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# European Banking Authority One Canada Square (Floor 46)Canary WharfLondon E14 5AA

# EBA Draft Regulatory Technical Standards on criteria for determining the Minimum Requirement for own funds and Eligible Liabilities (MREL) under Directive 2014/59/EU

# Barclays welcomes the opportunity to comment on the EBA’s proposals for Minimum Requirement for own funds and Eligible Liabilities (MREL), and is supportive of the need to ensure sufficient loss absorbing and recapitalisation capacity is available for EU banks in resolution. Please find our overall comments outlined below, followed by our specific responses to the 12 consultation questions (Appendix 1) and a list of technical clarifications we would welcome (Appendix 2).

# Peter Freilinger

# Head of Structural Reform and RRP

Barclays

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# **Overall comments**

# Barclays supports the overall aim of the Minimum Requirement for own funds and Eligible Liabilities (MREL), to ensure that European banks have sufficient bail-inable liabilities to absorb stressed losses and be recapitalised at the point of non-viability. We welcome the EBA’s proposal to take account of resolution strategy and TLAC requirements for G-SIBs in setting MREL, and we agree with the proposal for the resolution authority to take a firm’s prudential capital requirements set by their supervisor as a starting point, rather than undertake an independent assessment.

# As a G-SIB, Barclays will be within scope of the FSB’s global standards for Total Loss Absorbing Capacity (TLAC), and agree with the EBA’s observation that resolution authorities for G-SIBs can implement MREL consistently with the international framework for TLAC. Indeed, we would welcome a broad alignment of MREL with TLAC for consistency across firms and jurisdictions, including instrument eligibility, subordination requirements (to make the bail-in process cleaner and smoother, given the potential legal challenges if instruments excluded from bail-in rank alongside MREL), location and timing.

# Whereas the FSB’s external TLAC requirements apply on a consolidated group basis for firms with a Single Point of Entry (SPE) resolution strategy, with internal TLAC requirements for each material subsidiary, we understand MREL will be applied to such a group and its EU subsidiaries. We would encourage national resolution authorities to confirm how they will view material entities for TLAC under the MREL framework. We would also welcome confirmation that it is permissible to meet subsidiary requirements through a combination of ‘internal MREL’ and external MREL meeting the eligibility criteria, and confirmation that – during transition – external MREL issued by a subsidiary (including senior unsecured debt) can be counted towards the group requirement provided it is included in the consolidated group’s balance sheet.

# Relatedly, where (internal) MREL is ‘downstreamed’ to material subsidiaries via an intermediate entity, and where the applicable regulatory regime includes solo capital requirements, the intermediate entity will attract solo capital charges on funding exposures to its material subsidiaries. This could give rise to level-playing field issues if rules are not applied on a consistent basis internationally. We would therefore ask the EBA to work with the BCBS to consider whether a waiver from intra-group capital requirements, Large Exposure rules and leverage ratio requirements would be appropriate for internal MREL exposures (where not covered by the Basel capital framework).

# We share the EBA’s expectation that (at least some) European regulators will implement the TLAC requirements for G-SIBs using the BRRD’s MREL framework, since this is already in place in national legislation, for example by translating a firm’s binding (RWA or leverage-based) TLAC constraint into a gross-liabilities MREL measure based on the firm’s balance sheet, updated on an annual basis. MREL requirements are expected to apply to European banks from 1 January 2016, whereas the FSB’s proposed TLAC requirements would apply ‘no earlier than 2019’. For European G-SIBs, at least during the MREL period of transition (proposed as 48 months, starting in January 2016), we would urge that instruments which are eligible for MREL in the BRRD (eg senior unsecured term debt, including structured notes and other unsecured liabilities issued by a bank subsidiary) may count towards the MREL (TLAC) requirement, even if they would not be eligible for TLAC once the final rules are applied (ie if subordination, contractual PONV, and group regulatory capital qualification is ultimately required).

# In this context, we urge that any requirement to issue contractual bail-in instruments as part of a subsidiary’s internal MREL (BRRD Article 45, 13-14) is not implemented during the transition phase and that authorities have regard to the relative ranking of HoldCo/OpCo creditor rights throughout the transition phase.

# Relatedly, we would ask the EBA to recommend European-wide solutions to underpin the BRRD position that banks’ senior unsecured debt may qualify as MREL, for example encouraging subordination (to operating liabilities) of senior unsecured debt on an EU statutory basis. Otherwise, if national authorities take different positions on the MREL-eligibiity of senior debt (especially for firms with TLAC requirements), this would risk creating an unlevel playing field internationally, with a competitive advantage bestowed on some firms.

# We request that national resolution authorities are clear and transparent to the market on which types of senior liabilities they would be likely to bail in (if needed), and which they would be minded to exercise discretion to exclude from bail-in (depending on prevailing circumstances). This may be different during transition (eg where a large stock of senior debt is outstanding at a subsidiary) as compared to the application of bail-in in an end-state HoldCo SPE model, and we believe more guidance could help to align investors’ expectations of bail-in risk more closely with MREL eligibility, and provide more clarity to holders of other senior liabilities (eg uninsured depositors, structured notes and derivatives).

# With respect to the EBA’s specific MREL proposals, we are concerned that the proposed MREL calibration method would result in excessive requirements through the double inclusion of buffers (in contrast to TLAC proposals of double the minimum capital ratio plus buffers), and that doubling Pillar 2 and buffers would also exacerbate any unlevel-playing field effects arising from national authority discretion. While we acknowledge that loss absorption requirements should be based on regulatory capital requirements, we believe recapitalisation amounts should be based on restoring post-resolution capital to the minimum requirement, with buffers rebuilt over time. With robust stress testing, banks hold enough capital to absorb extreme losses, and in most states of the world, if bank losses were to deplete capital below the regulatory minima, the capital would not be completely exhausted (even before BaU pre-provision profits). Indeed, Basel III introduced more stringent capital and liquidity requirements (so the baseline is stronger), and internal management buffers will also be held on top of minimum requirements.

#  **Appendix 1: Barclays’ response to the individual consultation questions**

1. **The draft text describes comprehensively capital requirements under CRR/CRD IV framework, which includes minimum CET1, AT1 and total capital requirements, capital buffers required by CRD IV, Pillar 2 capital requirements set on a case-by-case basis, and alternative backstop capital measures. The EBA is seeking comments on whether all elements of these capital requirements should be considered for the assessment of the loss absorption amount. Do you consider that any of these components of the overall capital requirement (other than the minimum CET1 requirement) are not appropriate indicators of loss in resolution, and if so why?**

The Basel capital framework, and robust stress testing (including by the ECB and EBA), has ensured that banks have sufficient capital to absorb extreme losses, and in most states of the world, if bank losses were to deplete capital below the regulatory minima, the capital would not be completely exhausted (even before BaU pre-provision profits)[[1]](#footnote-1). We also observe that a bank’s loss absorbing capacity would extend beyond instruments that qualify as regulatory capital (eg legacy capital) or MREL (eg unsecured term debt with less than 12 months remaining maturity). We therefore believe it would be sufficiently prudent to base the assumption of capital to be lost on the minimum capital requirement (rather than that plus buffers), consistent with the FSB’s TLAC proposal.

Regarding the individual elements above the minimum, we note that Pillar 2 is set at the discretion of supervisors and, while this may be tied to expected loss, where it is not (eg for non-Pillar 1 risk types such as interest rate risk in the banking book, lease tail risk, insurance risk etc, and where there is a resolvability component to any Pillar 2 add-ons) it seems inappropriate to include it in the loss absorption component. Other types of capital buffers – such as systemic risk buffers and countercyclical buffers – reflect metrics such as size and interconnectedness, or macroprudential tools used to lean against increases in system-wide risk, rather than expected loss.

The leverage ratio is not designed as an indicator of loss in resolution, but is intended to act as a backstop based on balance sheet size (and is not calculated in a consistent manner across jurisdictions). We therefore do not believe leverage is the best determinant of MREL, but if it is used (and we acknowledge it will form part of the TLAC requirement for G-SIBs), we would ask that leverage is defined on a BCBS consistent basis.

1. **Should the resolution authority be allowed to adjust downwards? What are the specific circumstances under which resolution authorities should allow a smaller need to be able to absorb losses before entry into resolution and in the resolution process than indicated by the capital requirements?**

Yes, we welcome the proposed flexibility for the resolution authority to allow downward adjustments. This could be appropriate if, for example, a firm’s recovery plan (deemed credible by its home regulators) involved the sale of businesses, or the post-resolution group was expected to be smaller and / or less interconnected.

1. **Should any additional benchmarks be used to assess the necessary degree of loss absorbency? If yes, how should these be defined and how should they be used in combination with the capital requirements benchmark? Should such benchmarks also allow for a decrease of the loss absorption amount compared to the institution’s capital requirements?**

No, the loss absorbency benchmarks seem comprehensive.

1. **Do you consider that any of those components of the overall capital requirement are not appropriate indicators of the capital required after resolution, and if so why?**

We agree that the amount of capital required post-resolution should in part depend on the resolution strategy. We believe that in bail-in a firm should be recapitalised to the minimum regulatory capital, with buffers rebuilt over time (within a timeframe determined by the prevailing circumstances), whereas the MREL proposals imply instant replenishment of all buffers in a bail-in, which we are strongly opposed to.

We believe it would be inappropriate to include any Pillar 2 TLAC component for a G-SIB (as translated into MREL) in the post-resolution requirement, since that would reflect any firm-specific impediments to resolvability and in a post-resolution world the firm would have been resolved.

1. **Is it appropriate to have a single peer group of G-SIIs, or should this be subdivided by the level of the G-SII capital buffer? Should the peer group approach be extended to Other Systemically Important Institutions (O-SIIs), at the option of resolution authorities? If yes, would the appropriate peer group be the group of O-SIIs established in the same jurisdiction? Should the peer group approach be further extended to other types of institution?**

Given the vast potential differences in G-SIBs’ balance sheet composition, minimum capital ratios, position in the economic cycle, fiscal and monetary policy being pursued by their home and host governments, recapitalisation requirements will always be different. While a peer-group approach (across all G-SIBs) would provide one comparator, we believe post-resolution capital requirements would more appropriately be set by regulators on a case-by-case basis depending on the firm’s circumstances. We are therefore opposed to the proposal in Article 3(7) to require recapitalisation to at least the median CET1 ratio of a G-SIB peer group, and also consider it inappropriate to base recapitalisation requirements on O-SIIs in a jurisdiction[[2]](#footnote-2).

If, however, a peer-group approach is adopted, we believe peer groups divided by their precise G-SIB capital buffer would be too narrow (it could be only 1-2 other firms).

1. **The approach outlined in Articles 2 and 3 will reflect differences between consolidated and subsidiary capital requirements. Are there additional ways in which specific features of subsidiaries within a banking group should be reflected?**

For SPE firms, where HoldCo is the resolution entity, we believe MREL should be set primarily on a group consolidated basis, with firms able to apply for a waiver from requirements for non-material subsidiaries. Where subsidiary requirements are applied, the subsidiary should be able to meet this wholly or partially through internal MREL issued to the parent, or through external MREL that meets the eligibility criteria.

For MPE firms, with multiple resolution entities, MREL should be held at the resolution entity (subsidiary) level.

Where (internal) MREL is ‘downstreamed’ to material subsidiaries via an intermediate entity, and where the applicable regulatory regime includes solo capital requirements, the intermediate entity will attract solo capital charges on funding exposures to its material subsidiaries. This could give rise to level playing field issues if rules are not applied on a consistent basis internationally. We would therefore ask the EBA to work with the BCBS to establish whether a waiver from intra-group capital requirements, Large Exposure rules and leverage ratio requirements would be appropriate for internal MREL exposures (where not covered by the Basel capital framework).

Finally, we note that certain of the elements of the proposed loss absorption amount and recapitalisation amount are applicable only at the consolidated level, for example the G-SIB buffer and Pillar 2 requirements. Furthermore, leverage requirements are not necessarily applied at the level of subsidiaries. It follows that these requirements should be disregarded when calculating the MREL for subsidiaries.

1. **Do you agree that there should be a de minimis derogation from this provision for excluded liabilities which account for less than 10% of a given insolvency class?**

Yes, we believe a de minimis derogation is appropriate, given the existence of excluded ‘administrative’ liabilities (such as tax liabilities and utility bills), as well as liabilities which the resolution authority may use its discretion to exclude.

Although it is difficult to pin-point precisely the right level, a derogation threshold of at least 10% seems appropriate, since we believe that expected losses for senior creditors in insolvency (which constitutes the No Creditor Worse Off (NCWO) counterfactual) would typically be at least 10% higher than in a resolution which preserved the firm as a continuing business (given the legal and other costs of insolvency and likely firesale of assets). Moreover, if debt is converted to equity (at book value), then this provides more comfort against successful NCWO claims. Alongside the need to take into account the ‘ordinary course of business liabilities’, we would supportive of setting a higher threshold of 15-20%.

1. **Do you agree that resolution authorities should seek to ensure that systemic institutions have sufficient MREL to make it possible to access resolution funds for the full range of financing purposes specified in the BRRD?**

No. Some national authorities may determine that it is not desirable to rely on resolution funds (for a loss ‘tranche’ of 8-13% of liabilities), since this would imply transferring the loss from the firm’s creditors to the banking industry more broadly (which could exacerbate contagion), and increase moral hazard.

We note that the 8.0% refers to allocated losses and not to MREL-eligible liabilities, so it should be possible to bail-in 8% of liabilities with an MREL requirement lower than that (ie some liabilities would not be eligible because they had fallen below 12 months remaining maturity).

1. **Is this limit on the transition period [48 months] appropriate?**

No, we believe a longer transition period (of 5-6 years) would be more appropriate, given the significance of the requirements, likely market capacity constraints and intention to align MREL requirements with TLAC requirements for G-SIBs (where we would welcome alignment of the conformance periods). In determining the transition period, resolution authorities should also have regard to the timing of structural reform programmes for individual institutions, and the challenges of implementing such structural reforms simultaneously with MREL and TLAC requirements.

We urge that any requirement to issue contractual bail-in instruments as part of a subsidiary’s internal MREL (BRRD Article 45, 13-14) is not implemented during the transition phase and that authorities have regard to the relative ranking of HoldCo/OpCo creditor rights throughout the transition phase.

Article 9(2) could also provide that resolution authorities should be required to notify each institution of its planned MREL within a certain period of time before each 12 month period begins, to enable institutions to prepare adequately for the implementation of MREL. We believe the final sentence of Article 9(2) should be amended so that resolution authorities can only subsequently revise planned MREL for future 12 month periods, and so that resolution authorities cannot reduce the length of the transition period or retrospectively increase planned MREL during any 12 month period which has already commenced. Otherwise, there will be significant market uncertainty and issuance planning will be difficult.

1. **Should the resolution authority also set a transitional period for the MREL of banks which are undergoing or have undergone a resolution process?**

Once MREL is depleted in resolution, we would expect the minimum capital requirements to be restored immediately and the buffers to be rebuilt over time, with the timeframe dependent on prevailing circumstances.

1. **Overall, do you consider that the draft RTS strikes the appropriate balance between the need to adapt the MREL to the circumstances of individual institutions and promoting consistency in the setting of adequate levels of MREL across resolution authorities?**

While we acknowledge that some aspects are firm-specific (eg the preferred resolution strategy), overall it seems that – especially if a minimum 8% of total liabilities is required – the MREL proposals would impose a high minimum requirement across the industry, without taking full account of the risk profile of individual firms’ balance sheets.

Where resolution authorities are required to make judgements about whether certain instruments are expected to be excluded from bail-in in setting MREL (eg corporate deposits, structured notes), we feel a consistent approach would assist investors in understanding and pricing risk.

We consider that a key risk to consistency of MREL requirements across Member States is that resolution authorities could specify that, in order to constitute MREL, instruments must contain particular terms in addition to meeting the criteria of Article 45(4) of the Directive. We would ask that the EBA encourages resolution authorities not to impose additional criteria beyond those in Article 45(4) of the Directive, at least until the FSB’s TLAC requirements have been confirmed. Otherwise, there may not be a level playing field across institutions in the Union.

1. **Are there additional issues, not identified in this section, which should be considered in the final impact assessment?**

The impact assessment should take into account the proposed TLAC requirements for G-SIBs (including market capacity issues), and likelihood of this being extended to D-SIBs in due course.

**Appendix 2: Technical clarifications requested**

1. Can the EBA clarify that for SPE firms, what MREL requirements will be applied to subsidiaries (including post-structural reforms), and that a subsidiary can meet its MREL requirements through both internal and external MREL?
2. Will internal MREL issued by a subsidiary need to be subordinated, include contractual PONV clauses and qualify as group regulatory capital to qualify as MREL?
3. Does the EBA expect the BRRD Level 1 text to be reopened on the definition of MREL, in light of the FSB’s proposals on TLAC (eg to align subordination requirements), in the interests of ensuring a level playing field across resolution authorities in the Union?
4. Can the EBA confirm that where legacy capital is not included in regulatory capital, but would still be bailed in, this will count towards MREL (along with any other subordinated liabilities), given its subordination and consistency with the recent EBA guidance for EU banks on (equal) treatment of legacy capital in a bail-in?
5. Can the EBA clarify that for leverage exposure definitions, the BCBS methodology will be followed to ensure harmonised standards?
6. If the Basel 1 floor is included in the MREL calibration, will this be the existing Basel 1 capital floor or the floor in place following the current BCBS consultation?
1. BCBS analysis shows that the mean average of historical losses in a systemic crisis is 7% of RWAs (median 3.7%) with the figures for peak losses during the recent crisis being 5% (mean) and 3% (median) respectively (BCBS: Calibrating regulatory minimum capital requirements and capital buffers: a top down approach, October 2010) [↑](#footnote-ref-1)
2. We understand that in this context O-SIIs means D-SIBs, rather than eg insurance companies and CCPs – which would have different risk profiles and capital needs – and would encourage the EBA to clarify that in the final RTS. [↑](#footnote-ref-2)