

EBA/CP/2020/16

24 July 2020

Consultation Paper

Draft Regulatory Technical Standards on specifying the methodology to be used by resolution authorities to estimate the requirement referred to in Article 104a of Directive 2013/36/EU and the combined buffer requirement for resolution entities at the resolution group consolidated level for the purpose of setting MREL under BRRD Art. 45c(4)

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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 24 October 2020. 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 (EU) 1725/2018 of the European Parliament and of the Council of 23 October 2018. Further information on data protection can be found under the Legal notice section of the EBA website.

2. Executive Summary

Pursuant to Article 45e(1) of Directive 2014/59/EU (BRRD), resolution entities shall comply with MREL on a consolidated basis at the level of the resolution group. However, MREL is calibrated on the basis of going-concern capital requirements that are, for some, set at group level – with a perimeter that differs from the resolution group’s perimeter. The difference, in some cases, can be particularly significant - for groups with a multiple point of entry strategy for instance- and thus lead to group capital requirements that may under or over estimate the risks within a resolution group.

Currently resolution authorities will typically use the group capital requirements to calibrate MREL at resolution group level. The legislator, in Article 45c(4) of BRRD, tasked the EBA with developing a methodology for authorities to estimate the capital requirements to be used as an input for calibrating MREL.

This consultation paper puts forward this methodology as a draft technical standard and invites responses to specific questions.

The methodology, developed in consultation with competent authorities, relies first on the introduction of a threshold to only capture resolution groups that sufficiently differ to the prudential group. In a second time, the methodology aims to be pragmatic by combining a top down and bottom-up approach to estimating pillar 2 and combined buffer requirements (CBR).

The proposed methodology aims to minimise the burden on resolution authorities while creating a positive dynamic between banks, resolution and competent authorities to improve the calibration of MREL at resolution group level – where those differ from prudential groups.

Next steps

The finalisation of the draft RTS and communication to the European Commission is planned by December 2020 - in line with the EBA risk reduction measure roadmap published in November 2019¹.

¹ <https://eba.europa.eu/eba-publishes-its-roadmap-risk-reduction-measures-package>

3. Background and rationale

3.1 Background

Directive 2014/59/EU (BRRD) establishes a framework for the recovery and resolution of credit institutions, investment firms and related entities. In this framework, resolution authorities, after consulting the relevant competent authorities, shall ensure that institutions meet at all times a minimum requirement for own funds and liabilities eligible for bail-in (MREL).

The primary objective of MREL is to allow the recapitalisation of a resolution, that is, to ensure it is able to report capital levels above its minimum capital requirement – sufficiently to generate confidence. This is why, as per Article 45c(3), (5) or (7), MREL is calibrated using the minimum capital requirement and buffers applicable to a banking group or the relevant entity.

Article 45e(1) of BRRD specifies that MREL is set at resolution group level, however in certain cases, the perimeter of the resolution group differs from the perimeter of the banking group. This in particular, can be the case with multiple point of entry resolution strategies which foresee the split-up of the banking group into several distinct entities post-resolution. But it can also be the case for SPE banking groups, for example where the point-of-entry deviates from the top parent company. In those cases, because capital requirements are set at the prudential group level and thus may not effectively reflect the risk at the level of the resolution group.

So far, resolution authorities have generally used the capital requirements for the group to which the resolution group belong to calibrate MREL.

A policy option to address this issue would be to require competent authorities to align the prudential with the resolution group perimeter. However, this option was considered too costly by the co-legislators, as prudential perimeters will reflect on-going business needs, while resolution perimeter might differ.

Instead, the EBA was tasked with developing a methodology for resolution authorities to estimate capital requirements and combined buffer requirements to use as an input when calibrating MREL. The EBA, in collaboration with EU resolution authorities, and in consultation with competent authorities, has developed an approach based on the following objectives:

- a. Avoid require sub-consolidation at resolution group level
- b. Avoid confusion regarding the roles between resolution authorities and supervisors in relation to capital setting
- c. Create a framework for a dialogue between the bank, the relevant competent and resolution authorities to improve the accuracy of the estimate over time
- d. Be straightforward and avoid overburdening resolution authorities
- e. Avoid preventing further adjustments as per usual MREL setting process

3.2 Proposed approach

The proposed approach aims to focus on resolution groups that are significantly different from the prudential group on which capital requirements have been set.

When developing the technical standard it became apparent that some resolution groups do differ from the prudential group but only marginally. Typically, the prudential perimeter will not include a holding company that is part of the resolution group. While technically different the risk inherent to the two perimeters are not significantly different.

To ensure that this methodology only captures resolution groups where an estimation of P2 and CBR is effectively needed it was decided to introduce a materiality threshold of 5%. The threshold is meant to express the difference between the total risk exposure measure of the resolution group and the banking group or entity closest in size for which own funds requirements have been effectively set by the competent authority. This level was chosen both based on existing materiality threshold considered in resolution international standards (e.g. TLAC term-sheet) and following a survey with resolution authorities that confirmed the effectiveness of the proposed threshold.

Question for the Public Consultation: Do you agree with the proposed 5% materiality threshold?

If a resolution group is more than 5% different in terms of TREA from either the overall banking group or from the main entity for which an additional own fund requirement (P2R) has been set, then two main ways of estimating the resolution group capital requirements for the purpose of setting MREL are proposed.

A top-down approach, where the resolution authorities should seek to adjust the group requirement, or the one to which the resolution group is the closest, and for which a capital requirement has been set : under this approach the adjustments should only be done on the basis of the input provided by the competent authority – e.g. the part of the group P2 requirement that is driven by an entity or a type of risk outside of the resolution group. The rationale for limiting the possibility of adjustment to this input aims to ensure that the capital-setting responsibility remains with competent authorities – authorities who, following resolution, would need to authorise the resolved entity or group. If no input for adjustment is provided by the competent authority then the resolution authority uses the group requirement to calibrate MREL at the resolution group level.

A bottom-up approach, to be used in cases where at least one of the solo requirement set on entities comprising the resolution group is higher than the group requirement. The view is that varying levels of capital requirements is indicative of risks that are not homogenous within the group. In such case, the resolution authority should calculate the weighted average of the individual pillar 2 requirements – and apply it only if it is higher than the adjusted group requirement.

Question for the Public Consultation: Do you agree with the proposed approach to estimating pillar 2?

With regard to the estimation of the combined buffer requirement the proposed approach is equally straightforward and proportionate. Under the proposed methodology, the following would apply:



For the GSII buffer, the proposal is to keep the GSII buffer as an input to computing MREL. However, as per BRRD article 45c(3) 7 subparagraph, this leaves the possibility for the resolution authority to adjust the CBR when calibrating based on the resolution plan and thus not to apply the GSII buffer.

For the OSII buffer, the proposal is to use as an input to calibrate MREL the buffer of either the banking group or largest entity constituting the resolution group – whichever is the closest in size. Again, the level of the OSII buffer can be adjusted up or down by the resolution authority as per BRRD article 45c(7) paragraph 6.

As for the OSIIS buffer, the proposal for the Systemic Risk buffer is to use as an input to calibrate MREL the buffer of either the banking group or largest entity constituting the resolution group – whichever is the closest in size. Again, the level of the OSII buffer can be adjusted up or down by the resolution authority as per BRRD article 45c(7) paragraph 6.

No estimation methodology is proposed for both the capital conservation buffer and the countercyclical buffer. This is because the former is not bank specific and would be simply set at the consolidated resolution group level and the latter is not included in the MREL calibration.

Question for the Public Consultation: Do you agree with the proposed approach to estimating Combined buffer Requirement?

4. Draft regulatory technical standards

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE DELEGATED ACT

Article 45c (4) of Directive 2014/59/EU as amended by Directive (EU) 2019/879 ('the Directive') empowers the Commission to adopt, following submission of draft regulatory technical standards by the European Banking Authority (EBA), and in accordance with Articles 10 to 14 of Regulation No (EU) 1093/2010, delegated acts specifying the methodology to be used by resolution authorities to estimate the requirement referred to in Article 104a of Directive 2013/36/EU and the combined buffer requirement for resolution entities at the resolution group consolidated level where the resolution group is not subject to those requirements under that Directive.

In accordance with Article 10(1) of Regulation No (EU) 1093/2010 establishing the EBA, the Commission shall decide within three months of receipt of the draft regulatory technical standards whether to endorse the drafts submitted. The Commission may also endorse the draft standards in part only, or with amendments, where the Union's interests so require, having regard to the specific procedure laid down in those Articles.

2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT

In accordance with the third subparagraph of Article 10(1) of Regulation No (EU) 1093/2010, the EBA has carried out a public consultation on the draft regulatory technical standards submitted to the Commission in accordance with Article 45c (4) of Directive 2014/59/EU as amended by Directive (EU) 2019/879. A consultation paper was published on the EBA internet site on xx 2020 and the consultation closed on xx [month in letters] 2020. Moreover, the EBA invited the EBA's Banking Stakeholder Group set up in accordance with Article 37 of Regulation No (EU) 1093/2010 to provide advice on them. Together with the draft regulatory technical standards, the EBA has submitted an explanation on how the outcome of these consultations has been taken into account in the development of the final draft technical standards submitted to the Commission.

Together with the draft technical standards, and in accordance with the third subparagraph of Article 10(1) of Regulation No (EU) 1093/2010, the EBA has submitted its Impact Assessment, including its analysis of the costs and benefits, related to the draft regulatory technical standards submitted to the Commission. This analysis is available at... [insert here the link to the 'regulatory activity page' of the relevant RTS- to be provided by Communications colleagues], pages [xx-xx] of the Final Draft Regulatory Technical Standards package.

3. LEGAL ELEMENTS OF THE DELEGATED ACT

[Provide a *summary* of the main provisions of the draft TS].





COMMISSION DELEGATED REGULATION (EU) .../..
of XXX

supplementing Directive 2014/59/EU the European Parliament and of the Council with regard to regulatory technical standards specifying the methodology to be used by resolution authorities to estimate the requirement referred to in Article 104a of Directive 2013/36/EU and the combined buffer requirement for resolution entities at the resolution group consolidated level where the resolution group is not subject to those requirements under that Directive for the propose of Article 45c(4) of Directive 2014/59/EU..

(Text with EEA relevance)

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 and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012², and in particular Article 45c(4) thereof,

Whereas:

- (1) The additional own funds requirement referred to in Article 104a of Directive 2013/36/EU of the European Parliament and of the Council³ and the combined buffer requirement defined in Article 128, first subparagraph, point (6), of that Directive are inputs to calculate the loss absorption and recapitalisation amounts set out in Article 45c(3) of Directive 2014/59/EU. Those requirements are to be used by resolution authorities to set the minimum requirement for own funds and eligible liabilities ('MREL') referred to in Article 45(1) of that Directive.
- (2) According to Article 45e(1) of Directive 2014/59/EU, resolution entities are to comply with MREL on a consolidated basis at the level of the resolution group. Article 2(1), point (83b), points (a) and (b), of Directive 2014/59/EU define a resolution group as a resolution entity and its subsidiaries that are neither resolution entities themselves, nor subsidiaries of other resolution entities, or as credit institutions permanently affiliated to a central body and central body itself when at least one of those credit institutions or the central body is a resolution entity, and their respective subsidiaries. A resolution group may thus not always be identical to

² OJ L 173, 12.6.2014, p. 190.

³ Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment funds, amending Directive 2002/87/EC and repealing 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).



a group as defined in Article 2(1), point (26), of Directive 2014/59/EU, in particular when a group is composed of more than one resolution groups. The additional own funds requirement referred and the combined buffer requirement apply to the Union parent institution at the group consolidated level in accordance with Article 11 of Regulation (EU) 575/2013, but might not apply to the resolution entity at the resolution group consolidated level because the resolution group might not cover the entire group. It is therefore necessary to specify a methodology for estimating those requirements for that situation.

- (3) Where the total risk exposure amount of a resolution group represents almost the entirety of the risk exposure amount of a group, it is an indication that the risks or elements of risks present in that resolution group do not materially differ from those present in the group. In that case, the resolution authority should use the additional own funds requirement applying to the Union parent institution at the group consolidated level as an estimation of the additional own funds requirement, when calibrating the minimum requirement for own funds and eligible liabilities applying to the resolution entity at the resolution group consolidated level.
- (4) Likewise, where a resolution group can almost entirely be attributed to one entity of that resolution group, this is an indication that the risks or elements of risks present in that resolution group are not materially different from those present in that entity of the resolution group. Accordingly, where the total risk exposure amount of the resolution group does not differ significantly from that of the largest entity of that resolution group, then the resolution authority should use the additional own funds requirement of that largest entity as an estimation for the additional own funds requirement when calibrating the MREL for the resolution entity at the resolution group consolidated level.
- (5) Resolution authorities should use different estimations for the additional own funds requirement of the resolution entity at the resolution group consolidated level in other circumstances. For instance, where a resolution group is more complex and its specificities cannot be fully captured by mirroring the additional own funds requirement applying either to the Union parent institution at the group consolidated level or to the largest entity of the resolution group. Where the additional own funds requirement applying to the Union parent institution at the group consolidated level is higher than the additional own funds requirement of each entity of the resolution group, the additional own funds requirement applying to the Union parent institution at the group consolidated level should serve as a basis for estimating the additional own funds requirement of the resolution entity at the resolution group consolidated level. Resolution authorities should, on the basis of information provided by the competent authority, seek to adjust that estimation. This is to reflect the specific risks of the resolution group compared to the risks of the Union parent institution at the group consolidated level. That adjustment should take into account that some risks



of the resolution group may not be present in other entities of the group that are not part of the resolution group or that some risks that are present in those entities of the group are not present in the resolution group itself.

- (6) The circumstance where one or more individual requirements within the resolution group are higher than the additional own fund requirement applying to the Union parent institution at the group consolidated level is an indication of idiosyncratic risks or elements of risk within the resolution group. Those idiosyncratic risks or elements of risk may be less important when considered across the group at consolidated level, for example because they may be offset by countervailing risk factors outside of the resolution group. To estimate the additional own funds requirement of the resolution entity at the resolution group consolidated level, the resolution authority should thus, whenever such circumstance occurs, compare the result of the estimation based on adjustments to the additional own funds requirement applying to the Union parent institution at the group consolidated level with an estimation based on a weighted average of the additional own fund requirements of all entities of the resolution group. The resolution authority should use as an input to compute MREL the estimation that delivers the higher requirement.
- (7) For more complex groups, resolution authorities, should where possible, on the basis of elements provided by the competent authority adjust the additional own fund requirement of the Union parent institution at the group consolidated level to reflect that some risks or elements of risk covered by that additional own funds requirement are not relevant to the resolution group concerned, for instance because of their nature or geographical location. Resolution authorities should also, where possible on the basis of elements provided by the supervisory authority, make adjustments to that requirement to take into account that some risks or elements of risk of the resolution group are not fully reflected in that requirement or are netted within it, but are nevertheless relevant to the resolution group. All adjustments should be based on information provided by the relevant competent authorities, where available, since those authorities are responsible for estimating the ongoing risks to which entities of a group are exposed. Where such adjustments are not possible, the resolution authority shall use the unadjusted requirement.
- (8) The capital conservation buffer rate does not vary across institutions. That rate should therefore be used as an estimation of the capital conservation buffer of the resolution entity at the resolution group consolidated level.
- (9) In order to reflect the planned structure of the group after the implementation of the preferred resolution strategy, buffer requirements aimed to address systemic risk (GSII, OSII and systemic risk buffer) should by default be deemed to be identical to the requirements set on the basis which is the closest, in terms of total risk exposure amount, to the resolution group.



- (10) According to Article 45c(3), first subparagraph, point (a), point (ii), of Directive 2014/59/EU, the recapitalisation amount is the amount that allows the resolution group resulting from resolution to restore compliance with, among others, the additional own funds requirement at the consolidated resolution group level after the implementation of the preferred resolution strategy. According to Article 45c(3), seventh subparagraph of Directive 2014/59/EU, the amount necessary to ensure that, following resolution, the resolution entity is able to sustain sufficient market confidence for an appropriate period is to be equal to the combined buffer requirement, that is to apply after the application of the resolution tools less the countercyclical capital buffer. The recapitalisation amount, including the amount to sustain market confidence, is a part of the MREL and may be adjusted downwards or upwards under Directive 2014/59/EU to reflect the changes to the resolution group after the application of the resolution tools. Accordingly, only the additional own funds and combined buffer requirements applied to the resolution entity at the resolution group consolidated level that are used to calibrate the MREL should be estimated, but that estimation should be without prejudice to any adjustments to the recapitalisation amount, including its amount to sustain market confidence, when setting the MREL under Directive 2014/59/EU.
- (11) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority to the Commission.
- (12) 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 of the European Parliament and of the Council⁴,

HAS ADOPTED THIS REGULATION:

Article 1

Estimation of the additional own funds requirement

1. Where a resolution entity has not been subject to an additional own funds requirement at the resolution group consolidated level, resolution authorities shall estimate that requirement in accordance with paragraphs 2 to 7 to use as an input when computing MREL at the resolution consolidated level.

⁴ Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

2. Where the total risk exposure amount of the resolution entity at the resolution group consolidated level differs by 5% or less to the total risk exposure amount of the Union parent institution at the group consolidated level. Then resolution authorities shall use the additional own funds requirement imposed on the Union parent institution at the group consolidated level as an estimation of that requirement for computing MREL for the resolution entity at the resolution group consolidated level.
3. Resolution authorities shall use as an estimation for the additional own funds requirement of the resolution entity at the resolution group consolidated level the additional own funds requirement of the entity accounting for the largest proportion of the consolidated total risk exposure amount of the resolution group where all of the following applies:
 - a) the total risk exposure amount of the resolution entity at the resolution group consolidated level differs by more than 5 % from the total risk exposure amount of the Union parent institution at the group consolidated level;
 - b) the total risk exposure amount of the resolution entity at the resolution group consolidated level is equal to, or differs by less than 5 %, from the individual total risk exposure amount of the entity accounting for the largest proportion of the consolidated total risk exposure amount of the resolution group;
 - c) the additional own funds requirement of the entity accounting for the largest proportion of the consolidated total risk exposure amount of the resolution group is greater than zero.
4. Where paragraphs 2 and 3 do not apply and none of the entities that are part of the resolution group are subject to a higher additional own funds requirement than the additional own funds requirement imposed on the Union parent institution at the group consolidated level, resolution authorities shall use as an estimation for the additional own funds requirement of the resolution entity at the resolution group consolidated level the additional own funds requirement imposed on the Union parent institution at the group consolidated level, subject to the adjustments referred to in Article 2.
5. Where paragraphs 2 and 3 do not apply and one or more of the entities that are part of the resolution group are subject to a higher additional own funds requirement than the additional own funds requirement imposed on the Union parent institution at the group consolidated level, resolution authorities shall use as an estimation for the additional own funds requirement of the resolution entity at the resolution group consolidated level the higher of the following:
 - (a) the additional own funds requirement imposed on the Union parent institution at the group consolidated level subject to the adjustments referred to in Article 2;



- (b) the sum of the products of the additional own funds requirements of the entities of the resolution group and the respective individual total risk amounts of those entities divided by the sum of the individual total risk exposure amounts of those entities.
6. For the purposes of paragraph 5, point (b), where no waiver has been granted in accordance with Part One, Title II, Chapter 2, Sections 2 and 3 of Regulation (EU) No 575/2013, and no additional own funds requirement has been imposed on an entity on an individual basis, the additional own funds requirement of that entity shall be zero.
7. For the purposes of this Article, the total risk exposure amount shall be calculated in accordance with paragraphs 3 and 4 of Article 92 of Regulation (EU) 575/2013 and on an individual or consolidated basis, as applicable.

Article 2

Adjustments for the estimation of the additional own funds requirement

1. For the purposes of Article 1(4) and of Article 1(5), point (a), resolution authorities shall, after consulting the relevant competent authority, adjust their estimation of the additional own funds requirement of the resolution entity at the resolution group consolidated level in any of the following cases:
- a) some of the risks or elements of risk, for the coverage of which the additional own funds requirement was imposed on the Union parent institution at the group consolidated level by the competent authority in accordance with Directive 2013/36 Article 104(1)a, are not present in the resolution group concerned;
- b) some risks or elements of risk for the coverage of which no additional own funds requirement was imposed on the Union parent institution at the group consolidated level - by the competent authority in accordance with Directive 2013/36 Article 104(1)a - are present in that resolution group.
2. Adjustments shall not take place where the resolution authority, after having consulted the competent authority and having taken into account the information provided by the competent authority, determines that no significant risk is not relevant to the resolution group concerned or has not been taken into account.

Article 3

Methodology for the estimation of the combined buffer requirement of resolution entities

1. The estimation of the combined buffer requirement of the resolution entity at the resolution group consolidated basis shall be the sum of the buffer requirements referred to in Article 129(1), paragraphs 4 and 5 of Article 131 and Article 133(4) of



Directive 2013/36/EU, as applicable, as estimated in accordance with paragraphs 2 to 4 of this Article.

2. Resolution authorities shall use as an estimation for the capital conservation buffer requirement referred to in Article 129(1) of Directive 2013/36/EU for the resolution entity at the resolution group consolidated level the capital conservation buffer requirement imposed on the Union parent institution at the group consolidated level.
3. Resolution authorities shall use as an estimation for the ‘G-SII buffer’ requirement referred to in Article 131(4) of Directive 2013/36/EU for the resolution entity at the resolution group consolidated basis the ‘G-SII buffer’ requirement imposed on the Union parent institution at the group consolidated level.
4. Resolution authorities shall use as an estimation of the ‘O-SII’ buffer requirement referred to in Article 131(5) of Directive 2013/36/EU for the resolution entity at the resolution group consolidated level the ‘O-SII’ buffer requirement imposed on the Union parent institution at the group consolidated level. Where the ‘O-SII’ buffer requirement has also been set at another level of consolidation than at the group level, resolution authorities shall use as an estimation for that requirement the ‘O-SII’ buffer requirement set at the level of consolidation that is the closest to the total risk exposure amount of the resolution group.
5. Resolution authorities shall use as an estimation of the systemic risk buffer requirement referred to in Article 133(4) of Directive 2013/36/EU for the resolution entity at the consolidated resolution group level the systemic risk buffer requirement imposed on the Union parent institution at the group consolidated level in accordance with Article 133(4) of Directive 2013/36/EU. Where a systemic risk buffer has also been set at another level of consolidation than at the group level, resolution authorities shall use as an estimation for that requirement the systemic risk buffer requirement set at the level of consolidation that is closest to the total risk exposure amount of the resolution group.

Article 4

Entry into force.

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

On behalf of the President

[Position]

5. Accompanying documents

5.1 Draft cost-benefit analysis / impact assessment

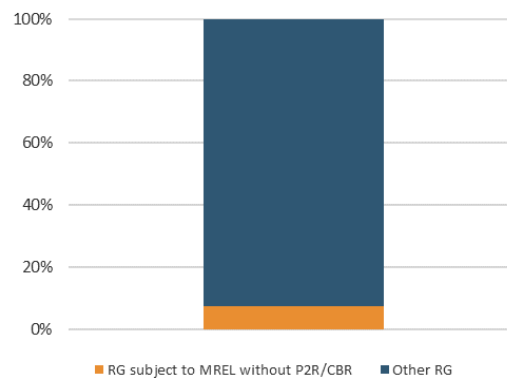
2. Article 45c(4) of the BRRD2 requires the EBA to develop draft RTS specifying the methodology to be used by resolution authorities to estimate prudential requirements for resolution entities at the resolution group consolidated level where the resolution group is not subject to those requirement under Directive 2013/36/EU (CRD IV).
3. As per Article 10(1) of Regulation (EU) No 1093/2010 (EBA Regulation), any regulatory technical standards developed by the EBA shall be accompanied by an Impact Assessment (IA), which analyses ‘the potential related costs and benefits’.
4. This section presents the cost-benefit analysis of the main policy options included in the RTS described in this CP. The IA draws from data collected from resolution authorities by the *BRRD2 mandates – Pillar 2 estimate* survey (P2R survey).

A. Problem identification

5. Resolution entities are required to comply with minimum requirement for own funds and eligible liabilities (MREL) on a consolidated basis at the level of the resolution group. The calculation of MREL is based on the formulae in Article 45c(3) BRRD2 and includes as components prudential requirements defined in CRD IV, namely the additional own funds requirement (P2R) according to Article 104a of CRD IV and the combined buffer requirement (CBR) according to Article 128 first sub-paragraph, point (6) of CRD IV.
6. These prudential requirements are set by competent authorities for the Union parent institution at the group consolidated level (consolidated banking group) and at individual and sub-consolidated levels of entities within the banking group, where no waivers or exemptions apply.
7. Resolution groups, however, are defined in accordance with the preferred resolution strategy, and might deviate from the prudential perimeter. They therefore may not have own P2R and CBR estimates. As a result, resolution authorities currently apply the banking group’s prudential requirements to resolution entities for the calculation of consolidated MREL, which reflect not the true risk associated with the resolution group.
8. The results from the P2R survey show that for 93% of EU resolution groups earmarked for resolution as opposed to liquidation, and are thus subject to MREL with a positive recapitalisation amount, the perimeter of the resolution group and the banking group is identical (**Figure 1**). For the remaining 7%, resolution authorities are required to develop their

own estimates of prudential requirements to be used as input to calibrate MREL at the level of the resolution group.

Figure 1 Share of resolution entities currently subject to MREL on consolidated basis and not subject to prudential requirements, in %



Sources: EBA P2R survey.

Notes: Based on a sample of 345 resolution groups.

9. In addition, two resolution authorities expect that prudential requirements for resolution groups will be needed in the future as resolution group consolidation may change.

B. Policy objectives

10. At high-level, the RTS are expected to contribute to the general objectives of a high, effective and consistent level of banking regulation across the EU.

11. More specifically, the RTS should strengthen the risk-sensitive calculation of MREL for resolution groups under the scope of the RTS and enhance the comparability of resolution requirements across the EU.

12. At the technical level, the RTS provide resolution authorities with an adequate and harmonised methodology to estimate prudential requirements for resolution groups currently not subject to prudential requirements.

C. Baseline scenario

13. Without any further regulatory intervention, resolution authorities follow current national practices to apply P2R and CBR of the consolidated banking group to resolution groups without own prudential requirements.

14. The problem that the calculation of MREL for those entities is based on P2R and CBR estimates, which may not truly reflect the risk associated with the resolution group, will persist.

15. The baseline scenario in relation to P2R is further discussed under Option 1.1.

D. Options considered

Additional own funds requirement (P2R)

16. For the estimation of the P2R, the following options are considered.

Option 1.1: Top-down approach

17. The top-down approach reflects the baseline scenario. Resolution authorities apply P2R estimates provided by competent authorities for the consolidated banking group to the MREL calculation for the resolution entity at the group consolidated level.

Option 1.2: Bottom-up approach

18. The initial approach required a full sub-consolidated P2R estimation at the consolidated resolution group level. This approach would be too burdensome for designated authorities and is therefore rejected. Instead, a simplified sub-consolidated estimation (bottom-up approach) is considered.

19. The bottom-up approach uses for the estimation of resolution group P2R individual and sub-consolidated P2R of each entity within the resolution group, weighted by their total risk exposure amount (TREA).

Option 1.3: Combined adjusted top-down and simplified bottom-up approach

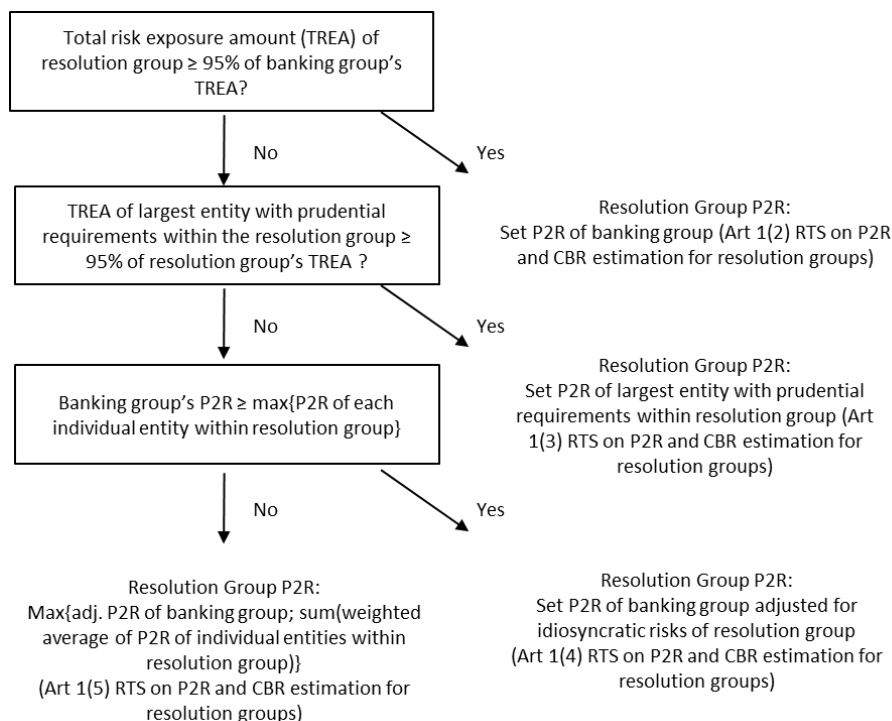
20. **Figure 2** shows the combined top-down and bottom-up approach to estimate P2R of the resolution group (Option 1.3).

21. In cases where the risks present in the resolution group coincide with the risks of another entity of the group, for which prudential requirements are set by competent authorities, resolution authorities will use the P2R estimates of this entity.⁵

22. In cases, where the scope of the resolution group is not comparable to the scope of any other entity of the group, resolution authorities will either use the simplified bottom-up approach or will consult competent authorities to determine the resolution group's P2R. For the later, the banking group's P2R serves as a basis and is adjusted for the specific risks of the resolution group.

⁵ For this purpose the scope of consolidation of the resolution group is compared with i) the scope of consolidation of the banking group and ii) the scope of consolidation of the largest entity within the resolution group. A 95% threshold applies.

Figure 2 Combined top-down and bottom-up approach



Combined buffer requirements (CBR)

- 23. To set the CBR used in the calculation of MREL, resolution authorities need to provide estimates for each relevant element of the CBR - the capital conservation buffer (CCoB), the G-SII buffer, the O-SII buffer and the Systemic Risk buffer (SyRB).
- 24. For the macroprudential measures, which are set at EU level (CCoB) or consolidated banking group level (G-SII buffer), the buffer requirements of the banking group are applied to the resolution group.
- 25. The O-SII buffer and SyRB on the other hand are estimated at the individual level of the entity. Following options are considered for their estimation.

Option 2.1: Individual sub-consolidated requirement

Under Option 2.1, a full sub-consolidated risk assessment of the resolution group is carried out by the resolution authority, in cooperation with competent authorities, to provide individual O-SII buffer and SyRB for the resolution group.

Option 2.2 Combined top-down and bottom-up approach

Under Option 2.2, the SyRB and O-SII buffer of the resolution group are based on the requirements set at the level of consolidation that is the closest to the TREA of the resolution group.

E. Cost-Benefit Analysis and preferred option

26. Figure 1 shows that for only 25 EU resolution groups (7%), for which resolution planning is carried out, a methodology to estimate prudential requirements is currently required.

27. The cost-benefit analysis is drafted based on implication on those cases.

Additional own funds requirement

28. The top-down approach (Option 1.1) has the advantage that resolution authorities can use a simple methodology. This option takes advantage of already existing P2R estimates developed by competent authorities, without the need for cooperation between the authorities. Option 1.1 reflect current national practices and is simple, harmonised and requires no additional data.

29. Figure 3 shows that from the 25 cases, where resolution authorities identified the need for a P2R estimate, 64% of resolution groups materially differ from the banking group in terms of TREA. Here, the top-down approach can lead to imprecise P2R because of overestimation (accounting for risks that are outside the resolution entity) or underestimation (offsetting positions, which lie outside the resolution group) of the risks.

30. While Option 1.1 provides a simple methodology, which requires little to no incremental costs for resolution authorities and resolution entities, the methodology can result in imprecise P2R estimates.

Figure 3 Scope of resolution group compared to banking group (in term of TREA), in %



Sources: EBA P2R survey.

Notes: Based on a sample of 25 cases identified from 345 resolution groups.

31. The initially considered full sub-consolidated P2R estimation requires designated authorities to perform a full supervisory review and evaluation process. This requires, at the minimum, quarterly monitoring of key indicators, assessment of all elements every three years and annual

summary of the elements and engagement with institution’s management every three years.⁶ This process is considered too burdensome for the sole purpose to be used in the MREL calculation.

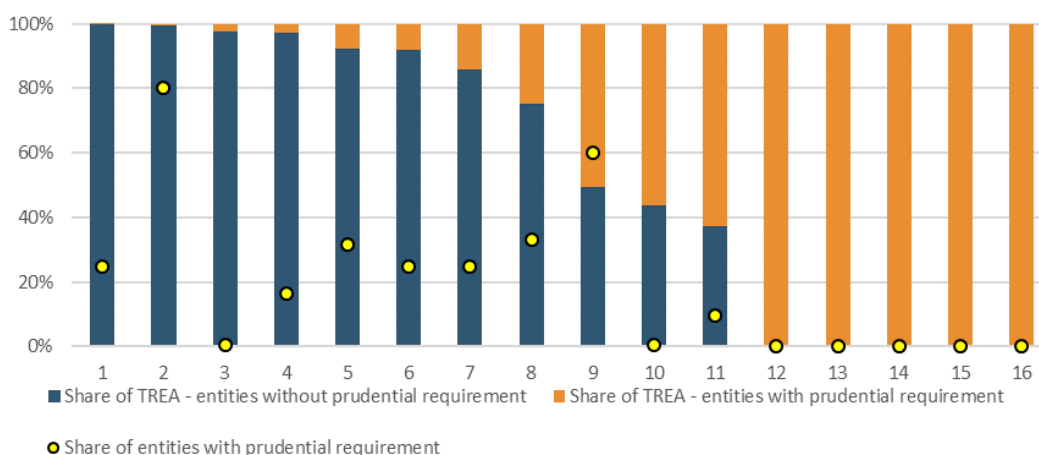
32. Instead, Option 1.2 compound the risk profile of the resolution group by evaluating the riskiness of each entity within the resolution group. This option also takes advantage of already existing P2R estimates of entities within the resolution group. It is simple and requires no additional data or cooperation between authorities.

33. This approach, however, can lead to imprecise P2R estimates as it ignores benefits from consolidation and can be impractical in case of complex resolution groups. It further assumes that individual entities, which are exempted or waived from prudential requirements, are risk free.

34. Figure 4 shows that resolution groups in the sample consist of a large share of individual entities without prudential requirements (479 out of 504 individual entities).⁷ In terms of TREA, for half of the resolution groups, entities with a prudential requirement present less than 25% of these resolution group, i.e. 75% of the resolution group is assumed to be risk free.

35. The bottom-up approach provides a simple and more precise P2R estimation. However, in cases where for the majority of entities in the group no prudential requirement apply, the approach may underestimate the risks of the group.

Figure 4 Share/Number of entities without prudential requirements, in %



Sources: EBA P2R survey.

Notes: Based on a sample of 25 cases identified from 345 resolution groups.⁷

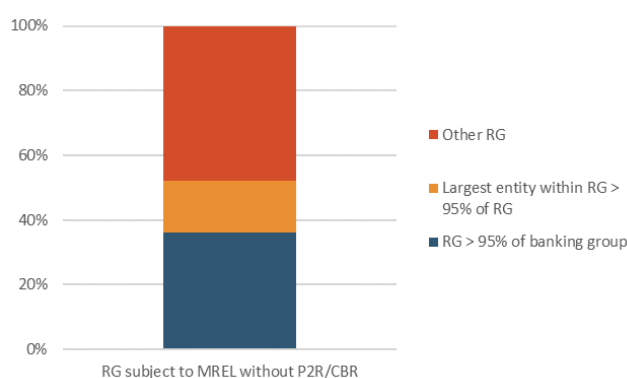
⁶ EBA (July 2018): *Guidelines on common procedures and methodologies for supervisory review and evaluation process (SREP) and supervisory stress testing.*

⁷ Figure 4 shows results for the resolution groups, for which the top-down approach is not applicable, i.e. banking group TREA < 95% resolution group TREA.

36. Option 1.3 extends the simplicity of the top-down approach to the bottom-up approach, by allowing resolution authorities to assign P2R of the largest entity within the resolution group to the resolution group. This approach takes advantage of existing P2R estimates at various levels within the group. This approach can be applied to 52% of the resolution groups in the sample. In addition, option 1.3 gives resolution authorities the flexibility to adjust for the resolution group's idiosyncratic risks where necessary.

37. **Figure 5** shows that resolution authorities can simply rely on existing banking group P2R (for 36% of cases) or on the P2R of the largest entity within the resolution group (16% of cases) in the majority of current cases.

Figure 5 Share of resolution groups under simple top-down/bottom-up approach



Sources: EBA P2R survey.

Notes: Based on a sample of 25 cases identified from 345 resolution groups.

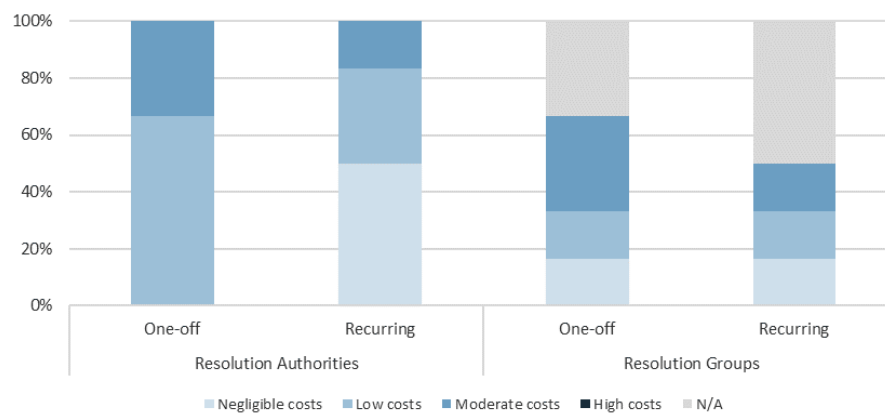
38. For entities, for which the simplified approach under option 1.3 would result in imprecise requirements (48% of cases), Option 1.3 provides resolution authorities the flexibility to develop own P2R for those entities.

39. The proposed approach does not require a full supervisory review and evaluation process, but is instead based on the bottom-up approach subject to the (adjusted) banking group P2R as a floor. This approach prevents the blend responsibilities of resolution and supervisory authorities and rather allows resolution authorities to draw from supervisor's expertise when applying a simple approach to evaluate the risks of those entities.

40. Resolution authorities expect that the costs for them related with the Methodology under Option 1.3 are negligible to moderate (Figure 6). The costs for resolution groups are expected to be slightly higher, where applicable.

41. In terms of higher MREL requirements due to higher P2R, the result of the survey shows that only in cases where resolution authorities would apply an adjusted banking group P2R (40%), the methodology of Option 1.3 would potentially lead to a higher estimates.

Figure 6 One off and recurring costs, in %



Sources: EBA P2R survey.

Notes: Based on a sample of 25 cases identified from 345 resolution groups.

42. Option 1.3 has been adopted.

Combined buffer requirements (CBR)

43. Option 2.1 requires the relevant authority to perform a complex risk assessment process. The O-SII buffer estimate requires an annually assessment of the systemic risk of an entity. For this purpose, relevant authorities need to calculate quantitative indicators (related to size, interconnectedness, relevance for the economy, complexity) to indicate the systemic importance. Where quantitative indicators are not sufficient, the process is complemented by supervisory judgment.⁸

44. In the absence of an EU framework for Systemic risk buffer (SyRB) estimation, relevant authorities are required under Option 2.1 to access the resolution group's risks from propagation and amplification of shocks within the financial system, from the structural characteristics of the banking sector as a whole and from negative shocks to the banking sector stemming from the real economy.⁹

45. This approach will result in precise requirements estimation, however, it will require relevant authorities to engage in a complex and burdensome risk assessment, which includes the collection and evaluation of new data and allocation of significant resources to the process.

46. Option 2.2 on the other hand benefits from existing buffer requirements and provides a simple approach for resolution authorities to assign them to resolution groups.

⁸ EBA (2014): *Guidelines on criteria to assess other systemically important institutions (O-SIIs)*.

⁹ ESRB (2017): *Final report on the use of structural macroprudential instruments in the EU*.



47. Further, Option 2.1 assigns tasks to resolution authorities that are usually performed by supervisory authorities, which creates friction to the clear separation of responsibilities of regulatory authorities in the banking sector.

48. Option 2.2 has been adopted.

5.2 Overview of questions for consultation

Do you agree with the proposed 5% threshold?

Do you agree with the proposed methodology for estimating pillar 2 requirements?

Do you agree with the proposed methodology for estimating the combined buffer requirement?