexit

- 46 **The impact of Brexit on recognition of resolution action and related MREL eligibility may differ depending on which scenario materialises, which is uncertain at the date of publication.** The SRB monitors the evolution of the stock and issuances of liabilities governed by UK law in the context of Brexit. Such liabilities are MREL-eligible based on the application of the current legal framework, and would continue to be so during the transition period ending on 31 December 2020 as foreseen under the draft agreement on the withdrawal of the UK from the EU. The ratification of the withdrawal agreement, as well as the specifics of the status of recognition of

⁽¹¹⁾ Member States of the EU with the exception of the United Kingdom in the context of Brexit, see also next Section.

resolution action after the transition period or in other exit scenarios including a no-deal scenario, are unknown at the date of publication.

- 47 **Banks are expected to tackle proactively the possible impact of Brexit.** Banks are expected to include contractual recognition clauses in the new issuances of MREL-eligible instruments in accordance with Article 55 of the BRRD and be prepared to demonstrate that any decision of a “EU27” resolution authority would be effective in the future. In addition, banks are expected to consider issuing MREL-eligible instruments under the “EU27” governing laws to achieve legal certainty with regards to their loss-absorbing capacity ⁽¹²⁾.
- 48 **The SRB will treat Brexit-induced shortfalls on a case-by-case basis.** In the case that banks have an MREL shortfall as a consequence of issuances governed by the laws of the UK being rendered ineligible, or where a significant stock of such liabilities could affect resolvability (e.g. if such liabilities could not be exposed to losses but rank *pari passu* with MREL eligible liabilities negatively impacting the NCWO risk), the SRB will consider each situation on a case-by-case basis, while ensuring consistency across all banks under its remit. This may, in specific cases, entail new or an extension of transition periods for banks having MREL shortfalls as a consequence of ineligibility of the issuances governed by the law of the UK for MREL purposes. Banks are expected to engage in a dialogue with the SRB on their MREL issuance planning to address possible shortfalls in line with the SRB MREL policy and/or on the potential impact on resolvability related to their stock of instruments intended to be eligible to meet the MREL target.

C — TARGETS AT INDIVIDUAL LEVEL - CALIBRATION

Binding targets will be set for relevant subsidiaries

- 49 **Binding decisions on MREL at individual level will be taken for entities meeting relevance criteria.** In a view to ensure a sufficient quantum of loss absorbing capacity in all parts of the resolution group, the SRB will issue binding targets at the individual level to subsidiaries of banking groups considered as relevant legal entities (RLEs), representing or providing more than 5% of the group's total risk exposure amount or leverage exposure or total operating income; or providing critical functions.
- 50 **The SRB will expand the scope in future cycles.** The focus on RLEs in this planning cycle shall not prevent banks from implementing an internal MREL mechanism encompassing other entities included in the resolution group. The SRB intends to

⁽¹²⁾ See also the SRB position paper dated 15 November 2018 ([link](#)) and the expectations of the EBA stated in its Opinion of 25 June 2018 (EBA/Op/2018/05).

expand, in future cycles, the scope to other subsidiaries not yet covered by a formal decision.

- 51 **The SRB may exempt certain subsidiaries from individual MREL targets under the conditions set by the legal framework.** While mortgage credit institutions are exempted from individual MREL targets by law subject to Art. 45.3 BRRD, other subsidiaries may be waived from MREL on a case-by-case basis, without automaticity. The SRB will assess the possibility to grant a waiver in line with the conditions set by the applicable legislation, with a particular focus on the presence of practical or legal impediments to the transfer of funds within the group in a resolution context. The SRB will pay particular attention to the interplay with supervisory requirements and the possible impact of waivers on the resolution strategy.

Bank-specific calibration following the general approach and the applicable group resolution strategy

- 52 **Calibration of individual targets generally follows the methodology for consolidated targets.** The calibration of individual targets is based on the same provisions applicable for consolidated targets. The default amounts for the LAA, RCA and MCC are calculated taking into account the relevant prudential requirements at individual level (P2R, buffers) so as to apply the default formula.

TARGETS AT INDIVIDUAL LEVEL - ELIGIBILITY

Eligibility criteria for individual MREL follows the applicable legal framework

- 53 **Eligibility criteria for external MREL apply.** As the BRRD applies to all forms of MREL instruments, all criteria set out in Art. 45 BRRD should apply both to consolidated and individual MREL targets. That is, these instruments must comply with the criteria set out in Articles 44 and 45 BRRD, as well as all relevant SRB criteria (e.g. third country law, etc.). In particular, prepositioning the amount of instruments corresponding to the target is mandatory given that eligible instruments must be issued and fully paid-up in accordance with Art. 45(4)(a) BRRD.

Banks are expected to prepare for the future regime

- 54 **Eligibility criteria set out in BRRD for individual MREL targets will be complemented by expectations towards banks on internal MREL features.** The eligibility criteria currently foreseen in BRRD will be the basis for enforcement of the individual requirements. However, to ensure that banks move towards the implementation of a fully-fledged internal MREL mechanism, the SRB will communicate expectations, on an informative basis, complementing the criteria set out in Art. 44 and 45 BRRD. This informative guidance is aligned as closely as possible with eligibility

for internal MREL as foreseen in the forthcoming “Banking Package” to enhance the internal loss absorbing capacity of the group, making SPE strategies more robust and preparing banks for the future legal framework.

- 55 **The SRB expects banks to build a proper internal MREL mechanism where issuances are directed towards group entities or other existing shareholders⁽¹³⁾.** In this context, liabilities of the subsidiary eligible for internal MREL should be issued to and bought by the resolution entity either directly or indirectly through other intermediate entities in the same resolution group or by an existing shareholder of the subsidiary that is not part of the same resolution group as long as the exercise of the power of write down or convert would not affect the control of the subsidiary by the resolution entity.
- 56 **The SRB recognises instruments issued indirectly to the resolution entity along the chain of ownership.** The SRB will assess whether there are any legal and technical obstacles preventing the subsidiary from transferring losses up to the resolution entity. The transferability of losses throughout the resolution group should be assessed so as to provide assurance that indirect issuances are not an impediment to resolvability.
- 57 **Instruments eligible for internal MREL are expected to be subordinated to all operating liabilities.** This condition allows the subsidiary to continue to operate and perform its critical functions. Subordination of internal MREL is necessary to upstream losses to the resolution entity without breaching the NCWO principle at the level of the resolution entity.
- 58 **Subordination to externally issued instruments.** In addition, to ensure the feasible and credible upstreaming of losses to the resolution entity, eligible instruments for internal MREL are expected to be subordinated to instruments issued by the subsidiary to external investors other than the existing shareholders of the subsidiary. Within a resolution group, the losses arising in the subsidiary should be borne by the holders of the subsidiary’s own funds (i.e. the resolution entity, other entities part of the resolution group following the shareholding structure and external minority shareholders, if relevant) ahead of external creditors.

D – TRANSITION PERIODS

Bank-specific transition periods will support banks’ efforts to reach MREL targets

⁽¹³⁾ Including minority or joint shareholders.

- 59 **Binding MREL targets are set with a bank-specific transition period.** The SRB has decided to continue setting, as a general rule, individual transition periods of up to a maximum of four years for consolidated as well as individual MREL targets. The transition periods are defined based on quantity (target) and quality (subordination level) requirements to pave the way for building up banks' loss-absorbing and recapitalisation capacities. The transition periods take into account bank- and market-specific characteristics. For banks that already meet the binding target, there will generally be no transition period.
- 60 **In addition, the SRB will set non-binding interim targets to ensure the feasibility of reaching the target at the end of the transition period ⁽¹⁴⁾.** The SRB may need to adjust future transition periods, shortening or lengthening them depending on the applicable conditions. The SRB expects banks to reach the interim targets and will closely monitor, with national resolution authorities of the Banking Union, compliance with the MREL decisions.
- 61 **Banks will be requested to provide an implementation and monitoring plan** to ensure that the SRB has the necessary information to verify compliance with its decisions, forecast future evolution of MREL levels, and monitor the development of the group's internal monitoring and control framework.
- 62 **Furthermore, additional reporting obligations will be progressively imposed in order to increase the frequency of submission of the Liability Data Reports.** In the meantime, ad hoc requests will be foreseen by the SRB to collect necessary data directly from banks to fulfil SRM monitoring duties, in particular with respect to the issuances of MREL-eligible instruments.

CONCLUSION AND NEXT STEPS

- 63 **The 2018 SRB policy for banks pertaining to the second wave of resolution plans refines the MREL 2017 approach and introduces a series of new elements strengthening the function of MREL as key tool to achieve resolvability.** By introducing a reduced perimeter of eligible instruments for consolidated targets, binding subordination requirements at increased levels, binding targets at individual level, and an additional step to tailor MREL to transfer strategies, the SRB is raising the bar in terms of bank resolvability and MREL targets to prepare the ground for future regulatory changes in the context of the introduction of the "banking package".

⁽¹⁴⁾ Interim targets are expressed as a percentage of total liabilities and own funds, in order to monitor compliance with the binding reference of the MREL decision (RWA and nominal amount can be used for information purposes).

- 64 **The SRB will review this statement of policy for MREL setting in 2019 on the basis of the final legislative outcomes of the “Banking Package”**, and reserves the right to update its policy upon the publication of CRR2/BRRD2/SRMR2 in the Official Journal of the EU, with the aim of charting a consistent path and preparing banks to transition to the new regime, as well as to reflect any change necessary due to those requirements potentially coming into force already in 2019.
- 65 **MREL decisions are reviewed annually.** In accordance with the legislation, the SRB will continue revising the applicable MREL targets and transition periods as part of the future resolution planning cycles. In particular, the SRB will take into consideration any change stemming from supervisory decisions or linked to the evolution of banks’ risk profiles and overall structures.
- 66 **The monitoring of compliance with binding MREL decisions will require ongoing engagement with banks.** The SRB will request banks to provide implementation and monitoring plans, as well as enhance their reporting capacity to address both a future increased frequency of LDR submissions, as well as ad hoc obligations to report on the issuances of MREL-eligible instruments.



ANNEX I

MINIMUM REQUIREMENTS FOR A LEGAL OPINION UNDER ART. 55(1) BRRD READ IN CONJUNCTION WITH ART. 45(5) BRRD AND 12(17) SRMR

The legal opinion shall:

1. Be reasoned and indicate whether the bail-in clause fully complies with Art. 44 of Commission Delegated Regulation 2016/1075, detailing the criteria set forth therein.
2. Take into account not only the general enforceability of the standard/template clause but also, to the extent relevant, all specific circumstances, rules governing the actual programme/offering/issuance, and ensure that no other contractual term or arrangement may impair the effectiveness and enforceability of the clause.
3. Include an analysis of possible impediments to the effectiveness and enforceability of the clause, drawing from insolvency law, securities law and the general legal framework of the third country jurisdiction, such as public policy.
4. Include an assessment on the effectiveness of the clause in case of non-coincidence of jurisdiction and governing law (i.e. if the chosen court (the jurisdiction) is called to apply a foreign law), particularly in terms of how in practice the chosen forum will apply the governing law.



Single Resolution Board

Treurenberg 22, 1049 Brussels

<https://srb.europa.eu/>