WKO BANK · VERSICHERUNG

EBA

Division Bank and Insurance
Austrian Federal Economic Chamber
Wiedner Hauptstraße 63 | P.O. Box 320
1045 Vienna
T +43 (0)5 90 900-DW | F +43 (0)5 90 900-272
E bsbv@wko.at
W http://wko.at/bsbv

Your ref., Your message of	Our ref., person in charge	Extension	Date
53	Kern	3132	August 25th, 2016

Comments on EBA Consultation on "Interim report on the implementation and design of the minimum requirement for own funds and eligible liabilities (MREL)"

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as legal representation of the entire Austrian banking industry, appreciates the possibility to comment on the above cited consultation paper and would like to submit the following position:

A. Answers to EBA specific questions

1. Reference base for MREL

We are generally in favour of changing the reference base to RWA. For us it seems a logical step given the methodology for the determination of MREL in the EBA RTS starting from the expression of the requirement in terms of RWA, which is then translated into a requirement in terms of own funds and total liabilities. In addition, the change in the reference base would align the formulation of the requirement with TLAC requirements.
Nevertheless we would like to point out that the calibration of the MREL ratio (in the second step, as decided by the SRB) should take into account the proportion between RWAs and Total Assets of individual banks so that banks with a higher relative share of RWAs over Assets are not penalized (i.e. no double counting of risk already reflected in RWA-calculations also in the MREL-ratio determination).

We note that the EBA report does not mention the Basel I floor as an alternative backstop measure for the calculation of MREL. We would request clarification whether this omission is done on purpose or whether the current treatment in the EBA RTS on MREL, which looks at both the leverage ratio and the Basel I floor as backstops, is expected to be maintained. We would support dropping the Basel I floor as this not only creates additional complexity but the measure itself is becoming more and more 'anachronistic' as other measures are being phased in. Furthermore, the future of the Basel I floor beyond its transitional end date of 31 December 2017 is uncertain and it would, in our view, not be appropriate to retain it as a backstop for MREL if it were no longer part of the capital framework.

In any event, the interaction of the Basel I Floor with minimum capital requirements, additional capital requirements and buffers as set out in the MREL RTS should be aligned between the loss absorption and recapitalisation amounts. While the loss absorption amount clearly specifies the Basel I floor as a backstop to TOTAL capital requirements, including buffers, the wording for the recapitalisation amount is not clear on how the Basel I floor should be used as a backstop. We would ask the EBA to specify that the Basel I floor should also be compared to TOTAL capital requirements, including buffers, with respect to the recapitalisation amount by clarifying the current wording in the MREL RTS which leads to differences in interpretation between resolution authorities.

2. Relationship with regulatory requirements

In our view the removal of double counting could make sense on the assumption that the MREL ratio is calibrated accordingly (i.e. recapitalization amounts required under a resolution scenario are measured to achieve capital ratios excluding buffers).

As the EBA indicates, there is a potential interplay between the position of the buffers (and the requirement that CET1 used for buffers cannot be used for MREL) and the determination of the maximum distributable amount (MDA) and potential distribution restrictions when combined buffer requirements are breached. The EBA implicitly (although this is not stated explicitly in the report) seems to assume that distribution restrictions would be triggered if the CET1 capital of a bank is insufficient to meet Pillar 1 and Pillar 2 capital (CET1) requirements, MREL CET1 requirements and buffer requirements. In order for this to occur, the relevant Articles in the CRD would need to be amended; however, in this respect there is no reference made in this report. In addition we object an automatic MDA restriction as soon as a bank has breached the CBR which sits on top of the MREL when the bank still fulfils all capital requirements (including CBR) [at least for the coupon distribution] as otherwise it would have a detrimental effect on the ability to issue own funds instruments.

It would also be important to clarify how a bank would determine the amount of CET1 required to fulfil MREL requirements sitting ‘underneath’ the combined buffer requirement, particularly in cases where banks have an excess of MREL-eligible liabilities and own funds compared to their requirements. In this context could banks assume to first ‘fill in’ the MREL requirement with eligible liabilities other than own funds and apply own funds only for any residual amount of the requirement (thus leaving the maximum possible amount of CET1 to cover the buffers). In contrast we would oppose an approach of a ‘composition requirement’ for MREL similar to those for Pillar 2, imposing a mandatory proportion of CET1 to be applied to MREL. This would be an undue requirement especially for deposited funded banks with ‘excess deposits’.

In any event, the current RTS on MREL would have to be changed to ensure that the buffers are not considered to be part of either the loss absorption or recapitalisation amounts, i.e. not part of the MREL requirement.

Regarding the relationship between MREL and other regulatory requirements we would like to point out that there are many different resolution mechanisms in the private sector which should be also taken into consideration in an appropriate manner- notably Art 10 CRR groups with unlimited joint liability schemes, models under Art 113 (6) CRR and IPS systems. Art 10 CRR groups have established protection schemes for individual member banks which are widely recognised in banking legislation. These mechanisms provide such a protection on individual institutions that a group level MREL requirement would be sufficient, while also observing the NCWO principle. Waivers resulting from the CRR (e.g. Art 10 CRR waivers for affiliated institutions) should be taken into consideration when determining the MREL requirements.

Otherwise, MREL requirements on individual institution's level for such models could lead to capital requirements on individual level through a back door and therefore contradict other prudential provisions resulting from the CRR. Also, recital 23 and Art 32 BRRD explicitly acknowledge private sector measures.

An aspect that is (currently) not part of the Interim Report but might be considered as important for further assessment would be the deductions of MREL holdings. As is the case with the ongoing discussion regarding the implementation of TLAC it also becomes a more and more important topic for the marketability of instruments.

3. Relationship between MREL and NSFR

> *EBA provisional recommendation (page 53)*
> *The EBA's provisional view is that interactions between MREL and the net stable funding ratio (NSFR) do not give rise to any need for policy change.*

We do agree with EBA's provisional view.

4. Breach of MREL

We emphasize that the following principles should be ensured:

1) Under no circumstances a breach of MREL requirements, and in particular a breach of the recapitalization amount should be an automatic indication of failing or likely to fail. Only in combination with a breach of other capital requirements at the same time an "MREL breach" could be taken as an indication for the setting of further measurements, i.e. the preparation of a strategy to restore the MREL requirement.

2) In the context of point 1) it is necessary to make sure that the ECB (as the competent authority) sets its measures before SRB (as the resolution authority) might consider starting any action, like measures defined by the recovery plan. In other words, the intervention regime must avoid a situation where there is no breach with respect to the capital ratios set by the ECB.

3) The proportionality principle will need to be taken into account, i.e. all measures available to the ECB need to be initiated and have proven not to be successful before the SRB starts with resolution steps

4) We would like to point out that it is very important to harmonize all the requirements in one framework in order to ensure utmost consistency and to avoid any conflict of measures initiated/considered by the various authorities involved and to ensure procedural certainty for the involved financial institutions.

We agree that Resolution authorities should take the leading role in case of a breach of MREL. However a breach of MREL requirement should not be an automatic indication of failing or likely to fail, unless other requirements (e.g. minimum capital requirements, the leverage ratio or the LCR) are breached at the same time.

In particular in cases where the preferred resolution strategy is bail-in and MREL is set at a level of twice the minimum capital requirements (potentially including twice the Pillar 2 add-on plus – at least at the moment – elements of capital buffers), a breach of the MREL requirement does under no circumstances mean that the bank is not sound on a going-concern basis. The breach of

MREL may present an impediment to resolvability; however, this in itself cannot be interpreted as an indicator of failing or likely to fail.

Therefore, a breach of MREL should be treated like a breach of the combined buffer requirement, i.e. require the bank to prepare a strategy to restore the MREL requirement within an agreed timeframe (similar to the capital conservation plan required in cases of a CBR breach). Measures and solutions should always reflect the actual situation, in particular as some 'breaches' of MREL can be purely technical or just a question of timing, e.g. when an anticipated bond issue is delayed by a few weeks, leading to available MREL dropping below the requirement.

We believe that the competences of Resolution authority set in BRRD are adequate to address the issue (monitor development of MREL, require solution if MREL is not sufficient and escalate the problem) as Resolution authorities are obliged to require and verify that institutions meet the MREL requirement and shall take any decision in parallel with the development and the maintenance of resolution plans (BRRD, Art 45 (15)).
At any rate we would welcome a tight cooperation and coordination between resolution and competent authorities in order to avoid diverging actions and therefore limiting the impact.

5. Adequacy and calibration

The EBA provisionally recommends that the calibration of MREL should in all cases be **closely linked to and justified by** the institution's resolution strategy. We fully agree with this approach and would in particular want to highlight the need for justification by authorities setting MREL as – at least in our experience – this is not yet sufficiently the case. This would also include following the procedure set out in the BRRD stating that the determination of any consolidated requirement would need to be taken by a resolution college, taking into account the resolution strategy and the MREL levels set (or contemplated) at individual entity level.
We believe this creates particular challenges for institutions headquartered in the Banking Union but with significant operations in non-Eurozone Member States, as the SRB's approach to setting MREL does not appear to align with this envisaged procedure. In this respect we would also like to highlight that we do not consider that the SRB has really 'publicly communicated its policy intentions for setting MREL'. Statements so far have been very unspecific, in some cases at odds with the EBA RTS (e.g. when stating that G-SIBs would have to hold at least 8% of own funds and eligible liabilities as MREL). Additionally – and most important – the outcome of the dialogue with individual institutions does not appear to reflect the public statements made in any cases. Further convergence of the approach therefore seems to be highly necessary.

The EBA also states that business models should be considered in the determination of MREL when they lead to differences in resolution strategy. We agree with this statement but would also state that the chosen resolution strategy should respect the business model, e.g. deposit-based banks should not be forced to change their business model, strategy and funding profile as a result of NRAs (or the SRB) determining a 'preferred resolution strategy'.

The EBA states that MREL should be set at the higher of the requirement resulting from the assessment at individual level as outlined in the BRRD (firm-specific Pillar 2 requirement) and any Pillar 1 requirement, should one be introduced. The EBA is, however, not clear on the character of such a Pillar 1 requirement, talking about 'floors' in the report. In our opinion, the only Pillar 1 requirement to be considered should be the TLAC requirement for G-SIBs and the 'higher of' test should thus only apply to G-SIBs subject to TLAC. No Pillar 1 minimum should be introduced for any other type of institution, where the firm-specific approach currently contained in the BRRD should be maintained.

As the ECB introduced a new mechanism for the SREP to be set for 2017 it has to be clarified that only the P2R will count towards the capital requirement in the calibration of the loss absorption and recapitalization amount required.

6. Eligibility

We agree with the EBA's view that relevant information should be available to bank creditors, i.e. banks' creditor hierarchies should be clear and in line with national insolvency law. In this respect it is worth noting that the creditor hierarchy prescribed in the BRRD is not always in line with national insolvency law, leading to different hierarchies with respect to resolution vs. insolvency, which can create issues with respect to the 'no creditor worse off' principle.

The clarity of the creditor hierarchy is not only important in the case of resolution but more generally with respect to going-concern funding operations, as the hierarchy (and attendant expectation of risk) is a key input to pricing of instruments by both issuers and investors.

We would like to stress that there needs to be a sufficient transitional period in order to fully replace the outstanding debt with the issuances featuring the required contractual conditions. Most importantly, all the currently existing debt should be grandfathered for the purpose of calculating the MREL ratio. Furthermore we expect and support a harmonization across European countries in regard to the subordination rankings under MREL.

There should not be a general subordination requirement for MREL-eligible liabilities. The EBA states that subordination may be required for 'some banks'. We would urge the EBA that 'some banks' should not be defined using general labels (e.g. all O-SIIs), but that the need for subordination should be considered on a case-by-case basis, taking into account the following factors:

- *The resolution strategy for the entity in question*: Even within a G-SII or O-SII group, some entities may be considered immaterial and the resolution strategy with respect to this entity might, therefore, be orderly liquidation (this is particularly important in MPE strategies). MREL for these entities is likely to be set at a level of capital requirements only, so there would be no need to require subordination of MREL-eligible liabilities.
- *The liability structure of the entity in question*: Where institutions have very limited amounts of liabilities ranking pari-passu with senior debt (e.g. corporate deposits or excluded operating liabilities), subordination may not be required, as the senior debt tranche would represent a relatively separate step in the creditor hierarchy, subordinated to preferred or covered deposits and some other excluded liabilities (e.g. staff and tax liabilities).
- *The amount of the MREL requirement being met with liabilities*: Where an institution can satisfy its MREL requirement largely with capital instruments and subordinated loans counting as own funds, requiring subordination for the remaining 'eligible liabilities' may not be necessary.

With respect to subordination, our preferred approach would be for a harmonised approach across the EU that allows for both, a legal framework with as well as without subordination, as this would facilitate comparability as well as creating transparency for market participants.

We agree that information on creditor hierarchies should be available to investors, regardless of the form of subordination employed. However, we are not sure that the proposed disclosure items necessarily lead to the desired outcome. Below we comment on each of the proposed types of disclosure:

i. *Bank balance-sheet structure*: We do not think that the disclosure of bank balance-sheet structure would improve transparency with respect to the insolvency ranking, particularly given potential differences between resolution and insolvency law. In addition, the resulting disclosures would be significantly more complex than current disclosures in order to provide sufficient detail on, e.g. the difference between MREL-eligibility and bail-inability, potential exclusions from bail-in and the insolvency hierarchy. This would not be in the interest of investors or debtors.

ii. *Banks' MREL requirements*: Disclosure of the MREL requirement in itself is insufficient for investors to determine their position in the insolvency hierarchy, especially as bail-in does not stop at MREL-eligible instruments but encompasses all instruments that could be subject to bail-in (in particular debt with a remaining maturity below one year).

iii. *Availability of standardised information on statutory creditor hierarchies*: This information will help to some extent in providing transparency on creditor hierarchies; however, it would not address any issues affecting this hierarchy arising from either structural or contractual subordination. As the important information for investors is where they stand in the hierarchy irrespective of the type of subordination or other statutory provisions, the information on statutory hierarchies only would be insufficient.

We believe that any type of standardised disclosure at aggregate level (in particular for a banking group providing consolidated figures) will not be sufficient for investors to fully understand their position in the creditor hierarchy. This is particularly true as bail-in will be executed at legal-entity level and as such unconsolidated figures / accounts would be required for analysis.

In our view, the relevant information on creditor hierarchies need to be contained in information on the individual instrument as this is where investors can analyse the risk they would take by investing in the instrument. Investors should understand the product they buy and all necessary information needs to be provided at the point of making the investment decision.

We also have a number of additional concerns regarding mandatory disclosures as set out below:

- *Timing:* If disclosures are made at year-end (e.g. in line with Pillar 3 disclosures) but an investor is contemplating a new product in July, the liability structure of the bank will already have changed since the last disclosure and the public information is, therefore, no longer relevant, again pointing to detailed disclosures having to be made at product level at the time of issuance.
- *Internal vs. external MREL:* We assume disclosures should only be relevant in case of external MREL requirements. For internal MREL, both parties to the transaction are part of the same group and there should be no need to provide disclosures in these cases. As internal MREL is only relevant in an SPE resolution strategy, where the subsidiaries would not themselves enter resolution, any third-party creditor of the subsidiary would not be at risk of bail-in and, therefore, would not need additional information on creditor hierarchies in resolution. The normal insolvency hierarchies would still be relevant for investors in these cases; however, as this should already be an aspect in their considerations today, there is no need for additional disclosures either.

- *Disclosure at legal entity level:* There is a general question as to the location of disclosures at legal entity level. The Basel Committee is currently considering the inclusion of disclosures for TLAC in Pillar 3 requirements. Having said this, Pillar 3 requirements in the EU only apply at group consolidated level and, for material subsidiaries, to a limited extent at either solo or consolidated level. Therefore, it is unclear where any of the envisioned disclosures might be included. Would disclosure requirements be extended to all legal entities (or only resolution entities)? Would they have to be included in financial statements (bearing in mind that not all of these entities would be required to publish their financial statements) or in some other form of disclosure? In any event, the disclosure requirements are likely to create additional layers of complexity which could be avoided if disclosures were mandatory in product information for investors but not at aggregate level.

In this context we would also highlight the aspect of a lack in standard setting for reporting requirements, which should also be considered by the EBA. EBA should take a leading role for setting a reporting standard for MREL, e.g. in the form of or similar to an ITS, especially ensuring clear and unambiguous definitions for each of the reporting items.

As a final point, the EBA mentions that there is a need to allow for the write-down or conversion of internal MREL instruments in cases where the subsidiary holding the internal MREL is not itself in resolution (particularly important in SPE resolution strategies). We believe that in most cases a contractual solution should suffice, as internal MREL will be subject to internal arrangements within banking groups and present no particular issues with respect to contractual clauses. Using Article 59 of the BRRD to create a statutory framework is, in our view, not necessary at this stage. We also note that while we understand the rationale set out in the report to extend Article 59 to internal MREL, the most recent non-paper by the European Commission contained drafting proposing this extension for all MREL-eligible liabilities, i.e. including external MREL. We oppose such a blanket extension as bail-in of external MREL should only occur in resolution and a write-down power outside of resolution is thus not necessary for external instruments (as it is issued out of resolution entities).

7. Third country recognition

One aspect that should be considered is the issue that potentially arises through the UK's BREXIT decision. Were the UK to leave the EU, it would become a third country – there should be considerations about what requirements would apply in case a country leaves the Union, i.e. would all contracts automatically become subject to Article 55 requirements or would this apply only to contracts entered into after the actual 'leaving date'?

A more general issue pertains to the question of 'equivalence'. The regime would be significantly easier to apply, if there was a centralised process for assessing the equivalence of third-country resolution regimes. For example, if the FSB concluded that jurisdictions implemented the key attributes with respect to bail-in powers in line with the FSB proposals, the EBA could consider them equivalent for the purposes of Article 55 and publish this acknowledgement so that banks would not need to include contractual language in contracts under the law of these jurisdictions. Similarly, this regime could be applied in the BREXIT situation, i.e. the EBA could still consider the UK an equivalent jurisdiction based on an assessment of its implementation of the BRRD.

Considering the overall goal of market-transparency and equal terms of competition within the EU, approach number i) should be the preferred one, implementing certain additional product-related exemptions and avoiding any different solutions on the national level in this case.

8. Calibration of MREL

EBA provisional recommendation (page 68):
The EBA provisionally recommends that calibration of MREL should in all cases be closely linked to and justified by the institution's resolution strategy. Business models may be worth considering when calibrating MREL to the extent they translate into /lead to differences in resolution strategies.
The EBA provisionally recommends that the current MREL assessment framework (under BRRD Article 45 and the RTS on MREL) be retained as the basis for setting 'Pillar 2'/firm-specific MREL requirements. This means that MREL should be set as the higher of the requirement resulting from this assessment and any Pillar 1 requirement, should one be introduced. Firm specific requirements should only be set at levels necessary to implement the resolution strategy.

We generally concur with these views. From a procedural perspective, we would suggest that the MREL yearly assessment should be combined with the SREP assessment.

A. Further Comments to the EBA Interim Report not specifically raised

1. Approval for redemption of MREL instruments

The report considers a number of options for approvals for redemption of MREL-eligible liabilities. Before discussing the issues with each of the options considered below, we would like to reiterate that there is currently no approval requirement for redemptions of MREL-eligible instruments in the BRRD and that the TLAC term sheet, which includes an approval requirement, only requires this in cases where the redemption would lead to a breach of the TLAC requirement.

We believe that the requirement stipulated in Art 78 CRR should not be extended to MREL eligible liabilities. According to the experiences so far the approval-process leads to a significant burden for both, institutions and competent authorities and takes too long to react fast to current market conditions and therefore to safeguard a functioning market. Additionally, such permissions could have a negative impact on the placement of such instruments since the flexibility of investors in selling their investments in MREL eligible liabilities would be restricted.

We therefore are in favour of the last option proposed by the EBA (see page 51).

This raises the question whether there should be any approval requirement for MREL-eligible liabilities introduced in the BRRD at all, obviating the need for any of the proposed options. If the objective was to introduce a requirement in order to facilitate the implementation of TLAC, any requirement should not exceed the provisions of the TLAC term sheet.

Below we comment on the proposed options in more detail:

- *Extending approval for redemption to all external MREL-eligible instruments:* This approach is considered far too strict - especially for banks with a very high amount of MREL eligible liabilities. In addition, it is not considered workable in cases where deposits constitute eligible liabilities. Requiring approvals in all these cases would significantly impede banks' liquidity and funding risk management in addition to creating significant administrative burden for both institutions and competent authorities. As the current process of obtaining approval for redemptions of capital instruments has already proven to be extremely cumbersome and time-consuming (with approvals taking significant amounts of time), an extension to all MREL-eligible liabilities is not considered workable.

- *Further extending approval for redemption to internal TLAC / MREL*: In general this option considers two separate issues, i.e. an approval might be required in all instances where redemptions are contemplated (similar to the previous point) or only in cases where the redemption would lead to a breach of the internal TLAC/MREL requirement. With respect to the first part, the points made above under the first option equally apply, with the volume of potential approvals further multiplied. For the second part, it would first be necessary to establish a binding internal MREL requirement (which is currently not included in the BRRD and the report itself does not provide any information on how internal MREL would be established). Given that the TLAC term sheet also does not foresee any approval requirement for redemptions of internal TLAC, we would recommend not introducing this requirement for MREL.
- *Powers for resolution authorities to monitor, and potentially enforce, the MREL maturity structure:* We agree that the resolution authority should monitor the MREL maturity structure and potentially make recommendations. However, there is a need to consider the work undertaken by competent authorities with respect to a review of the funding and liquidity management of the institution, which will include a review of the maturity profile of funding and also include recommendations as appropriate. Any duplication of analysis and – in a worst case – contradicting recommendations should be avoided. As such, we believe that it should be the primary responsibility of the competent authorities to monitor the funding maturity profile with the resolution authorities providing a 'second pair of eyes' but only making recommendations deviating from those of the competent authorities if these can be justified from a resolvability perspective. Under no circumstances should resolution authorities have the power to enforce an MREL maturity structure as the funding maturity structure (and strategy) of a bank is an important part of its liquidity and funding risk management framework. Maturity structures will also be influenced by market conditions (which may make longer term funding more or less attractive/available) and pricing considerations in addition to risk considerations. In addition, the only requirement for MREL in terms of a maturity is a remaining maturity in excess of one year, so imposing any maturity structure that goes beyond this requirement is in our view not consistent with the legal requirements.
- *Requiring approval from competent authority only if a breach of the MREL requirement would occur as a result of the redemption of the instruments (as in TLAC term sheet):* As already outlined in the introduction, we question the need to impose an approval requirement for MREL as this is not currently foreseen in the BRRD. The option to align the requirement with the TLAC requirement represents the maximum that should be required with respect to MREL. Nevertheless, even under this option there is the question of how the approval process should be designed. In our view, this should not follow the same rules, documentation requirements and approval processes as those required for capital instruments, as that process has proven too time-consuming for both banks and competent authorities with decisions taking several months. The EBA should consider which parts of the process could be simplified as eligible liabilities do not have the same characteristics as own funds. In addition, the requirements might be differentiated depending on the size and/or anticipated duration of the breach.

An important point to consider with respect to the approval for redemptions is the interaction with the consequences of an MREL breach. Clearly, if option 4 as set out above is taken and the resolution authorities approve the (temporary) MREL breach resulting from redemption, there should be no consequences for banks resulting from this breach.

2. Comments on impact analysis

The EBA interim report includes a section on quantitative findings which is based on a sample of banks from across the EU. The analysis highlights issues due to differences in business models, banking systems, etc. and analyses the impact of MREL requirement under a number of scenarios. While the analysis appears relatively comprehensive, it still suffers from a number of shortcomings as outlined below.

- *Completeness*: The analysis does not cover the entire EU, i.e. a number of countries are missing entirely. While they, in aggregate, do not account for more than 30% of banking assets in the EU, issues that may affect individual countries are not considered. For us, the exclusion of Croatia, Romania, Slovakia and Slovenia is of particular importance, as these markets represent significant operations for the Group.
- *Consolidated vs. solo level*: Since MREL is a requirement at individual institution level, any quantitative impact analysis needs to be undertaken at individual institution level as well in order to determine whether there are potential issues related to specific markets, business models or types of institutions. The majority of the analysis is undertaken (as in previous exercises) at consolidated level and the EBA acknowledges that the analysis only includes 'a few' subsidiaries of EU parent institutions. As a result, the reported shortfall may significantly underestimate the actual shortfalls at legal entity level.
- *Pillar 2 requirements*: While we appreciate the data constraints that led the EBA to consider a 'standard' Pillar 2 add-on of 2% for all banks, this vastly underestimates the true Pillar 2 add-on for many institutions and – as a result – leads to a significant underestimation of MREL requirements in all scenarios. The issue is particularly acute in some jurisdictions that set comparatively high Pillar 2 requirements and – coupled with the lack of analysis at solo-institution level – masks potential problems for individual institutions or individual markets.
- *Buffer requirements*: The analysis only includes the capital conservation buffer and G-SII buffers where applicable but excludes countercyclical buffers, O-SII buffers and systemic risk buffers. As, in particular, systemic risk buffers are significantly higher than G-SII buffers in most cases, and apply to a much larger population of banks, the analysis vastly underestimates the actual MREL requirements of institutions across the EU and again masks effects in specific jurisdictions. This further exacerbates the issues already highlighted with respect to Pillar 2 requirements.
- *Deposit-funded banks*[1]*:* The analysis considers the issue of deposit-funded banks, however, does so in an insufficient manner. The EBA chose two thresholds for the identification of a deposit-funded bank (30% and 40%). In our view, this approach is insufficient, as there are banks for which retail deposits represent more than 50% of their funding base. The difference of over 10% of the funding base compared to the most conservative scenario employed by the EBA, and the resulting lack of MREL-eligible liabilities, is again a factor contributing to the underestimation of the overall funding need in the analysis.
- *Calibration scenarios:* The report includes three calibration scenarios with the first and third scenarios described as unrealistic (and therefore for illustrative purposes only). While we agree that scenario 1 could be considered a 'best-case', scenario 3 is still far

[1] Related to this point, we question the construction of Figure 6 in the report, which depicts the composition of MREL for different categories of banks. We assume the 'stacks' represent aggregate data, although this is not clear. More importantly, the stacks (at least those for O-SIIs and Other) would – in our view – look significantly different if disaggregated by jurisdiction, as the preponderance of deposit funded banks in some markets would be evident. As presented at the moment, this graph does not accurately represent the funding structure in many jurisdictions and as such creates an inaccurate picture of the situation in the EU banking sector

removed from a 'worst-case' scenario that could occur on the basis of the current RTS on MREL. Both scenario 2 and scenario 3 include only a standardised Pillar 2 add-on, no countercyclical, O-SII or systemic risk buffers and any buffer requirement (capital conservation and G-SII buffer where applicable) only once in the loss absorption amount. As already outlined above, actual buffer requirements (Pillar 2 and others) are higher than those assumed in the analysis and the EBA RTS also allows for the inclusion of all buffers in the recapitalisation amount. Including significantly higher buffer requirements and including them twice in the total MREL requirement would show the 'real' worst case scenario for European banks (and actually a scenario that is contemplated in interactions with the SRB!) and as such should be quantified as the analysis otherwise underestimates the true effects on the European banking system.

In addition, the EBA mentions at several points in the report that the scenarios 'are likely to be too conservative' for some banks and then makes 'more realistic' assumptions. While we agree with this assessment, the scenarios are also not conservative enough for some banks and a more realistic assumption in their case would result in much higher MREL requirements (this is especially relevant with respect to Pillar 2 add-ons and systemic risk buffer requirements).

As a result of the shortcomings listed above, we believe that the current quantitative analysis is insufficient to convey a true picture of the impact of MREL requirements in the EU. Not only does it lack detail in terms of requirements at individual institution and/or jurisdiction level, 'glossing over' real national differences and issues for banks with particular business models, but it also – in our view – vastly underestimates true funding needs by ignoring significant amounts of buffer requirements and the possibility of the EBA RTS (and emerging practice of some NRAs and the SRB) to require buffers also as part of the recapitalisation amount.

We ask you to give our remarks due consideration.

Yours sincerely,

Dr. Franz Rudorfer
Managing Director
Division Bank and Insurance