

EBA/RTS/2020/14

23 December 2020

Final Report

Draft 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 for the purpose of setting minimum requirements for own funds and eligible liabilities under Article 45c(4) of the BRRD

Contents

1. Executive summary	3
2. Background and rationale	4
3. Draft regulatory technical standards	7
4. Accompanying documents	15
4.1 Draft cost–benefit analysis/impact assessment	15
4.2 Views of the Banking Stakeholder Group	23
4.3 Feedback on the public consultation	23

1. Executive summary

Pursuant to Article 45e(1) of Directive 2014/59/EU (the Bank Recovery and Resolution Directive – BRRD), resolution entities must comply with the minimum requirement for own funds and eligible liabilities (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 overestimate the risks within a resolution group.

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

These draft regulatory technical standards (RTS) set out this methodology, which, first, introduces a threshold to capture only resolution groups that differ sufficiently from the prudential group. Second, the methodology aims to be pragmatic by combining top-down and bottom-up approaches to estimating the additional own fund requirement (Pillar 2 requirement – P2R) and the combined buffer requirement (CBR).

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

The draft RTS will be submitted to the Commission for endorsement before being published in the *Official Journal of the European Union*. The RTS will apply from the twentieth day following that of their publication in the *Official Journal of the European Union*.

2. Background and rationale

2.1 Background

The BRRD establishes a framework for the recovery and resolution of credit institutions, investment firms and related entities. Under this framework, resolution authorities, after consulting the relevant competent authorities, must ensure that institutions meet at all times an MREL.

The primary objective of MREL is to enable the recapitalisation of a resolution entity, that is, to ensure that it is able to report capital levels above its minimum capital requirement and sufficient to generate confidence. This is why, in accordance with Article 45c(3), (5) or (7) of the BRRD, MREL is calibrated using the minimum capital requirements and buffers applicable to a banking group or relevant entity.

Article 45e(1) of the 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 may be the case in particular for multiple point of entry resolution strategies that envisage the breaking up of the banking group into several distinct entities post resolution. But it may also be the case for single point of entry banking groups, for example where the point of entry is not the top parent company. In those cases, because capital requirements are set at the prudential group level, they 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 belongs to calibrate MREL.

A policy option to address this issue would be to require competent authorities to align the prudential and resolution group perimeters. However, this option was considered too costly by the co-legislators, as prudential perimeters have to reflect ongoing business needs, while resolution perimeters may differ.

Instead, the EBA was tasked with developing a methodology for resolution authorities to use in estimating capital requirements and CBRs to use as inputs when calibrating MREL. The EBA, in collaboration with EU resolution authorities, and in consultation with competent authorities, has developed an approach intended to:

- a. avoid a requirement for subconsolidation at resolution group level;
- b. avoid confusion regarding the roles of resolution authorities and supervisors in relation to setting capital requirements;
- c. create a framework for dialogue between the bank and the relevant competent and resolution authorities to improve the accuracy of estimates over time;
- d. be straightforward and avoid overburdening resolution authorities;
- e. allow further adjustments, as in the usual MREL-setting process.

2.2 Proposed approach

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

In developing the RTS, it became apparent that some resolution groups differ from the prudential group only marginally. Typically, the prudential perimeter will not include a holding company that is part of the resolution group. While technically the perimeters are different, the levels of risk are not significantly different.

To ensure that this methodology captures only resolution groups for which estimates of P2R and CBR are actually needed, it was decided to introduce a materiality threshold of 5%. The threshold is meant to express the difference between the total risk exposure amount (TREA) of the resolution group and that of the banking group or entity closest in size for which own funds requirements have been effectively set by the competent authority. The level of the threshold was chosen based on the existing materiality threshold considered in international standards on resolution (e.g. the total loss-absorbing capacity term sheet) and following a survey of resolution authorities that confirmed the effectiveness of the proposed threshold.

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

The first is a top-down approach, whereby the resolution authorities should seek to adjust the requirement for the banking group, or the entity to which the resolution group is closest in size and for which capital requirements have been set. Following this approach, the adjustment should be made only on the basis of the input provided by the competent authority, that is, the part of the group's P2 requirement that is driven by an entity or a type of risk outside the resolution group. The rationale for limiting the adjustment in this way is to ensure that responsibility for setting capital requirements remains with competent authorities, the authorities who, following resolution, would need to authorise the resolved entity or group. If no input for the adjustment is provided by the competent authority, the resolution authority should use the group's requirements to calibrate MREL at the resolution group level.

The second is a bottom-up approach, to be used in cases where at least one of the solo requirements set for entities comprising the resolution group is higher than the group's requirement. The view is that varying levels of capital requirements are indicative of risks that are not homogenous within the group. In such a case, the resolution authority should calculate the weighted average of the individual P2Rs and apply it only if it is higher than the adjusted requirement for the group.

With regard to the estimation of the CBR, the proposed approach is equally straightforward and proportionate. The proposed methodology is described below.

- For the global systemically important institution (G-SII) buffer, the proposal is to use the GSII buffer when the Group's top entity is also the resolution entity for the resolution group. Still, pursuant to Article 45c(3) of the BRRD, seventh subparagraph, the resolution authority may, when calibrating requirements, adjust the CBR on the basis of the resolution plan and thus not apply the G-SII buffer.



- For the other systemically important institution (O-SII) buffer, the proposal is to use as an input to calibrate MREL the buffer of either the banking group or the largest entity constituting the resolution group, whichever is the closest in size to the resolution group. Again, the level of the O-SII buffer can be adjusted up or down by the resolution authority pursuant to Article 45c(7) of the BRRD, sixth subparagraph.
- As for the O-SII 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 the largest entity constituting the resolution group, whichever is the closest in size to the resolution group. Again, the level of the systemic risk buffer can be adjusted up or down by the resolution authority pursuant to Article 45c(7) of the BRRD, sixth subparagraph.

No estimation methodology is proposed for the capital conservation buffer or the countercyclical buffer. This is because the former is not bank specific and is simply set at the consolidated resolution group level and the latter applies to specific exposures.

3. Draft regulatory technical standards

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

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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 purpose 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 648/2012,¹ 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 Council² 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

¹ OJ L 173, 12.6.2014, p. 190.

² 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 Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

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 the 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 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 group. The additional own funds requirement and the combined buffer requirement apply to the Union parent institution at the group consolidated level in accordance with Article 11 of Regulation (EU) No 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 risk 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 is almost entirely composed of one entity of that resolution group, this is an indication that the risks or elements of risk 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, the resolution authority should use the additional own funds requirement of that largest entity as an estimation of 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 with 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 that one or more individual requirements within the resolution group are higher than the additional own funds 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 the resolution group. To estimate the additional own funds requirement of the resolution entity at the resolution group consolidated level, the resolution authority should, therefore, whenever this circumstance occurs, compare an 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 funds 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 information provided by the competent authority adjust the additional own funds 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 information 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 at addressing systemic risk (the global systemically important institution (G-SII) buffer, other systemically important institution (O-SII) buffer and the systemic risk buffer) should by default be deemed to be identical to the requirements set for the entity that 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 other requirements, 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 required 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 the amount required 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 Council,³

HAS ADOPTED THIS REGULATION:

Article 1

Estimation of the additional own funds requirement

³ 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 (OJL 331, 15.12.2010, p. 12).

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.
2. Where the total risk exposure amount of the resolution entity at the resolution group consolidated level differs by 5% or less from the total risk exposure amount of the Union parent institution at the group consolidated level, 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 of 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 of 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 of 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 exposure 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 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) No 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 Article 104(1)a of Directive 2013/36/EU 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, can not establish that any significant risk relates to entities or activities located outside the resolution group.

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 of 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. Where the resolution entity is also the Union parent undertaking, resolution authorities shall use as an estimation of 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 of that requirement the O-SII buffer requirement set at the level of consolidation that is the closest, in terms of total risk exposure amount, to 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 of that requirement the systemic risk buffer requirement set at the level of consolidation that is closest, in terms of total risk exposure amount, to 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]

4. Accompanying documents

4.1 Draft cost–benefit analysis/impact assessment

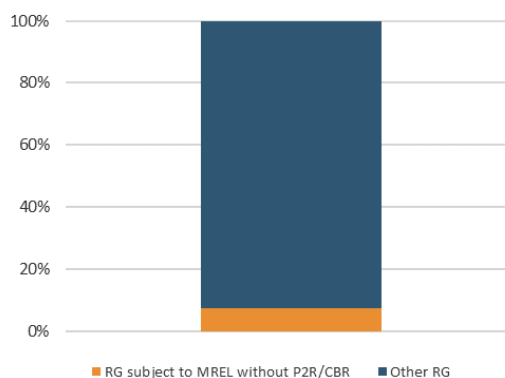
- Article 45c(4) of the BRRD2 requires the EBA to develop draft RTS specifying the methodology to be used by resolution authorities to estimate prudential requirements for resolution entities at the resolution group consolidated level where the resolution group is not subject to those requirements under Directive 2013/36/EU (CRD IV).
- Under Article 10(1) of Regulation (EU) No 1093/2010 (the EBA Regulation), any RTS developed by the EBA shall be accompanied by an impact assessment that analyses ‘the potential related costs and benefits’.
- This section presents the cost–benefit analysis of the main policy options included in the RTS described in the Consultation Paper. The impact assessment draws on data collected from resolution authorities in the survey BRRD2 Mandates–Pillar 2 (the P2R survey).

A. Problem identification

- Resolution entities are required to comply with 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) of BRRD2 and uses prudential requirements defined in CRD IV, namely the P2R under Article 104a of CRD IV and the CBR under Article 128, first subparagraph, point (6), of CRD IV.
- 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 subconsolidated levels for entities within the banking group, where no waivers or exemptions apply.
- Resolution groups, however, are defined in accordance with the preferred resolution strategy, and may 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 do not reflect the true risk associated with the resolution group.
- The results from the P2R survey show that for 93% of EU resolution groups earmarked for resolution as opposed to liquidation, and which 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 inputs to calibrate MREL at the level of the resolution group.

Figure 1: Shares of resolution groups currently subject to MREL on a consolidated basis and not subject to prudential requirements, and other resolution groups



Source: EBA P2R survey.

Notes: Based on a sample of 345 resolution groups. RG, resolution group.

- 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

- At a 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.
- More specifically, the RTS should strengthen the risk-sensitive calculation of MREL for resolution groups that fall within the scope of the RTS and enhance the comparability of resolution requirements across the EU.
- At a technical level, the RTS provide resolution authorities with an adequate and harmonised methodology to use in estimating prudential requirements for resolution groups currently not subject to prudential requirements.

C. Baseline scenario

- Without any further regulatory intervention, resolution authorities would follow current national practices to apply the P2R and CBR of the consolidated banking group to resolution groups without own prudential requirements.
- The problem that the calculation of MREL for those entities is based on P2R and CBR estimates that may not truly reflect the risk associated with the resolution group would persist.

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

D. Options considered

Additional own funds requirement

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

Option 1.1: Top-down approach

- 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

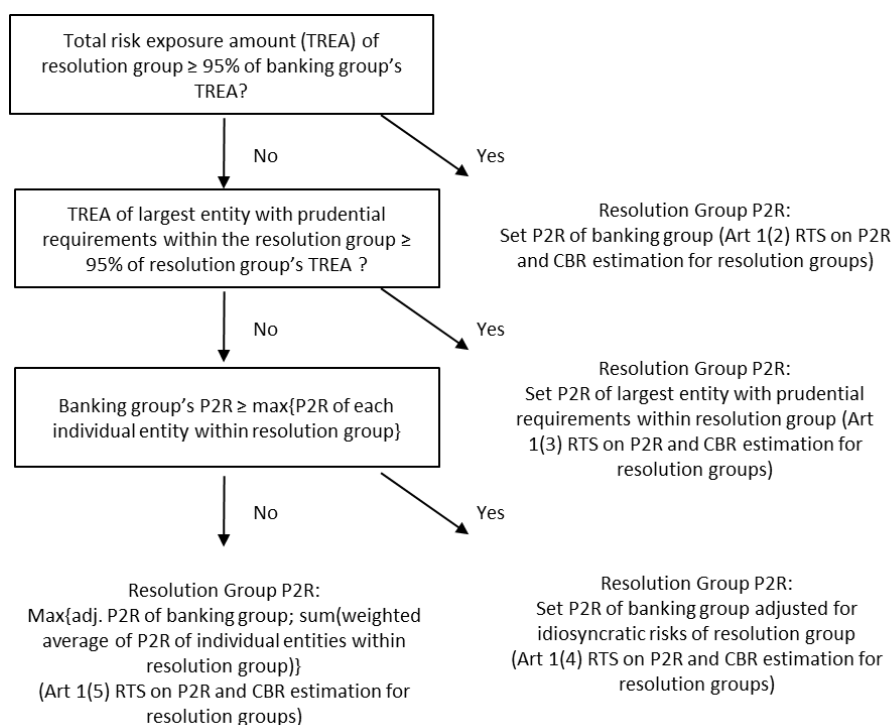
- The initial approach required a full subconsolidated P2R estimation at the consolidated resolution group level. This approach would be too burdensome for the relevant authorities and has therefore been rejected. Instead, a simplified subconsolidated estimation (bottom-up approach) is considered.
- The bottom-up approach uses for the estimation of resolution group P2R the individual and subconsolidated P2Rs of each entity within the resolution group, weighted by their TREA.

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

- Figure 2 shows the combined top-down and bottom-up approach to estimating the P2R of the resolution group (Option 1.3).
- 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 estimate of this entity.⁴
- 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. In the latter case, the banking group's P2R serves as a basis and is adjusted to take into account the specific risks of the resolution group.

⁴ 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 requirement

- 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, the G-SII buffer, the O-SII buffer and the systemic risk buffer.
- For macroprudential measures that are set at EU level (the capital conservation buffer) or consolidated banking group level (the G-SII buffer), the buffer requirements of the banking group are applied to the resolution group.
- The O-SII buffer and the systemic risk buffer, on the other hand, are estimated at the individual level of the entity. The following options are considered for their estimation.

Option 2.1: Individual subconsolidated requirement

Under Option 2.1, a full subconsolidated 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 systemic risk buffer for the resolution group.

Option 2.2 Combined top-down and bottom-up approach

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

E. Cost–benefit analysis and preferred option

- Figure 1 shows that a methodology to estimate prudential requirements is currently required for only 25 EU resolution groups for which resolution planning is carried out (7%).
- The cost–benefit analysis has been drafted on that basis.

Additional own funds requirement

- The top-down approach (Option 1.1) has the advantage that resolution authorities can use a simple methodology. This option takes advantage of existing P2R estimates developed by competent authorities, without the need for cooperation between the authorities. Option 1.1 reflects current national practices, is simple and harmonised, and requires no additional data.
- Figure 3 shows that, of the 25 cases in which 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 inaccurate P2Rs because of overestimation (accounting for risks that are outside the resolution entity) or underestimation (offsetting positions that lie outside the resolution group) of the risks.
- While Option 1.1 provides a simple methodology that gives rise to little or no incremental cost for resolution authorities and resolution entities, the methodology could result in inaccurate P2R estimates.

Figure 3: Resolution groups compared with banking groups in terms of TREA



Source: EBA P2R survey.

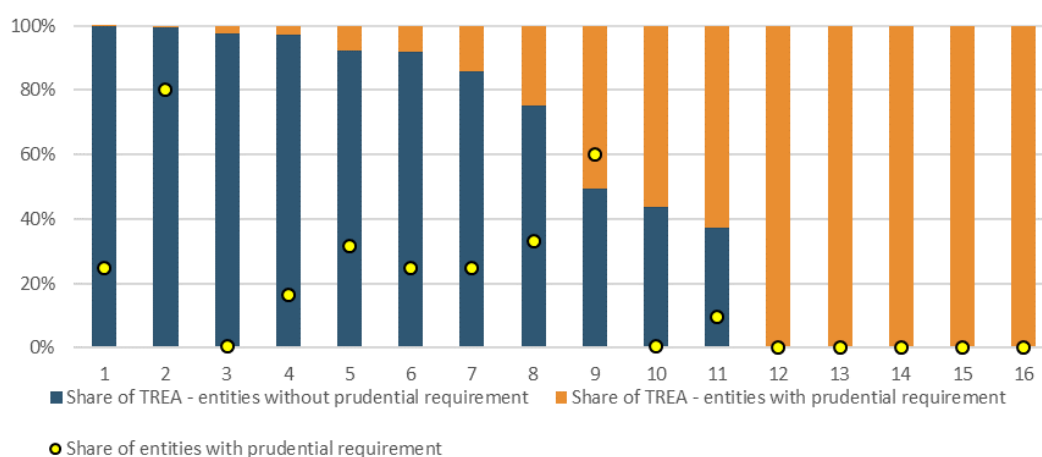
Notes: Based on a sample of 25 cases identified from 345 resolution groups. BG, banking group; RG, resolution group.

- The full subconsolidated P2R estimation initially considered 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, an annual summary of the elements and engagement with the institution’s management every three years.⁵ This process is considered too burdensome for the sole purpose of use in the MREL calculation.

- Instead, Option 1.2 assesses the risk profile of the resolution group by evaluating the riskiness of each entity within the resolution group. This option also takes advantage of existing P2R estimates for entities within the resolution group. It is simple and requires no additional data or cooperation between authorities.
- This approach, however, could lead to inaccurate P2R estimates, as it ignores benefits arising from consolidation, and it could be impractical for complex resolution groups. Furthermore, it assumes that individual entities that are exempted or waived from prudential requirements are risk free.
- Figure 4 shows that resolution groups in the sample include a large share of individual entities without prudential requirements (479 out of 504 individual entities).⁶ In terms of TREA, for half of the resolution groups, entities with a prudential requirement make up less than 25% of these resolution groups, i.e. 75% of the resolution group is assumed to be risk free.
- The bottom-up approach provides a simple and more precise P2R estimation methodology. However, in cases where for the majority of entities in the group no prudential requirements apply, the approach may underestimate the risks of the group.

Figure 4: Shares/numbers of entities without prudential requirements



Source: EBA P2R survey.

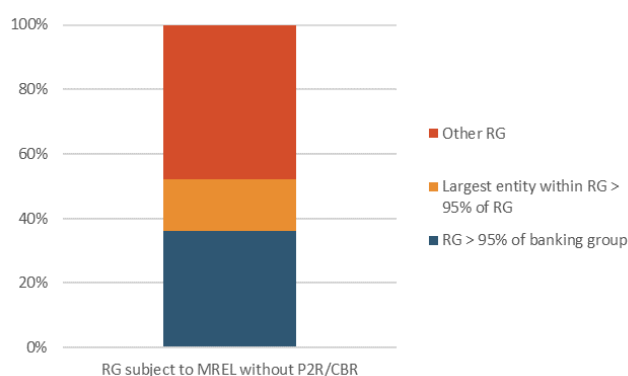
Notes: Based on a sample of 25 cases identified from 345 resolution groups.⁶

⁵ EBA, *Guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing* (July 2018).

⁶ Figure 4 shows results for the resolution groups for which the top-down approach is not applicable, i.e. banking groups with TREA < 95% of the resolution group’s TREA.

- Option 1.3 extends the simplicity of the top-down approach to the bottom-up approach, by allowing resolution authorities to assign the 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.
- Figure 5 shows that, in the majority of current cases, resolution authorities can simply rely on existing banking group P2Rs (36% of cases) or on the P2R of the largest entity within the resolution group (16% of cases).

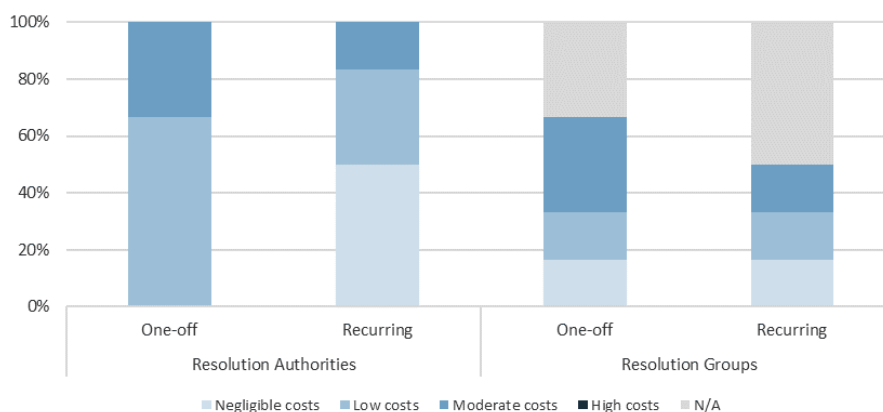
Figure 5: Shares of resolution groups under simple top-down/bottom-up approach



Source: EBA P2R survey.

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

- For entities for which the simplified approach under Option 1.3 would result in inaccurate requirements (48% of cases), Option 1.3 allows resolution authorities the flexibility to develop their own P2R estimates for those entities.
- 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 any confusion in the responsibilities of resolution and supervisory authorities and allows resolution authorities to draw on supervisors' expertise in applying a simple approach to evaluating the risks of those entities.
- Resolution authorities expect that the costs for them arising from the methodology under Option 1.3 would be negligible to moderate (Figure 6). The costs for resolution groups are expected to be slightly higher, where applicable.
- In terms of higher MREL requirements due to higher P2R, the results of the survey show that only in cases where resolution authorities apply an adjusted banking group P2R (40%) will the methodology under Option 1.3 potentially lead to higher requirements.

Figure 6: One off and recurring costs

Source: EBA P2R survey.

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

- Option 1.3 has been adopted.

Combined buffer requirement

- Option 2.1 requires the relevant authority to perform a complex risk assessment process. The O-SII buffer estimate requires an annual 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 assess systemic importance. Where quantitative indicators are not sufficient, the process is complemented by supervisory judgement.⁷
- In the absence of an EU framework for systemic risk buffer estimation, relevant authorities are required under Option 2.1 to assess the resolution group's risks in relation to propagation and amplification of shocks within the financial system, the structural characteristics of the banking sector as a whole and negative shocks to the banking sector stemming from the real economy.⁸
- This approach would result in precise estimations of requirements; however, it would require the relevant authorities to engage in a complex and burdensome risk assessment, which would include the collection and evaluation of new data and require the allocation of significant resources to the process.
- Option 2.2, on the other hand, takes advantage of existing buffer requirements and provides a simple approach that resolution authorities can use to assign them to resolution groups.

⁷ EBA, *Guidelines on criteria to assess other systemically important institutions (O-SIIs)* (2014).

⁸ European Systemic Risk Board, *Final report on the use of structural macroprudential instruments in the EU* (2017).



- Furthermore, Option 2.1 assigns tasks to resolution authorities that are usually performed by supervisory authorities, which disturbs the clear separation of responsibilities of regulatory authorities in the banking sector.
- Option 2.2 has been adopted.

4.2 Views of the Banking Stakeholder Group

The Banking Stakeholder Group gave its support to the proposed approach and provided insightful feedback, in particular on the level of the threshold and on the wording of the RTS, in particular the formula for the bottom-up approach under Article 1(5)b of the draft RTS.

4.3 Feedback on the public consultation

The EBA publicly consulted on the draft proposal contained in this paper.

The consultation period lasted for 3 months and ended on 24 October 2020. Three responses were received, of which two were published on the EBA website.

This paper presents a summary of the key points and other comments arising from the consultation, the analysis and discussion triggered by those comments and the actions taken to address them if deemed necessary.

In several cases, industry bodies made similar comments or the same body repeated its comments in response to different questions. In such cases, the comments and the EBA's analysis are included in the section of this paper where the EBA considers them most appropriate.

Comments in the 'General comments' section have been grouped by category, as appropriate, regardless of if the answers were submitted to one of the questions or in a separate document.

Changes to the draft RTS have been incorporated where appropriate as a result of the responses received during the public consultation.

4.3.2 Summary of responses to the consultation and the EBA's analysis

Most general comments highlighted the importance of having the draft RTS cover situations other than those in which the banking group has a multiple point of entry strategy. This is something that has been given due consideration in the development of the draft RTS, which cover single point of entry banking groups, for example in the situation where the point of entry deviates from the top parent company and, therefore, because the capital requirements are set at the prudential group level, they may not accurately reflect the risk at the level of the resolution group.

A few comments focused on the threshold, proposing a 10% level to ensure material differences are captured. However, the rationale provided was not convincing, since the 5% threshold aims to



capture all resolution groups that differ from the prudential group by 5% or more and thus will capture those that differ by 10%.

Some comments related to the need to ensure that the proposed methodology does not lead to the overestimation of either P2R or CBR. On P2R, the proposed approach allows resolution authorities to carry out necessary adjustments. On CBR, the proposed approach to estimating the G-SII buffers would not lead to overestimation and, in any case, resolution authorities retain the flexibility to make adjustments in the light of the resolution plan.



Comments	Summary of responses received	EBA analysis	Amendments to the proposals
General comments on Consultation Paper EBA/CP/2020/16			
	<p>Some comments noted that a difference between the prudential perimeter and the resolution group perimeter can occur in instances other than in the case of a multiple point of entry resolution strategy.</p>	<p>Indeed, the resolution group can differ from the prudential group in other instances than in the case of a multiple point of entry resolution strategy, and the ‘Background and rationale’ section states precisely that:</p> <p>‘This may be the case in particular for multiple point of entry resolution strategies that envisage the breaking up of the banking group into several distinct entities post resolution. But it may also be the case for single point of entry 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, they may not effectively reflect the risk at the level of the resolution group.’</p>	<p>No change.</p>
	<p>Some comments suggested that the draft RTS should also mention the impact of institutions that would not be supported in resolution as a basis for estimating P2R and CBR.</p>	<p>Article 83b of the BRRD defines a resolution group as a resolution entity and its subsidiaries. Thus, the fact that some entities will not be supported in resolution does not affect the composition of the resolution group or how it differs from the prudential group.</p>	<p>No change.</p>



Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Responses to questions in Consultation Paper EBA/CP/2020/16			
Q1 – Do you agree with the proposed 5% materiality threshold?	Some comments suggested increasing the threshold to 10% to ensure that material differences are captured. The 10% level was viewed as in line with the EBA RTS on MREL threshold on excluded liabilities.	The 5% threshold aims to capture all resolution groups that differ from the prudential group by 5% or more and thus will capture those that differ by 10%. Furthermore, the 10% threshold in Article 3 of the EBA RTS on MREL is not a materiality threshold per se. The 5% materiality threshold is already embedded in EU legislation, in the EBA ITS on resolution reporting (DR2018/02, Article 2(4)a) as the criteria for identifying relevant legal entities.	No change.
Do you agree with the proposed approach to estimating P2R?	Several comments asked for clarification on the perimeter of entities included in the formula of Article 1(5), point (b).	All entities comprising the resolution group should be included in the bottom-up approach.	Draft RTS amended as suggested.
	Some comments asked for the RTS to clarify that the proposed approach was intended to estimate a rate and not an absolute amount.	The draft RTS refer to the P2R, which is defined as a percentage of TREA.	No change.



Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	<p>Some comments raised concerns that the methodology for estimating P2R as set out in Article 1 did not take into account the specificities of banking groups under a multiple point of entry resolution strategy. In particular the concerns related to the point that applying the group P2R to the resolution group might cover risks that lie outside the resolution group.</p>	<p>Article 2 of the draft RTS requires authorities to seek to make adjustments to the group's requirements to ensure that the estimated additional own fund requirement does not capture risk outside the resolution group.</p>	<p>No change.</p>
<p>Do you agree with the proposed approach to estimating Combined buffer Requirement?</p>	<p>Several comments raised concerns that the proposed methodology for estimating CBR for the purpose of setting MREL would lead to overestimation of the recapitalisation amount.</p>	<p>The proposed methodology is for estimating the input to calibrate MREL and not to calibrate MREL itself. Therefore, resolution authorities still have the liberty to include, or not, any components of the estimated CBR when calibrating the market confidence charge (see recital 10).</p> <p>However, for the purpose of estimating the G-SII buffer, the proposed approach was too broad and has now been amended.</p>	<p>Article 3.3 amended</p>
	<p>Some comments asked for the RTS to clarify that the proposed approach was intended to estimate a rate and not an absolute amount.</p>	<p>The draft RTS refer to the CBR, which is defined as a percentage of TREA.</p>	<p>No change.</p>



