BANK OF ENGLAND

Resolution

Consultation Paper

The Bank of England's review of its approach to setting a minimum requirement for own funds and eligible liabilities (MREL)

July 2021

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The Bank of England welcomes comments by 1 October 2021. Please provide those comments by email to: MREL.Review@bankofengland.co.uk

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Introduction

Background

The Bank of England (the Bank), as the UK resolution authority, is responsible for taking action to manage the failure of certain financial institutions[1] and/or their groups (together, firms) – including UK-headquartered banking groups and UK-incorporated banks and building societies – a process known as 'resolution'.[2] Resolution allows the shareholders and unsecured creditors of failed firms to be fully exposed to losses, while ensuring the critical functions of the firm can continue and helping to preserve financial stability. Resolution reduces risks to depositors, the financial system, and public funds that could arise due to the failure of a firm. By ensuring losses will fall on a failed firm's investors, rather than depositors or taxpayers, resolution can both reduce the risk of firm failures by supporting market discipline and limit the impact of failure when it does occur.

The minimum requirement for own funds and eligible liabilities (MREL) is a minimum requirement for firms to maintain equity and eligible debt so that they can be 'bailed in' or otherwise support a resolution should a firm fail.[3] MREL must be set in line with the provisions of the Banking Act, the No. 2 Order and relevant binding technical standards, including the MREL BTS[4]. The purpose of MREL is to help ensure that, when firms fail, the resolution authority can use these financial resources to absorb losses and recapitalise the continuing business and support its restructuring. This reduces the likelihood that governments use public funds to rescue failing banks and in effect 'bail out' their creditors as was the case during the global financial crisis that began in 2007. During that crisis the bailouts were the only means of avoiding the negative consequences that firm insolvencies would have had on their depositors, the wider financial system, and the economy as a whole – in other words, the firms were 'too big to fail'. MREL is therefore a critical element of an effective resolution regime.

1 i) banks, building societies and certain investment firms that are authorised by the Prudential Regulation Authority (PRA) or Financial Conduct Authority (FCA); (ii) parent companies of such firms that are financial holding companies or mixed financial holding companies (holding companies); and (iii) PRA or FCA-authorised financial firms that are subsidiaries of such firms or such holding companies. For the purposes of this document, references to 'group' or 'banking group' should, unless otherwise stated, be interpreted as any group comprising one or more entities referred to in (i) to (iii) whether located and authorised in the United Kingdom or elsewhere.

2 As set out in "Implementation of the Investment Firms Prudential Regime and Basel 3 standards Consultation response" the Government, having consulted with the Bank, the PRA and the FCA, and taking into account consultation responses, has decided to remove FCA regulated EUR 730,000 Initial Capital Requirement firms from the scope of the UK resolution regime. Additional firms brought into the scope of the GBP 750,000 capital requirement will also not be within scope of the UK resolution regime. The changes to the scope of the resolution regime will require changes to the legislation underpinning the UK resolution regime. The Government has announced its intention to deliver this via secondary legislation later in 2021. PRA designated investment firms will continue to remain in scope of the UK resolution regime.

3 The Bank Recovery and Resolution (No. 2) Order 2014 (the No. 2 Order) – requires the Bank to use its power under section 3A(4) of the Banking Act to set a minimum requirement for own funds and eligible liabilities for relevant institutions. The Bank's power of direction applies to: (i) banks, building societies and certain investment firms (institutions) that are authorised by the PRA or FCA; (ii) parent companies of such institutions that are financial holding companies or mixed financial holding companies; and (iii) PRA or FCA-authorised financial institutions that are subsidiaries of such institutions or such parent companies. For the purposes of this paper, references to an 'institution' should in general be taken to also include the entities referred to in (ii) and (iii). The Bank is the United Kingdom's resolution authority, and the PRA or FCA is the competent authority.

4 The MREL BTS means European Commission Delegated Regulation (EU) 2016/1450 as retained in UK law. Technical Standards have been updated by the Bank to reflect the UK's withdrawal from the EU pursuant to the Financial Regulators' Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018, see in particular the Technical Standards (Bank Recovery and Resolution) (Amendment etc.) (EU Exit) (No. 1) Instrument 2019.

Structure of this Consultation Paper

The subsequent sections of this Consultation Paper set out the policy approaches which the Bank is consulting on. The first section sets out the Bank's proposed revisions to its approach to setting resolution strategy thresholds and the calibration of MREL within those thresholds. The second section sets out the Bank's proposed revisions to its approach to MREL eligibility. The third section sets out the Bank's proposed approach to intragroup MREL issues. Finally, the first Annex summarises the responses to the Bank's December 2020 DP, and the second Annex sets out the proposed changes to the text of the MREL Statement of Policy which this document is consulting on.[5]

The Bank's MREL review in the context of regulatory developments

The Bank first published its MREL policy in 2016, updating it in 2018 to reflect the Bank's approach to the intragroup distribution of MREL resources. The Bank reaffirmed in June 2018 that it would review the calibration of MREL and the final compliance date, prior to setting end-state MRELs, having particular regard to any intervening changes in the UK regulatory framework as well as firms' experience in issuing liabilities to meet their interim MRELs.

In light of challenges faced by some firms which are not G-SIBs or D-SIBs but which are currently in scope of stabilisation powers and therefore subject to MRELs in excess of their minimum capital requirements[6], and to enable the Bank to take into consideration the Financial Policy Committee (FPC) and Prudential Regulation Authority (PRA)'s review of the UK leverage ratio framework, in December 2020 the Bank delayed the end-state compliance date for this group of firms by one year, from 1 January 2022 to 1 January 2023.[7]

The Bank issued a Discussion Paper (DP) in December 2020 as the first stage of the MREL Review, and opened up a broad dialogue with interested parties on the development of the MREL framework. Given medium-sized banks and building societies' experience of issuing MREL-eligible instruments, the focus of the DP was on these firms (in this document we refer to the banks and building societies that are currently in scope of the Bank's stabilisation powers but are not G-SIBs or D-SIBs (or their subsidiaries) collectively using the shorthand of 'mid-tier firms').

Having gathered feedback and ideas from stakeholders to inform the Bank's views on the policy choices in the Review, the Bank is now engaging stakeholders on more detailed proposals in this Consultation Paper (CP). The Bank has also taken account of the FPC and PRA review of the UK leverage ratio framework in light of revised international standards, and broader market, technological and regulatory developments. These regulatory developments include the PRA's DP, 'A strong and simple prudential framework for non-systemic banks and building societies'[8] and the PRA's Policy Statement, 'Non-systemic UK banks: The Prudential Regulation Authority's approach to new and growing banks'[9]. The

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5 The second Annex also sets out draft changes to the text of the MREL Statement of Policy which are indicative of the Bank's intention to update the Statement of Policy in due course to reflect the UK's withdrawal from the EU and the end of the transition period, and on-shoring changes to the UK regulatory framework.

6 Pillar 1 plus Pillar 2A or, if higher, any applicable leverage ratio

7 Some mid-tiers firms currently have MREL end-state compliance dates after 2023. For these firms the end-state compliance date is unchanged. For mid-tier firms with their current end-state compliance dates in mid-2022, the delay will be to 1 January 2023.

8 DP1/21 – A strong and simple prudential framework for non-systemic banks and building societies | Bank of England

9 PS8/21 | CP9/20 Non-systemic UK banks: The Prudential Regulation Authority's approach to new and growing banks | Bank of England

Bank has also considered the terms of the UK's withdrawal from the European Union and the impact of extraordinary public health measures on the financial sector.

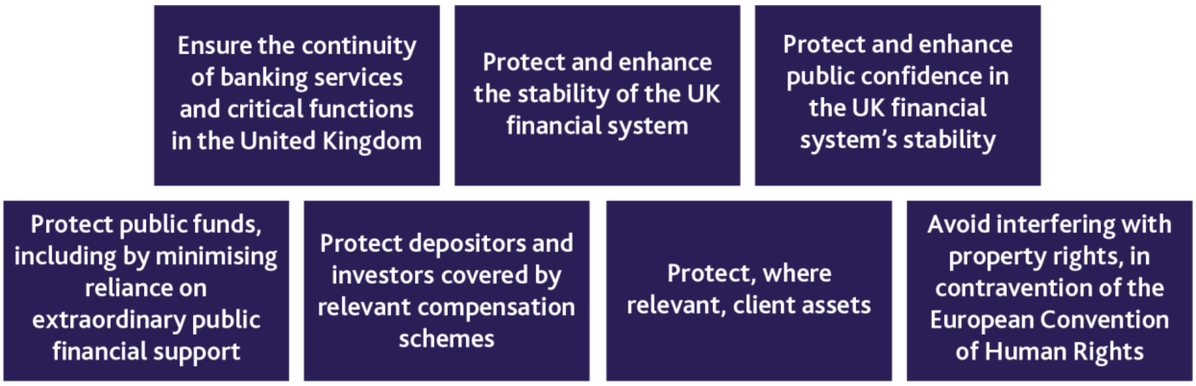
In formulating the proposals in this CP, the Bank has considered the feedback already provided in response to its earlier DP. This feedback is summarised in Annex 1 of this CP. Resolution policy decisions aim, among other things, to reduce risks to public funds in the longer term. As a result, the Bank and HM Treasury work to ensure that risks to public funds are considered as part of policy development. The Bank has therefore consulted on the proposals in this CP with HM Treasury. The Bank has also consulted other relevant authorities namely, the PRA, the Financial Conduct Authority (FCA) and the Financial Services Compensation Scheme (FSCS). The Bank is grateful to all those who responded to the DP, and for the constructive engagement which followed.

The proposals are ultimately intended to help ensure that all firms, including mid-tier firms and major UK firms can be resolved in an orderly manner consistent with the Bank's statutory objective to protect and enhance UK financial stability, as well as the statutory objectives of the UK's special resolution regime to which the authorities must have regard when using or considering the use of stabilisation powers (set out in section 4 of the Banking Act and summarised in **Figure 1** below)[10]. At the same time the proposals are also intended to be proportionate, and to provide firms with a clear, stepped and flexible glide-path to meeting their end-state MRELs.[11]

The Bank's MREL Review has considered the resolution strategy thresholds, the calibration of MREL, instrument eligibility, and the application of MRELs within banking groups. After taking account of the responses to this CP, the Bank's intention would be for changes to be made by the end of 2021 in the form of a revised MREL Statement of Policy to apply from January 2022.

Beyond this timeframe, as with all of its policies, the Bank will continue to keep its approach under review and respond to market developments and broader changes as appropriate.

Figure 1: The special resolution objectives in Section 4 of the Banking Act



The Bank's overall framework for setting MREL

The Bank aims to maintain a fit and ready resolution regime: fit for the purpose of maintaining financial stability and market discipline; and ready to be put into action to deal with the failure of one or more firms. The Bank's overall approach to ensuring resolvability

10 Section 4 of the Banking Act sets out the seven special resolution objectives and provides that they are to be balanced as appropriate in each case.

11 The Bank considers that the proposals do not give rise to equality or diversity implications.

supports financial stability through strong, effective and proportionate standards appropriate for the maintenance of a credible resolution regime.

The Bank sets MREL for individual firms and their groups to achieve one of three broad resolution strategies – modified insolvency (insolvency)[12], partial transfer, or bail-in. These strategies are designed to reflect the scale and nature of the impact of a firm's failure. The Bank determines a resolution strategy for each firm, in line with its legislative obligations including taking into account the expected impact of the firm's failure and the likely impact on the special resolution objectives[13], and sets the firm's MREL to support the effective execution of that strategy. The Bank must ensure that, if a firm met the four conditions for resolution set out in section 7 of the Banking Act[14], it could use the stabilisation powers effectively to resolve the firm in line with the special resolution objectives. The Bank therefore effectively needs to reach a judgment on whether or not, if a firm were to meet the first two conditions for resolution – that is, the firm is failing or likely to fail and it is not reasonably likely that action can be taken to avert that failure or likely failure – the final two conditions would also be met – that is, it is necessary to exercise stabilisation powers having regard to the public interest in the advancement of the special resolution objectives and, if so, that one or more of the special resolution objectives would not be met to the same extent by the winding up of the firm.

If the Bank considers that the winding up of the firm would be feasible and credible (meaning, in effect, that the Bank considers that the final two conditions for resolution would be unlikely to be met), it sets a preferred resolution strategy of insolvency and MREL is set at a level equal to the firm's minimum capital requirements, because there is no need to provide for recapitalisation in insolvency. However, for firms of a certain size, the Bank judges that if they fail, recapitalising them with investors' funds and either allowing them to continue while they address the causes of their failure, or looking to transfer the firm to a private sector purchaser or a bridge bank, would likely be in the public interest as necessary for the advancement of and proportionate to one or more of the special resolution objectives, while winding up of the firm would not meet those special resolution objectives to the same extent. For these firms the Bank sets higher MREL, usually at a level equal to twice the firm's minimum capital requirements. The effect of placing a firm into insolvency on its critical functions and deposits is explored in greater detail in the Bank's December 2020 MREL Review DP.[15]

In order to guide the setting of individual firms' resolution strategies and therefore MRELs, the Bank has published thresholds for MREL above minimum capital requirements. They are indicative and they are structured as ranges (40,000 to 80,000 transactional accounts[16] for

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12 The Banking Act provides for a number of modified insolvency regimes for certain institutions (the bank insolvency procedure (BIP), building society insolvency procedure (BSIP) and the special administration regime (SAR)). The special administration regime is set out in the Investment Bank Special Administration Regulations 2011 issued by HM Treasury pursuant to section 233 of the Banking Act.

13 As set out in section 4 of the Banking Act and discussed further below.

14 "Condition 1 is that the bank is failing or likely to fail.
Condition 2 is that, having regard to timing and other relevant circumstances, it is not reasonably likely that (ignoring the stabilisation powers) action will be taken by or in respect of the bank that will result in Condition 1 ceasing to be met.
Condition 3 is that the exercise of the power is necessary having regard to the public interest in the advancement of one or more of the special resolution objectives.
Condition 4 is that one or more of the special resolution objectives would not be met to the same extent by the winding up of the bank (whether under Part 2 or otherwise)."

15 The Bank of England's review of its approach to setting a minimum requirement for own funds and eligible liabilities (MREL) - Discussion Paper | Bank of England

16 Transactional accounts are defined as accounts from which withdrawals have been made nine or more times within a three-month period.

partial transfer strategies, and total assets of £15bn to £25bn for bail-in strategies) so that the Bank can apply a firm-specific judgment when applying the standards.[17]

At the point of actual failure, the choice of actual resolution strategy will take into account the circumstances of failure and may therefore vary from the preferred resolution strategy adopted during resolution planning. In the event of an actual failure, the Bank may consider it necessary in the public interest to place a firm into resolution despite it having previously set an insolvency strategy due, for example, to wider market dislocation and instability at the point of actual failure. The absence of a willing private sector purchaser might make a bail-in necessary for a firm with a partial transfer strategy.

In setting out the indicative thresholds, and making determinations of resolution strategies for individual firms, the Bank acts in accordance with its legal obligations as resolution authority. MREL must be set in line with the provisions of the Banking Act, the No. 2 Order and relevant binding technical standards, including the MREL BTS. This means, for example, that the indicative thresholds for resolution strategies are different to the thresholds which the PRA uses, for example, to designate certain firms as D-SIBs. Firms which do not meet the D-SIB criteria might still meet the threshold for resolution using stabilisation powers.

Sufficient loss absorbing and recapitalisation capacity is critical to ensure a successful resolution. If a firm were to fail without it, the Bank may be unable to use its resolution powers effectively. The alternative of an insolvency process could have adverse consequences for depositors and for financial stability more broadly.

The Bank requires MREL for firms with a bail-in or partial transfer resolution strategy to be met in the form of statutorily or structurally subordinated resources, and in general MREL must be at least twice the firm's minimum capital requirements. This helps to ensure that there are sufficient resources to allow regulatory capital fully to absorb losses following a conservative valuation of the firm's assets, and to recapitalise the firm to a level sufficient to ensure that it meets minimum capital requirements and commands market confidence. This stabilisation is intended to allow for an orderly restructuring which addresses the root causes of the firm's failure.

It is therefore critical that the Bank sets resolution strategies and MRELs that are consistent with the execution of an orderly resolution in the public interest without recourse to public solvency support, in a sufficiently broad range of possible circumstances. As part of the MREL Review, the Bank has considered whether any factors or developments have altered since the introduction of both the legislative framework for resolution in the Banking Act, and the publication of the MREL Statement of Policy in 2016 (amended in 2018), that might change its risk assessment around this range of circumstances.

Summary of the Bank's proposals in this Consultation Paper

Changes to the transactional accounts threshold: mitigating the risks of disruption in insolvency

The Bank considers that recent innovations in technology in the banking system may afford opportunities to mitigate disruptions that may occur in the insolvency of a failing mid-tier firm whose business model is dominated by transactional account banking. These developments include Open Banking and 'linked accounts' technology.

17 Bank of England (2018a), 'The Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL)', June 2018

The Bank will work with the industry, FSCS, FCA, and PRA with a view to developing alternative processes which may reduce disruption to transactional accounts in the event of an insolvency procedure. Subject to the outcomes of this work, the Bank is considering whether it could significantly raise or remove the transactional accounts threshold. This work would take some time to complete and so the Bank would not envisage being able to make any consequential changes to resolution strategies and MRELs for individual firms before end-2022 at the earliest.

Changes to the total assets threshold: stepped glide-path approach for 'growing into higher MREL'

The Bank remains of the view that above £15-25 billion total assets, a bail-in strategy that provides for the continuity of banking services is more likely to be appropriate. Some respondents to the Bank's December 2020 DP suggested the threshold could be raised significantly, noting international comparisons. The Bank considered these perspectives. Taking into account the special resolution objectives, the Bank considers that entry into insolvency of a firm of that size would be unlikely to serve the public interest effectively, and MREL is therefore required to support a bail-in resolution strategy.

However, the current total assets threshold is an indicative range and we have, since the introduction of the MREL policy in 2016, observed a wider range of business models of firms of this scale, and those seeking to grow into this threshold. Currently, in determining its case-by-case assessment of when a firm should be required to meet MREL in excess of minimum capital requirements, the Bank focuses on the firm's business model, scale and complexity. The Bank's proposals seek to respond to industry feedback that it is at times difficult for firms to access funding markets, and that imposing MREL in addition to minimum capital requirements at the end of a minimum three year notification period creates a regulatory cliff-edge.

The Bank is therefore proposing to modify its approach to setting MREL for new and growing firms which project themselves to grow in size beyond £15bn total assets, to provide as much advance certainty as possible to firms – the Bank expects a minimum of three years – of the point in time at which they will have to start their transition to meeting end-state MREL in excess of minimum capital requirements, as well as the transition itself.

This CP sets out a proposed 'stepped glide-path' for new and growing firms with increased transparency and predictability of requirements to support firms planning their access to funding markets and retention or otherwise of earnings. Firms will now have six years starting from the point at which their transition to end-state MREL begins to meet their end-state MREL in full, with two intermediate steps to smooth the cliff-edge. In addition firms will be able to apply for a 'flexible add-on' of up to a further two years should market conditions or other circumstances warrant an extension. Granting this add-on will be at the Bank's discretion acting in accordance with its legal obligations, including the obligation that the transitional period for a firm is as short as possible. The current population of mid-tier firms who are currently subject to MREL in excess of minimum capital requirements may also request the two year flexible add-on. The Bank does not expect to grant the flexible add-on to mid-tier firms that have met end-state MRELs. Firms growing towards the total assets threshold should therefore have at least three years' advance notice of when their transition to end-state MREL will start, and then between six to eight years to reach end-state MREL.

The proposals for a 'stepped glide-path' and 'flexible add-on' are each designed to recognise the experience of growing firms and their ability to access MREL investors, support funding market efficiency and reduce uncertainty.

Impact on public funds

One of the key purposes of resolution is to reduce risks to public funds. Under the UK special resolution regime, HM Treasury has sole responsibility for authorising the use by the Bank of England of any stabilisation power which would have implications for public funds.[18][19] Consistent with the Memorandum of Understanding between the Bank and HM Treasury on Resolution Planning and Financial Crisis Management,[20] in producing this CP the Bank has consulted HM Treasury. HM Treasury supports the Bank's revised approach to setting resolution strategies in the public interest, including the forward-looking total assets threshold above which the Bank would expect to consider setting a bail-in strategy. HM Treasury considers that the Bank's proposed changes to the framework for setting MREL should ensure that the Bank's MREL policy, including the calibration of end-state MREL, continues to provide an appropriate degree of protection of public funds while ensuring a proportionate approach for growing firms.

Proportionality and competition

The resolution regime is a key part of the post financial crisis reforms of the financial system. In setting resolution strategies, and MRELs, for individual firms, the Bank will continue to take into account the Bank's statutory objective to protect and enhance UK financial stability, as well as the statutory objectives of the UK's special resolution regime to which the authorities must have regard when using or considering the use of stabilisation powers and the Bank's general public law duties.

The UK resolution framework is set up by legislation to ensure full engagement between the Bank and PRA at key stages of an individual firm's life cycle, including in the determination of its MREL.[21] Although facilitating effective competition is not one of the Resolution Authority's statutory objectives, in producing this CP the Bank has consulted the PRA, which does have a secondary competition objective to facilitate effective competition in the markets for services provided by PRA regulated firms in carrying out regulated activities. Impacts on competition have therefore been considered in the Bank's assessment of the proportionality of its proposals.

In addition, consistent with the PRA's secondary competition objective, a key principle of the PRA's approach to supervision is that it does not seek to operate a zero-failure regime for firms. Rather, and working with the Bank as resolution authority where required, the PRA seeks to ensure that any firms that fail do so in an orderly manner. As set out in the PRA's DP, 'A strong and simple prudential framework for non-systemic banks and building societies', the PRA considers that effective competition involves the least efficient firms being able to exit the market in an orderly way. The resolution regime, of which MREL is a key component, helps to ensure that this is possible in the event that it is not possible for the firm to exit via a solvent wind down or through a modified insolvency process.

As set out in the FPC and PRA document 'Consultations by the FPC and PRA on changes to the UK leverage ratio framework' (the Leverage Review CP)[22], the FPC is proposing (among

[18] In light of this, the Bank is required to share its assessment of the implications for public funds when sharing individual resolution plans with HM Treasury (section 57B(2)(c) of the Financial Services Act 2012) and the Bank cannot exercise resolution powers over a firm which would be likely to have implications for public funds without HM Treasury's consent (section 78 of the Banking Act 2009).

[19] Chapter 11 of HM Treasury's Code of Practice describes the UK's resolution financing arrangements, which are financed through contributions from industry. Under these arrangements, a certain amount of funding raised from the UK's bank levy will immediately be made available to the Bank of England as necessary (on the Bank's request) to support the exercise of the resolution powers.

[20] HM Treasury (2017a), 'Memorandum of understanding on resolution planning and financial crisis management ', October 2017

[21] See Article 123(7) and Article 126(9) of the No.2 Order

[22] CP14/21 - Consultations by the FPC and PRA on changes to the UK leverage ratio framework | Bank of England

other things) to direct a minimum leverage ratio requirement for major UK firms and firms with significant non-UK assets. For all other firms (including smaller firms), the PRA is proposing to set a revised supervisory expectation. As observed in the Leverage Review CP, applying a supervisory expectation instead of a minimum requirement provides a more proportionate tool to mitigate the risk of excessive leverage for these firms. Importantly, in the Leverage Review CP, the PRA has proposed (among other things) that there would be no automatic consequences for a firm that does not meet the leverage ratio supervisory expectation and that the expectation would not need to be met immediately following resolution. MREL is set with reference to regulatory requirements, not supervisory expectations and the Bank, as resolution authority, confirmed to the PRA that it does not intend to propose changing this approach.

Questions for public consideration and comment

Do respondents have any views on the Bank's proposals on the resolution strategy thresholds and the calibration of MREL?

Do respondents have any views on the Bank's proposals on MREL eligibility?

The Bank would welcome written responses to these questions, or any other relevant observations, by 1 October 2021.

Please provide those responses by email to: MREL.Review@bankofengland.co.uk.

For consultation: the Bank's proposed approach to the resolution strategy thresholds and the calibration of MREL

In light of the DP responses (see Annex), which drew attention to the impact of MREL on mid-tier firms' growth and ability to compete with larger firms, the Bank has explored the potential implications of any decision to increase the indicative resolution strategy thresholds from their current levels. This would likely result in changing the resolution strategy for one or more mid-tier firms to an insolvency procedure. In addition to this, the Bank has also considered the calibration of MREL for firms of various sizes, particularly as they grow through the thresholds.

Changes to the transactional accounts threshold: mitigating the risks of disruption in insolvency

The Bank recognises that there have been market, technological, and consumer behaviour developments that may have a bearing on MREL policy: in particular the definition of transactional accounts for the purposes of the indicative threshold for partial transfer resolution strategies. This is in part due to the emergence of fintech firms and wider socio-demographic changes which have affected the structure of the UK banking system in the last few years.

In the December 2020 DP, the Bank expressed its intention to assess whether the current definition of "transactional accounts" accurately reflects the significance of an account from the perspective of the special resolution objectives. To that end, the Bank asked how it should update its definition of transactional accounts to take account of changes in market structure and customer behaviour.

Some respondents to the DP expressed support for a threshold capturing 'primary' accounts only, e.g. those where a household's main source of income is credited.

Notwithstanding this, under the current framework for depositor protection and preparedness for insolvency, the Bank considers that special resolution objectives would unlikely to be met through the BIP of a firm with a large number of transactional accounts. In particular covered depositors would suffer from:

- temporary lack of access to banking payment services i.e. the ability to make and receive payments;

- temporary lack of access to positive deposit balances with which to make payments; and

- permanent loss of associated account information e.g. payees, standing orders and direct debits, as well as payments history which can inform potential lenders' or creditors' credit decisions.

However, the Bank considers that recent innovations in technology in the banking system may afford opportunities to mitigate disruptions that may occur in the insolvency of a failing mid-tier firm whose business model is dominated by transactional account banking. These developments include Open Banking and 'linked accounts' technology.

The Bank will work with the industry, FSCS, FCA, and PRA with a view to developing alternative processes which may reduce disruption to transactional accounts in the event of an insolvency procedure. Subject to the outcomes of this work, the Bank is considering whether it could significantly raise or remove the transactional accounts threshold. This work would take some time to complete and so the Bank would not envisage being able to make any consequential changes to resolution strategies and MRELs for individual firms before end-2022 at the earliest.

Ahead of these prospective changes being made, the Bank proposes that:

- For firms that may exceed the transactional accounts indicative threshold in the future while the aforementioned review takes place, the Bank will make an institution specific judgement when setting a resolution strategy. In doing so the Bank will consider a number of factors, including if the institution provides significant amounts of transactional banking services or other critical functions. The Bank will endeavour to engage with these firms as early as possible (including pre-authorisation where relevant) and, in line with the approach for firms planning to grow beyond £15bn assets, will provide as much advance certainty as possible to firms (a 'notice period') of the point in time (T) at which they would need to start their transition to meeting MREL, as well as the transition itself. The length of the notice period for these firms may ultimately depend on a firm's transactional accounts growth rate. The Bank may decline to set T if it appears that a stabilisation powers resolution strategy is not likely to be required in the foreseeable future. In this case, the Bank may request that the firm revert to the Bank for a further assessment at a future point in time.

- Firms with a significant amount of transactional accounts that are currently subject to a partial transfer resolution strategy will continue to be so.

- The transition for all firms will be set on an institution specific basis, taking into account relevant factors such as the firm's ability to access funding markets. As a starting point the Bank expects to, where possible, adopt a similar transitional approach to firms who are growing into end-state MREL driven by the transactional accounts threshold as firms who are growing into end-state MREL driven by the total assets threshold.

- All firms subject to MREL in excess of minimum capital requirements will have the option of applying for a 'flexible add-on' of up to a further two years should market conditions or other circumstances warrant an extension. Granting this add-on would be at the Bank's discretion acting in accordance with its legal obligations, including the obligation that the transitional period for a firm is as short as possible. The Bank does not expect to grant the flexible add-on to firms who have met end-state MRELs.

Changes to the total assets threshold: stepped glide-path approach for 'growing into MREL'

Summary

The Bank remains of the view that above £15-25 billion total assets, a bail-in strategy that provides for the continuity of banking services is more likely to be appropriate. Some respondents to the Bank's December 2020 Discussion Paper suggested the threshold could be raised significantly, noting international comparisons. The Bank considered these perspectives. Taking into account the special resolution objectives, the Bank considers that entry into insolvency of a firm of that size would be unlikely to serve the public interest effectively, and MREL is therefore required to support a bail-in resolution strategy. The Bank will take into account the business model and the risks posed to the special resolution objectives when determining the resolution strategy for individual firms projected to grow above the £15bn threshold.

The Bank makes a firm-specific judgement, and the thresholds represent an expression of the Bank's likely approach. Notably, at the point of actual failure, the choice of resolution strategy will take into account the circumstances of failure and may therefore vary from the earlier resolution strategy adopted during resolution planning. For example there may be scenarios where the Bank considers it necessary in the public interest to place a bank into resolution despite it having previously set an insolvency strategy due to wider market dislocation and instability at the point of actual failure. The absence of a willing private sector purchaser might make a bail-in necessary for a bank with a partial transfer strategy.

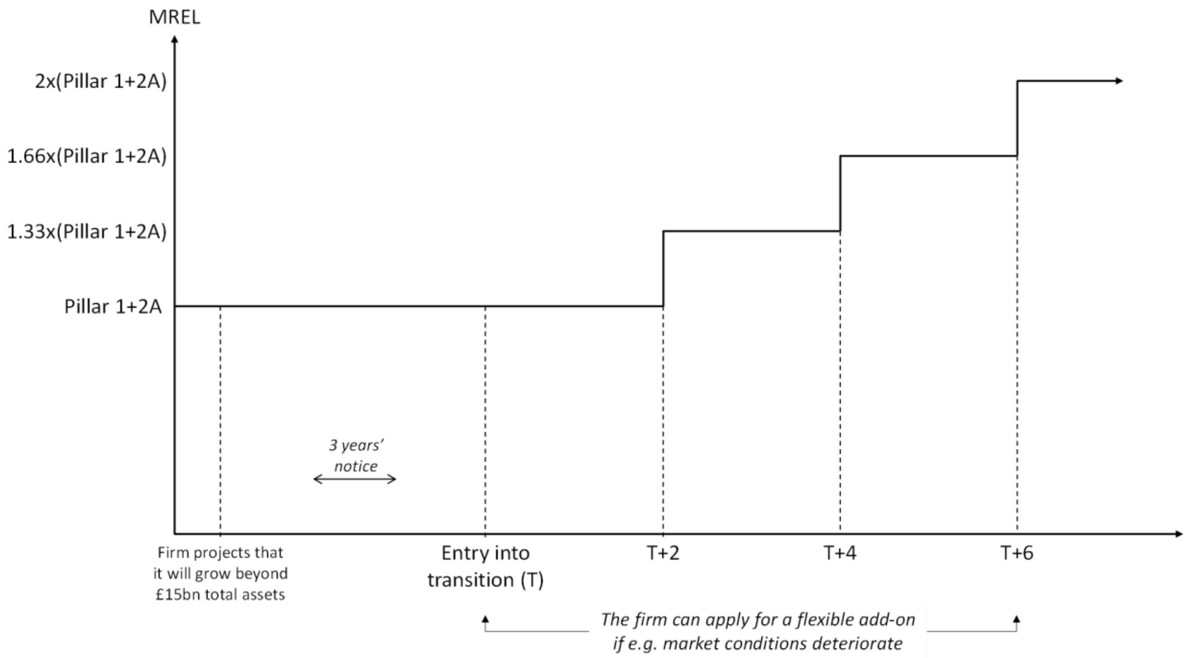
The current total assets threshold is an indicative range and we have, since the introduction of the MREL policy in 2016, observed a wider range of business models of mid-tier firms of this scale, and those seeking to grow into this category. In determining its case-by-case assessment of when firms should be required to meet MREL in excess of minimum capital requirements, the Bank will focus on a firm's business model, scale and complexity. The Bank is therefore proposing to modify its approach to setting MREL for firms which project to grow in size beyond £15bn total assets, to provide as much advance certainty as possible to firms – a 'notice period' of a minimum of three years – of the point in time at which they will need to start their transition to meeting MREL, as well as the transition itself. This does not mean that all firms will need to start building MREL as soon as they plan to grow past £15bn of total assets.

The Bank's proposals seek to respond to industry feedback that it is at times difficult for firms to access funding markets, and that imposing MREL at the end of a minimum three year notification period creates a regulatory cliff-edge. This CP sets out a 'stepped glide-path' with increased transparency and predictability of requirements. Firms will now have six years from the point at which their transition to end-state MREL begins to meet their end-state MREL in full, with two intermediate steps to reduce the scale of the cliff-edge. In addition, firms would be able to apply for a flexible add-on of up to a further two years should market conditions or other circumstances warrant an extension. The current population of mid-tier firms who are currently subject to MREL in excess of minimum capital requirements may also request the two year flexible add-on. Granting this add-on would be at the Bank's discretion acting in accordance with its legal obligations, including the obligation that the transitional period for a firm is as short as possible. The Bank does not expect to grant the flexible add-on to mid-tier firms who have met end-state MRELs. In combination with the above changes, firms growing towards the total assets threshold should therefore have at least three years' advance notice of when their transition to end-state MREL will start, and then between six to eight years to reach end-state MREL.

The Bank's proposals are set out in the table and diagram below:

MREL supported transition for total assets threshold				
Notice Period	**Start of MREL transition**	**Step 1**	**Step 2**	**Step 3**
MREL 0%	MREL 0%	MREL 33%*	MREL 66%*	MREL 100%*
3 years before firm expects to reach £15bn total assets	Date set by Bank (T)	T + 2 years	T + 4 years	T + 6 years
		+ 2 years flexible add-on if needed		

Note: **MREL required* ***in addition to*** *minimum capital requirements, expressed as a percentage of minimum capital requirements*



Detail

The proposed policy would apply to firms in three stages of their growth:

1. Preparing for MREL
2. Building up MREL – the stepped glide-path
3. And a flexible add-on of up to two years if needed

1) Preparing for MREL

The Bank proposes to replace its current indicative range of £15-25bn total assets by a notice period ending on a date by which a growing firm can be expected to enter MREL transition, if the firm plans to grow beyond £15bn total assets.

The Bank would invite firms to approach the Bank when they forecast that their total assets will exceed £15bn in the next three years. For new firms planning to grow quickly, this could happen at the point of authorisation. If the Bank considered that it would be appropriate to set a stabilisation powers resolution strategy for the firm if their business growth plans are brought to fruition, the Bank would then notify the firm of the point in time (T) at which MREL transition will start for that firm. The Bank would determine T on a case-by-case basis and taking into account, among other things, the business model and the criticality of functions it involves. Ordinarily, this would give firms an effective three year notice period before their transition to MREL is expected to start.

The Bank may set T as a point in time at or after the firm expects to surpass £15bn total assets, but would generally not expect to do so before it other than in exceptional circumstances. The Bank may judge that an entry point to MREL which effectively exceeds £15bn total assets is appropriate in the circumstances. In setting T, the Bank may take into account plans to grow the retail or other deposit books.

The Bank may decline to set T if it appears that a stabilisation powers resolution strategy is not likely to be required in the foreseeable future. In this case, the Bank may request that the firm revert to the Bank for a further assessment at a future point in time.

If, during the notice period preceding T, the firm's actual growth and / or business plan deviates significantly from that on which the Bank's determination of T was based, the Bank would expect the firm to notify the Bank. The Bank may then adjust T appropriately. The Bank would expect not to bring T forward to an earlier point in time except in exceptional circumstances, for example, if a firm had experienced sudden growth that was far beyond its initial projections. The Bank may push T back if a firm has not grown as planned; or, if the firm's growth ambitions have been significantly reduced or curtailed, the Bank may decide to withdraw its notification that the firm will enter MREL transition at a specific point of time.

2) Building up MREL – stepped glide path

On the basis of the firm's plans, the Bank will indicate the likely timings of each transitional MREL step (see below).

On notification of a date of expected entry into the MREL transition (T), the Bank will notify the firm of the indicative MRELs that will likely apply during each of its six (or, in some limited cases, more) years of transition to end-state MREL.

Entry into MREL transition (T): the date at which the firm enters MREL transition. For now, MREL as at T will remain equal to minimum capital requirements, but the firm is expected to make plans to reach the indicative MRELs at each of the three following steps.

- Step 1 (T + 2 years): two years after the firm enters MREL transition, MREL steps up to P1+P2A + 33%(P1+P2A).
- Step 2 (T + 4 years): two years after Step 1 (ie four years after T), MREL steps up to P1+P2A + 66%(P1+P2A).
- Step 3 (T + 6 years): two years after Step 2 (ie six years after T), MREL steps up to its end state of P1+P2A + 100%(P1+P2A).

The design of these proposals reflects the considerations outlined in the PRA's DP 'A strong and simple prudential framework for non-systemic banks and building societies', which include the consideration that having prudential requirements which change as firms grow larger or undertake more complex activities could create barriers to growth. The stepped glide-path outlined above ensures that requirements change gradually, without significant cliff-edges, to reduce the risk of this happening.

3) A flexible add-on of up to two years, if needed

In the event that, once a firm has entered MREL transition, a growing business model faces idiosyncratic challenges, or there is market dislocation which weakens debt issuance conditions, firms may request a maximum of an extra two years of additional transition time, to be granted at the Bank's discretion.

The up to two year flexible add-on is made up of two elements and can be used in more than one block of time but may not exceed two years in total over the transition period:

- an element that firms may plan for or be aware of in advance – which they could bring to the Bank's attention for consideration whilst their issuance plan is being drawn up to support their transition path, e.g. in response to closed periods, the need for issuance sizes with sufficient liquidity;
- events that occur during the course of the transition for which firms should raise a request as outlined below.

In deciding whether or not to grant an add-on the Bank may consider:

- whether the applicant firm had taken all steps and actions that were necessary (prior to any disruptive event occurring during the course of transition) to meet its target by the relevant deadline, including whether the firm has already benefitted from an add-on;
- whether there is market dislocation which impacts debt issuance conditions; and
- whether the firm's business model faces idiosyncratic challenges which justify an extension in the context of the Bank's legal obligations including the Bank's statutory objective to protect and enhance UK financial stability, as well as the statutory objectives of the UK's special resolution regime to which the authorities must have regard when using or considering the use of stabilisation powers.

The Bank would continue to determine whether a firm's business model and scale mean the use of stabilisation powers are appropriate with a view to giving firms three years' notice of that decision. This would remain a firm-specific judgement and not based on a hard total assets threshold. If the policy proposals set out in this consultation are adopted, the Bank would expect those firms who project to grow beyond £15bn total assets in the next three years formally to notify the Bank so that the Bank can then set their MREL transition path appropriately.

Impact of proposals on existing mid-tier firms currently in scope of MREL in excess of minimum capital requirements

The current population of mid-tier firms who are currently subject to MREL in excess of minimum capital requirements may also request the two-year flexible add-on. Granting this add-on would be at the Bank's discretion acting in accordance with its legal obligations, including the obligation that the transitional period for a firm is as short as possible. The Bank does not expect to grant the flexible add-on to mid-tier firms who have met end-state MRELs.

Beyond this, the policy proposals set out in this consultation do not affect the end-state MREL compliance date for mid-tier firms which have already received indicative MRELs in excess of minimum capital requirements.[23]

Calibration

The Bank has also considered its approach to the calibration of MREL in light of the responses to the DP. MREL is designed as the sum of two components:

- First, the loss absorption amount is equal to a firm's minimum capital requirements and is calibrated based on the assumption that all of this capital is lost up to and following the resolution valuation that accompanies a firm's entry into resolution. Although the UK resolution regime envisages placing a failed firm into resolution before it is balance sheet insolvent, the experience of the 2008 crisis was that a valuation of its assets following entry into resolution can uncover additional losses which wipe out any remaining capital.

- Second, the recapitalisation amount must be sufficient to restore the capital that a firm in resolution — or a successor entity to which its critical functions have been transferred — is likely to require to comply with the conditions for authorisation and command market confidence post-resolution. The calibration of the recapitalisation amount of MREL and quality of MREL is dependent on whether the preferred resolution strategy for an institution is bail-in, partial transfer or insolvency. The Bank is responsible for determining the preferred resolution strategy for each institution. Resolution powers (including the use of the bail-in tool or the partial transfer tool) are only applied if the Bank judges it is in the public interest and is necessary to advance the special resolution objectives. If the public interest test is not met, firms are placed instead into an insolvency procedure

After careful consideration, the Bank is not proposing to change the basic calibration framework for MREL with the consequence of reducing MRELs. MREL is key to achieving credible resolution and thereby the continuity of critical functions to the economy, reducing the social costs of firm failure. The calibration is designed to ensure firms have sufficient loss absorbing capacity (LAC) to support this. In concluding that changes would not be appropriate, we have re-examined how the MREL regime contributes to building up-front confidence that firms will have sufficient LAC.

Whereas the prudential regime is designed to reduce the probability of firm failure, the resolution regime is primarily a backstop focused on reducing the impact of failure. The MREL framework is therefore necessarily based on the assumption that a firm has failed, entered resolution, and so requires LAC sufficient to deliver continuity in a bail-in.

The Bank's approach as resolution authority is to avoid acting as a 'shadow supervisor' in setting MREL, for example by substituting its own judgement for that of the PRA. The MREL set by the Bank is therefore a function of:

- With respect to the loss absorption amount: the PRA's judgement on a firm's asset quality in its supervisory review that informs setting minimum capital requirements and;

[23] In light of challenges faced by some mid-tier firms of growing into higher MRELs, in December 2020 the Bank delayed the end-state compliance date for this group of firms by one year, from 1 January 2022 to 1 January 2023.

- With respect to the recapitalisation amount: the PRA's judgement on the amount required to continue to authorise a firm in resolution with a level of capital that commands market confidence.

The current PRA risk appetite for continuing authorisation of firms immediately following resolution is based on minimum capital requirements as described in the FPC's December 2019 Financial Stability Report:

> Minimum capital requirements aim to ensure that banks can continue to operate, even after a stress, with an adequate layer of capital to protect depositors, maintain the confidence of markets and enable an orderly failure without losses to the taxpayer. When a bank does not have sufficient loss-absorbing capacity to meet these requirements, the PRA may judge it to have breached its 'Threshold Conditions'… Once minimum capital requirements have absorbed the losses made by a failed bank, the recapitalisation element of MREL is used to build the capital base of a resolved bank, so that it meets Threshold Conditions.

As set out in the Leverage Review CP, the FPC is proposing (among other things) to direct a minimum leverage ratio requirement for major UK firms and firms with significant non-UK assets. For all other firms (including smaller firms), the PRA is proposing to set a revised supervisory expectation. As observed in the Leverage Review CP, applying a supervisory expectation instead of a minimum requirement provides a more proportionate tool to mitigate the risk of excessive leverage for these firms. Importantly, in the Leverage Review CP, the PRA has proposed (among other things) that there would be no automatic consequences for a firm that does not meet the leverage ratio supervisory expectation and that the expectation would not need to be met immediately following resolution. MREL is set with reference to regulatory requirements, not supervisory expectations and the Bank, as resolution authority, confirmed to the PRA that it does not intend to propose changing this approach.

Case-by-case assessment

The proposals in this CP relate to the Bank of England's general approach to setting MREL, and in particular how firms transition to meeting their end-state MREL. The Bank's general approach may need to take account of the circumstances of particular cases, reflecting the fact that MREL is an institution-specific requirement. For example, the Bank reserves the right, on an institution-specific basis, to set an earlier compliance date during the transition period for interim MRELs and/or end-state MRELs greater than capital requirements, for example where the Bank has concerns about the resolvability of a group or institution or set a shorter notice period to T, if the firm is unable to provide the Bank with sufficient notice of when they expect to exceed the total assets or transactional accounts thresholds. And once firms have met their end-state MRELs the Bank will continue to regularly review, and monitor their compliance with, their MRELs on an individual, case-by case basis.

Impact assessment

The Bank first published a detailed impact assessment of its approach to setting MREL in 2015[24], which was subsequently updated in 2017.[25] The Bank considers that the impact of its MREL policy would not fundamentally change, as a result of the proposals set out in this CP if adopted, compared to its assessments in 2015 and 2017. In particular the annual gross

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[24] Bank of England (2018a), 'The Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL)', June 2018

[25] Bank of England (2017a), 'Internal MREL – the Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL) within groups, and further issues – Consultation on a proposed updated Statement of Policy', October 2017

benefits associated with MREL are likely to continue to exceed the estimated macroeconomic costs of MREL by a considerable margin.[26]

However, as mentioned in the December 2020 DP,[27] the Bank has recently considered potential barriers and costs of issuing MREL for firms of different sizes. Since 2015, UK G-SIBs and D-SIBs have issued more than £250bn in aggregate of MREL-eligible instruments and issuance volumes have remained strong, including throughout the UK's EU withdrawal process and the Covid-19 pandemic. Mid-tier firms instead have issued c.£3.6bn of MREL-eligible debt since 2017. Most mid-tier firms have successfully issued Tier 2 capital instruments and MREL eligible liabilities with a coupon in the range of 1.5% to 4% in the last 3 years. By comparison, UK G-SIBs and D-SIBs have issued such liabilities with coupons in the range of 0.3% to 5%.

Having considered the challenges outlined above faced by mid-tier firms issuing MREL, as well as the responses to its December 2020 DP, the Bank is now consulting on changes to the total asset resolution strategy threshold that would introduce a stepped glide-path for 'growing into MREL'. This proposal would not reduce mid-tier firms' end-state MRELs and, therefore, the Bank continues to estimate that the marginal cost to existing mid-tier firms of holding end-state MREL resources will be c.£270m (2.3% of CET1).[28] However, the stepped glide-path would provide mid-tier firms with more time to reach that target, thereby reducing other barriers to issuing MREL and facilitating a smoother transition to end-state.

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[26] In 2017 the Bank estimated that annual gross benefits associated with MREL were likely to be within a range from 0.3% to 0.9% of annual GDP, while macroeconomic costs of MREL were assessed to be around 0.02% of GDP.

[27] Bank of England (2020a), 'The Bank of England's review of its approach to setting a minimum requirement for own funds and eligible liabilities (MREL)', December 2020

[28] This cost analysis depends crucially on the counterfactual – how much own funds and eligible liabilities would firms hold in any event, if they were not subject to MREL in excess of minimum capital requirements. The costs may also vary between firms. Various regulatory factors, such as for example the Net Stable Funding Ratio (NSFR), and market-based factors (including the need to be resilient relative to large peers) may mean that firms would retain at least some additional MREL resources even if not required to do so by the Bank.

For consultation: the Bank’s proposed approach to MREL eligibility

Further to the amended MREL Statement of Policy published in June 2018, the Bank has considered the risks to resolvability posed by the ongoing existence of regulatory capital instruments issued prior to the application in 2014 of the EU’s Capital Requirements Regulation (CRR)[29], which we refer to as 'legacy capital instruments'. These instruments often contain features, or combinations of features, that could result in the instruments not absorbing loss in the manner intended by the resolution regime.

The Bank, as resolution authority, is reminding firms to consider whether having non-CET1 own funds instruments that do not meet the MREL eligibility criteria, as set out in Section 5 of the MREL Statement of Policy, could create difficulties for resolution.

1. The Bank has a low risk tolerance for legacy capital instruments that are issued by UK entities (including both resolution entities and non-resolution entity UK subsidiaries) that are not governed by UK or EEA30 law and are not subject to statutory or contractual recognition of UK bail-in requirements.

2. Furthermore, the Bank is reminding firms to consider the challenges to resolvability posed by legacy capital instruments that are issued from non-resolution entity UK subsidiaries to holders outside the group and that will be ineligible to qualify as own funds either at the end of the CRR1 transitional period or after 28 June 2025.

The Bank has also considered the MREL eligibility of non-CET1 own funds instruments issued from non-resolution entity subsidiaries to holders outside the group. The Financial Stability Board (FSB)'s TLAC standard provides that these instruments should not count towards external or internal TLAC from 1 January 2022. In 2018, the Bank indicated that the existence from 1 January 2022 of outstanding instruments that meet these criteria, and that are counted as MREL, may lead the Bank to set higher end-state MREL to compensate for those issuances.

Having further considered the challenges to resolvability presented by such instruments, the Bank is consulting on amendments to the MREL Statement of Policy to require that, from 1 January 2022, non-CET1 own funds instruments issued from non-resolution entity UK

[29] Regulation (EU) No 575/2013

[30] Bank of England (2019a), ‘ The Bank of England’s amendments to financial services legislation under the European Union (Withdrawal) Act 2018’, February 2019. This sets out: “3.13 On the question of MREL eligibility of existing EEA law governed own funds and eligible liabilities which do not contain contractual recognition of bail-in clauses, the Bank clarifies the following:
• Consistent with paragraph 5.10 of the Bank’s MREL Statement of Policy, existing non[1]CET1 own funds instruments77 governed by EEA-law may continue to count towards MREL if they do not include a contractual recognition of bail-in term.78 Firms should, however, consider whether having EEA-law governed non-CET1 own funds instruments that do not include contractual recognition of bail-in terms could create difficulties for resolution. The Bank may direct a firm to renegotiate non-CET1 own funds instruments to include a contractual recognition of bail-in term to ensure a UK conversion/write down would be effective.
• Consistent with paragraph 5.8 of the Bank’s MREL Statement of Policy, other EEA law governed eligible liabilities may only count towards MREL if they include a contractual recognition of bail-in term. 3.14 The deadline for firms to meet their end-state MREL is 2022. Prior to this, the Bank requires firms to meet interim MRELs to ensure they build up their MREL resources steadily over time. The Bank is not altering this framework in light of UK withdrawal from the EU.”

subsidiaries to holders outside the group should no longer be eligible to count towards external or internal MREL.

The Bank notes that, in conducting their RAF assessments, major UK firms are expected under PRA Supervisory Statement 4/19 'Resolution assessment and public disclosure by firms' to undertake a forward-looking, realistic assessment of how their preparations for resolution would enable them to achieve the outcomes for resolvability as set out in the Bank's Statement of Policy on its Approach to Assessing Resolvability ('RAF SoP'). In this context, the RAF SoP notes that firms should consider any difficulties that may arise in writing down and/or converting their MREL instruments.

The Bank will assess major UK firms' ability to achieve the three resolvability outcomes set out in the RAF SoP during the first RAF cycle. This will include how firms have assessed risks to their resolvability posed by legacy capital instruments and any mitigating actions that firms have taken or propose to take.

The Bank's proposed approach to intragroup MREL distribution

The Bank proposes to leave its policy on intragroup MREL distribution unchanged. Consequently, no changes are being proposed to the following sections of the MREL Statement of Policy:

- section 6 – MREL in the context of groups;
- section 7 – Internal MREL; and
- section 8 – Internal MREL instrument eligibility.

The Bank's policy on intragroup MREL distribution, including the sections listed above, was updated in June 2018. The Bank is continuing to work with overseas authorities to enhance cross-border resolvability to strengthen the establishment of Single-Point of Entry (SPE) resolution strategies. The Bank will review its policy on intragroup MREL distribution in light of any progress in international engagement.

The largest banking groups in the United Kingdom are subject to legislation which requires them to carry out their core UK financial services activities within a ring-fenced body (RFB) and separate these from certain other activities of the wider group. Where an RFB is part of a material sub-group[31], the Bank's current policy scales the internal MREL for the top entity of the material sub-group at 90%, as a starting point[32]. This approach is intended to ensure that the setting of internal MREL for RFBs is in line with the range set out in the FSB's TLAC standard while minimising the RFB's dependence on the rest of the group, consistent with the PRA's ring-fencing objectives. The Bank is committed to working with overseas resolution authorities to build confidence in each other's resolution regimes. This could help contribute towards circumstances in which this scaling can be reduced in the future.

For groups with UK resolution entities, the MREL Statement of Policy states that the Bank expects that any 'surplus MREL' — the difference in requirements between external MREL and the sum of what must be issued to the resolution entity as internal loss-absorbing resources — should be readily available to recapitalise any direct or indirect subsidiary as necessary to support the execution of the resolution strategy and there should be no legal or operational barriers to this[33]. The Bank's view is that it may be appropriate to consider issues relating to surplus MREL in more detail in the future, including whether to elaborate on its surplus MREL policy. The Bank's approach would be informed by the outcome of the FSB's technical work on the concept of and management approaches to surplus MREL[34] and include consultation with other authorities in crisis management groups (CMGs). The Bank would also take into consideration firm submissions under the resolvability assessment framework (RAF)[35].

31 See para graph 7.4 of the MREL Statement of Policy.
32 Paragraph 7.9 of the MREL Statement of Policy.
33 Paragraph 6.4 of the MREL Statement of Policy.
34 See section 2.3 in Financial Stability Board (2020a), '2020 Resolution Report – "Be prepared"', November 2020
35 Bank of England (2019b), 'The Bank of England's approach to assessing resolvability – a Policy Statement', July 2019

Annex 1: Feedback on the Bank's December 2020 Discussion Paper (DP)

Background

In December 2020, the Bank released a discussion paper (DP) as the first part of the MREL review. The Bank received twenty-two formal responses, including from banks, building societies, industry associations and advisory firms, as well as extensive ad hoc engagement. The Bank would like to thank all respondents for their detailed and carefully considered responses and active engagement in the discussion period. This section discusses the key themes from responses and explains how the Bank has reflected the feedback in this CP.

Respondents provided feedback on the calibration of MREL, resolution strategy thresholds, MREL-eligible issuance, and the application of MRELs within banking groups. While respondents touched on a wide range of issues, a large area of focus was the impact of MREL on mid-tier firms' growth and ability to compete with larger firms.

The proposals in the CP reflect the Bank's careful consideration of respondents' feedback, as well as discussions with the PRA, the FCA, HM Treasury and the FSCS. The proposals aim to strike a balance between addressing respondents' concerns and other stakeholder views, while still meeting the Bank's legal obligations, including the Bank's statutory objective to protect and enhance UK financial stability, as well as the statutory objectives of the UK's special resolution regime to which the authorities must have regard when using or considering the use of stabilisation powers.

Calibration

The DP set out that the calibration of MREL is dependent on whether the preferred resolution strategy for a firm is modified insolvency (insolvency), partial transfer or bail-in. For firms with an insolvency resolution strategy, MREL is set at a level equal to minimum capital requirements. For mid-tier firms with a bail-in or partial transfer strategy, MREL is set at a level equal to twice their minimum capital requirements[36].

Cliff-edge in requirements

Several respondents requested changes to the 'doubling' of MREL as firms would come into scope of bail-in strategies, that is the setting of MREL for firms for whom bail-in is the preferred resolution strategy at a level equal to twice their minimum capital requirements. They viewed the 'doubling' as a cliff-edge increase in requirements for smaller firms that dis-incentivised growth and impeded their ability to compete with larger firms. Some respondents suggested a longer transition and 'stepped' increases to requirements to help address this concern. Several respondents requested greater clarity around when they will become in scope of MREL in excess of minimum capital requirements, noting that the indicative nature of the thresholds and the judgment-based approach to setting preferred resolution strategies gives rise to uncertainty for individual firms as to the point at which their MREL will be set at a level in excess of their minimum capital requirements.

The Bank acknowledges the feedback from smaller, growing firms that MREL presents a cliff-edge and the request for greater clarity around when they will become in scope of partial transfer and bail-in strategies. The Bank's proposals on thresholds and calibration have been developed with a view to addressing this feedback.

Quantum of MREL

Several respondents suggested that the current calibration of MREL was too high for small, growing firms. A number of respondents suggested the Bank explore alternative strategies

36 This may be adjusted for partial transfer to reflect the firm's resolution strategy.

that could lower MREL for smaller firms, such as 'bail-in to wind-down' and 'solvent wind-down'. Some respondents suggested that the calibration was too 'formulaic', and therefore not judgement based, and that regulatory capital requirements provided an over conservative proxy for loss absorption and recapitalisation needs in resolution. A few respondents suggested that recent and upcoming regulatory changes, such as the implementation of Ring-fencing and the RAF, should be reflected in lower MREL.

The Bank considers that the calibration of the amount of end-state MREL remains appropriate. MREL needs to be sufficient to absorb losses and recapitalise the continuing business, in order to allow for an orderly and successful restructuring. While the extent of losses, including those crystallised on the balance sheet following a conservative revaluation, in any actual resolution is inherently uncertain, the Bank considers that the minimum capital requirements continue to provide the most appropriate and consistent guide to loss absorption and recapitalisation needs. The Bank has considered requests to explore alternative strategies that could lower MREL. The Bank notes that solvent wind down (SWD) is a recovery option before entering a resolution.37 The Bank considers that setting a firm's MREL based on a plan to execute a 'bail-in to wind-down' strategy would be inconsistent with a key element of the bail-in tool, which is designed to be used with a view to restoring the viability of the failing firm. Executing such a strategy would also be unlikely to meet the special resolution objectives, in particular to ensure continuity of banking services and to avoid interfering with property rights. The Bank considers that regulatory initiatives, such as Ring-fencing and the RAF, do not warrant changes to MREL: they help to support firms' resolvability but they are not adequate substitutes for sufficient loss absorbing and recapitalisation capacity, because without sufficient capacity a successful resolution cannot take place. Therefore, the Bank is not proposing any changes to its calibration of the amount of end-state MREL.

Review of the UK leverage ratio framework

The DP noted that the FPC and PRC will conduct a review of the UK leverage ratio framework in light of revised international standards once there is further clarity on the new legal framework following the UK's withdrawal from the EU.

Several respondents raised concerns related to the impact on MREL if they were to become in scope of the leverage ratio requirements. Respondents noted that they were more likely to be affected if their assets were 'low-risk' and they were using the internal rating based approach to credit risk. Some respondents suggested modifications to the 'doubling' of minimum capital requirements for MREL so the impact of the leverage ratio requirement is reduced. A few respondents requested that the exemption of central bank exposures should be applied consistently across the MREL and leverage ratio frameworks. The Bank recognises that, if the scope of leverage ratio requirements were to be extended to mid-tier firms, MRELs and leverage ratio requirements could interact so as to increase, potentially significantly, the amount of own funds and eligible liabilities that some firms would need to maintain.

As set out in the Leverage Review CP, the FPC is proposing (among other things) to direct a minimum leverage ratio requirement for major UK firms and firms with significant non-UK assets. For all other firms (including smaller firms), the PRA is proposing to set a revised supervisory expectation. As observed in the Leverage Review CP, applying a supervisory expectation instead of a minimum requirement provides a more proportionate tool to mitigate the risk of excessive leverage for these firms. Importantly, in the Leverage Review CP, the PRA has proposed (among other things) that there would be no automatic

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[37] Bank of England – Prudential Regulation Authority (2021a), 'Supervisory Statement SS3/21 – Non-systemic UK banks: The Prudential Regulation Authority's approach to new and growing banks', April 2021

consequences for a firm that does not meet the leverage ratio supervisory expectation and that the expectation would not need to be met immediately following resolution. MREL is set with reference to regulatory requirements, not supervisory expectations and the Bank, as resolution authority, confirmed to the PRA that it does not intend to propose changing this approach.

Indicative thresholds

The DP set out that, in accordance with European Commission Delegated Regulation (EU) 2016/1075, as retained in UK law, the Bank determines a resolution strategy for each firm, in line with the special resolution objectives. Indicative thresholds guide the Bank's judgment. The current indicative thresholds are 40,000 to 80,000 transactional accounts for partial transfer strategies, and total assets of £15bn to £25bn for bail-in strategies.

Transparency

Several respondents requested greater transparency around when small and growing firms would become in scope of partial transfer or bail-in strategies. Respondents raised concerns around uncertainty created by the thresholds, given they were indicative only and presented as ranges.

The Bank acknowledges the uncertainty for growing firms around when they will become in scope of partial transfer or bail-in strategies. The Bank's proposals on thresholds and calibration have been developed with a view to addressing these concerns.

Adjustments to thresholds

Several respondents requested the thresholds be raised so that they reflect systemic risk and promote growth and competition. Some respondents requested that the indicative threshold of £15-25bn for bail-in be raised to mirror other thresholds in the prudential regime, such as the leverage ratio framework or the ring-fencing regime.

Several respondents requested that the indicative threshold of 40k to 80k transactional accounts be adjusted to take account of market developments. They argued that the threshold be increased to reflect a growing portion of retail customers that have more than one transactional account, making it less likely that depositors would be affected by a firm failure.

Several respondents proposed that burden sharing arrangements that shared the cost of a mid-tier firm failure with industry and/or public funds could provide for the thresholds to be raised. The Bank's proposals on thresholds and calibration have been developed with a view to addressing this feedback.

In response to requests for greater consistency, the Bank considers it appropriate that its indicative thresholds differ from other regulatory thresholds. This difference reflects that the special resolution objectives are different to the objectives underpinning other parts of the framework, such as the FPC's objectives[38] and the PRA's objectives39 in relation to the leverage ratio framework.

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38 Contributing to the Bank's objective to protect and enhance the stability of the UK financial system (primarily by identifying, monitoring and acting to remove or reduce risks to the stability of the whole or significant part of that system, with a view to protecting the resilience of that system) and, subject to that, supporting the economic policy of the Government, including its objectives for growth and employment.

39 A general objective to promote the safety and soundness of the firms it regulates, focusing on the adverse effects that they can have on the stability of the UK financial system. A secondary objective to facilitate effective competition in the markets for services provided by PRA-authorised firms.

MREL-eligible issuance

Several respondents raised concerns around challenges experienced by mid-tier firms in issuing MREL-eligible instruments at a cost competitive with larger peers and compatible with strategic growth plans. In particular, there were strong concerns of refinancing risk during times of market stress. Several respondents noted the cliff-edge increase in MREL when moving to a partial transfer or bail-in strategy. Several respondents requested a longer transition period to give growing firms sufficient time to establish themselves in the debt market and address future refinancing risk.

The Bank acknowledges the challenges of MREL-eligible issuance for growing firms. The Bank's proposals on thresholds and calibration have been developed with a view to addressing this feedback.

MREL in the context of groups

The DP set out that in June 2018, the Bank updated its MREL Statement of Policy to set out its approach to the distribution of loss absorbing capacity within banking groups i.e. internal MREL. Two respondents requested that the internal MREL scalar, including for ring-fenced banking groups, should be set at 75%, which is the lower end of the FSB range of 75-90%.

The Bank's policy on intragroup MREL distribution was updated in June 2018. The Bank is continuing to work with overseas authorities to enhance cross-border resolvability to strengthen the establishment of Single-Point of Entry (SPE) resolution strategies. The Bank will review its policy on intragroup MREL distribution in light of any progress in international engagement. For now, the Bank proposes to leave its policy on intragroup MREL distribution unchanged.

MREL eligibility

One respondent requested clarification on the expectation that institutions should not structure their MREL eligible liabilities in a way that creates incentives for the issuer to redeem them ahead of the contractual maturity date. The respondent requested that the Bank clarify that the expectation applies only at the point of a new issuance, and not subsequently, such as at the time of a tap.

The Bank considers that the responsibility for ensuring that liabilities, including own funds instruments, are eligible as MREL rests with institutions. The Bank is not proposing any changes to this approach.

Competition objective

Two respondents suggested that the Bank, as a resolution authority, should have a competition objective. This would be consistent with the PRA's secondary competition objective.

The statutory objectives of the UK's special resolution regime are set out in the Banking Act in the form of the special resolution objectives. The PRA's general objectives are set out in the Financial Services and Markets Act 2000, including a secondary objective to facilitate effective competition in the markets for services provided by PRA-authorised firms in carrying out regulated activities. As a public authority the Bank is also under general public law duties governing the actions of public bodies. The UK resolution framework is set up by legislation to ensure full engagement between the Bank and PRA, at key stages of an individual firm's life cycle, including in the determination of its MREL.[40] Impacts on competition are therefore considered in the Bank's assessment of the proportionality of its

40 See Article 123(7) and Article 126(9) of the No.2 Order

proposals and the Bank aims to ensure that the policy benefits derived from the requirements it sets are proportionate to the costs or burden placed on firms.

Any changes to the statutory framework governing the Bank as a resolution authority would be a matter for HM Government and Parliament to consider, and as such would be outside the scope of the Bank's MREL Review.

Future reviews

A few respondents requested that the MREL Statement of Policy and the approach to mid-tier firms be reviewed again in a few years' time to reflect market and regulatory developments.

As with all of its policies, the Bank will continue to keep its approach under review and respond to market developments and broader changes as appropriate.

Further issues

The Bank's publication of interim and end-state MRELs

One respondent commented that they were unable to reconcile the Bank's annual publication of interim and end-state MRELs with UK firms' own disclosures.

This CP focuses on resolution strategy thresholds, the calibration of MREL, instrument eligibility, and the application of MRELs within banking groups. Comments on the annual publication of interim and end-state MRELs are therefore not addressed in this CP. However, the Bank will consider feedback ahead of the next publication of interim and end-state MRELs. The annual interim and end-state MREL publication can be found on the Bank's website.[41]

Comparison with international standards

Several respondents noted that the UK's indicative thresholds were lower than those in other jurisdictions, thereby creating a disadvantage for UK-based firms. Respondents noted that in the US, the requirement to have recapitalisation capacity applies only to US G-SIBs and the US operations of the largest and most systemic foreign banking organisations. In the European Banking Union, the threshold is set at €100bn.

The Bank considers that differences in jurisdictions' approaches may reflect local banking markets and the differences across jurisdictions in the plausibility of finding a willing buyer for a failing firm; the authorities' risk appetite for the disruption caused by insolvency; and the scope to use alternative sources of recapitalisation capacity, including the potential use of public funds. The Bank provided a detailed international comparison on thresholds in Box 3 of the DP.

Environmental, Social and Governance (ESG) bonds

One respondent suggested that the MREL framework be used to help with the transition to a low carbon economy, specifically by incentivising institutions to raise ESG-linked MREL.

The Bank considers that the responsibility for ensuring that liabilities, including own funds instruments, are eligible as MREL rests with firms. In this context, firms may wish to structure their MREL-eligible instruments to include ESG-linked features. The Bank reminds firms that they are expected to be able to demonstrate compliance with the eligibility criteria on request.

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41 https://www.bankofengland.co.uk/financial-stability/resolution/mrels

Building Societies Act (1986)

One respondent requested that the Building Societies Act (1986) be amended to exclude Eligible Liabilities from the calculation of the funding limit (under the Act, Own Funds are already excluded). The Bank notes that this relates to legislative change and is a matter out of scope of the MREL Statement of Policy.

Annex 2: Proposed changes to the text of the Bank's MREL Statement of Policy

Statement of Policy on the Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL)

1 Background and statutory framework(1)(2)

1.1 This Statement of Policy is issued by the Bank of England (the Bank), as UK resolution authority, under section 3B(9) of the Banking Act 2009 as amended (the Banking Act). The Statement of Policy sets out how the Bank expects to use its power to direct a 'relevant person' to maintain a minimum requirement for own funds and eligible liabilities (MREL).

1.2 A 'relevant person' means:

(a) an institution(3) authorised for the purpose of the Financial Services and Markets Act 2000 (FSMA) by the Prudential Regulation Authority (PRA) or Financial Conduct Authority (FCA);(4)

(b) a parent of such an institution which (i) is a financial holding company or a mixed financial holding company; and (ii) is established in, or formed under the law of any part of, the United Kingdom; or

(c) a subsidiary of such an institution or of such a parent which (i) is a financial institution(5) authorised by the PRA or FCA; and (ii) is established in, or formed under the law of any part of, the United Kingdom.

1.3 The Bank is required to set MREL for all institutions. MREL must be set on both an individual institution and group consolidated basis. The Bank may set MREL for certain types of other relevant persons in an institution's group, specifically those entities listed under (b) and (c) above. As required by the Bank Recovery and Resolution (No.2) Order 2014 (the No. 2 Order) the Bank will use its power of direction pursuant to section 3A(4B) of the Banking Act to set MREL, in consultation with the PRA or FCA. References in this Statement of Policy to a 'group' means any group comprising one or more entities referred to in paragraph 1.2 above, whether established and authorised in the United Kingdom or elsewhere.

1.4 MREL must be set in line with the provisions of the No. 2 Order~~, the Bank Recovery and Resolution Directive (BRRD)~~ and the retained EU law version of the European Commission Delegated Regulation (EU) 2016/1450 (the MREL ~~R~~BTS). The Bank will also consider the Financial Stability Board's total loss-absorbing capacity (TLAC) standard ('FSB TLAC standard') when setting MREL.

1.5 The No. 2 Order requires the Bank to set MREL on the basis of the following criteria, which are further specified in the MREL B~~R~~TS:(6)

(a) the need to ensure that the institution can be resolved by the application of the stabilisation powers including, where appropriate, by making special bail-in provision within the meaning of section 48B of the Banking Act 2009~~the bail-in tool~~, in a way that meets the resolution objectives;

(1) This SoP should be read in line with Appendix 3.1 of PS 5/19 (see https://www.bankofengland.co.uk/paper/2019/the-boes-amendments-to-financial-services-legislation-under-the-eu-withdrawal-act-2018MREL), which sets out that firms should interpret non-binding EU materials them "in light of the UK's withdrawal from the EU and the end of the transition period, and onshoring changes that are being made to ensure that the UK regulatory framework operates appropriately." Firms should also "interpret the Guidelines and Recommendations in light of the use of any relevant transitional relief"

(2) This draft SoP is indicative of the Bank's intention to update the Statement of Policy in due course to reflect the UK's withdrawal from the EU and the end of the transition period, and onshoring changes to the UK regulatory framework.

(3) For the purposes of this Statement of Policy the term 'institution' means UK-incorporated banks, UK-incorporated building societies and investment firms, as defined by section 258A of the Banking Act 2009~~those UK-incorporated investment firms that are required to hold initial capital of €730,000, in particular those that deal as principal~~. References in this Statement to an 'institution' shall, in general and unless otherwise stated, be taken to also include 'relevant persons'.

(4) The PRA and FCA are the UK competent authorities. According to article 2 of the ~~Bank Recovery and Resolution Directive (2014/59/EU) and article 4 of the Capital Requirements Regulation (EU No. 575/2013), 'competent authority' means a public authority or body officially recognised by national law, which is empowered by national law to supervise institutions as part of the supervisory system in operation in the Member State concerned~~ No. 2 Order 'competent authority' means the supervisor of an authorised person under FSMA.

(5) The term 'financial institution' has the meaning given by article 4 (1) (26) of Regulation 575/2013/EU as it forms part of retained EU law.

(6) In accordance with the MREL BTS, the Bank may reduce MREL to take account of the amount which the UK deposit guarantee scheme is expected to contribute to the financing of the preferred resolution strategy.

(b) the need to ensure, in appropriate cases, that the institution has sufficient eligible liabilities to ensure that, if mandatory reduction provision within the meaning of section 6B of the Banking Act 2009 or special bail-in provision were made~~the bail-in tool were to be applied~~, losses could be absorbed and the capital~~common equity Tier 1 (CET1)~~ ratio and, as applicable, the leverage ratio of the institution could be restored to a level necessary to enable it to continue to comply with the conditions for authorisation under Part 4A of the Financial Services and Markets Act 2000 (FSMA) and to continue to carry out the activities for which it is authorised ~~under the Capital Requirements Directive 2013/36/EU (CRD4) or the Markets in Financial Instruments Directive 2014/65/EU (MiFID2)~~ and to sustain sufficient market confidence in the institution or entity;

(c) the need to ensure that, if the resolution plan anticipates that certain classes of eligible liabilities might be excluded from bail-in under section 48B(10) of the Banking Act 2009~~article 44(3) of the BRRD~~ or that certain classes of eligible liabilities might be transferred to a recipient in full under a partial transfer, the institution has sufficient other eligible liabilities to ensure that losses could be absorbed and the capital~~CET1~~ ratio and, as applicable, the leverage ratio, of the institution could be restored to a level necessary to enable it to continue to comply with the conditions for authorisation and to continue to carry out the activities for which it is authorised ~~under CRD4 or MiFID2~~;

(d) the size, the business model, the funding model and the risk profile of the institution;

~~(e) the extent to which the Deposit Guarantee Scheme could contribute to the financing of resolution in accordance with article 109 of the BRRD;~~

~~(f)~~(e) the extent to which the failure of the institution would have adverse effects on financial stability, including due to its interconnectedness with other institutions or with the rest of the financial system, through contagion to other institutions.

1.6 MREL is an institution-specific requirement, and the Bank will set MREL with the goal that individual institutions and groups can be resolved consistently with the resolution objectives under a preferred resolution strategy. This Statement of Policy describes the general framework the Bank will use when setting MREL, but is not definitive of any given relevant person's MREL.

~~1.7 Where an institution has significant branches or subsidiaries in one or more European Economic Area (EEA) states, its MREL may be subject to joint decision in a resolution college. MREL determined in line with this Statement of Policy would be the Bank's preferred outcome of that joint decision process.~~

Interaction of MREL and the capital framework

~~1.8~~ 1.7 The PRA has published a supervisory statement on the interaction of MREL and the capital framework.(1) The statement sets out the PRA's approach to:

(a) the interaction of MREL and the capital framework; and

(b) the interaction of MREL and the PRA Threshold Conditions.

~~1.9~~ 1.8 Please consult the PRA's supervisory statement for further details.

2 Definitions and interpretation

2.1 'Own funds' has the same meaning as in article 4(1)(118) of the retained EU law version of Regulation 575/2013/EU (CRR)(2).

2.2 'Own funds instruments' has the same meaning as in article 4(1)(119) of the CRR.

2.3 'MREL eligible liabilities' means eligible liabilities as defined in the Banking Act 2009 which meet the MREL eligibility criteria set out in this Statement of Policy.

2.4 There are two categories of MREL referred to in this document: 'external MREL' and 'internal MREL'.

2.5 External MREL instruments are issued from a 'resolution entity' in a group, that is to say, the entity

(1) PRA (2020)~~(2016)~~, 'The minimum requirement for own funds and eligible liabilities (MREL) – buffers and Threshold Conditions', PRA Supervisory Statement 16/16, available at ~~. The PRA has consulted on updating Supervisory Statement 16/16 to clarify that the expectations set out in SS16/16 are not intended to create a different buffer requirement from that which is usable in the going-concern regime, available at .~~ https://www.bankofengland.co.uk/prudential-regulation/publication/2016/the-minimum-requirement-for-own-funds-and-eligible-liabilities-mrel-ss

(2) The retained EU law version of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012

that would be subject to the use of resolution powers under the preferred resolution strategy.

2.6 Internal MREL instruments are issued from legal entities in a group that are not themselves resolution entities. They are issued directly or indirectly to the resolution entity in their group.

2.7 In developing the preferred resolution strategies, the Bank will identify the institution within the group (if any) to which the Bank would expect to apply its resolution powers and which would therefore be the UK resolution entity ([1]) for which 'external MREL' is set.

2.8 The group resolution strategy may either rely upon the use of resolution powers only at the parent of the group — known as a single point of entry (SPE) — or may depend upon resolution powers being used at more than one entity within the group — known as a multiple point of entry (MPE).

2.9 Under SPE, the internal MREL will be issued by other entities in the group to the resolution entity. In resolution, the write-down and/or conversion to equity of internal MREL will always result in the whole banking group remaining together as a group during the resolution, although parts of it may in time be wound down or sold off.

2.10 Under MPE, some of the resolution entities may issue MREL eligible liabilities either externally or alternatively to another entity higher up in the group. Where an MPE resolution entity has issued MREL eligible liabilities externally, the write-down and/or conversion of the instrument may cause the sub-group that it heads to separate from the rest of the banking group as part of the resolution. This is because the holders of the external MREL resources issued by these resolution entities may become the new shareholders of that entity, leading to a change in control.

3 Framework for setting MREL

3.1 This section sets out the framework the Bank uses to inform the calibration of an institution's MREL. Section 4 describes additional adjustments which may be made on the basis of the preferred resolution strategy for an institution, Section 5 describes additional criteria which liabilities must meet in order to qualify as external MREL resources, Section 6 sets out the Bank's principles for setting MRELs within groups, Section 7 describes internal MREL scope and calibration, Section 8 sets out internal MREL instrument eligibility, and Section 9 sets out the Bank's approach to the transition to final (end-state) MRELs, including interim requirements.

3.2 The Bank will communicate to institutions or their parent companies ~~annually~~ their resolution strategies, the critical functions([2]) (if any) that they or their group provide, and their external and internal MREL (if any).

3.3 The No. 2 Order and the MREL ~~R~~BTS provide the framework for the calibration of MREL. The Bank will set MREL in accordance with this framework. The MREL B~~R~~TS uses ~~the pre-existing CRD4([3])~~ capital requirements (Pillar 1, Pillar 2A and capital buffer requirements) and any applicable leverage ratio as reference points.

3.4 The Bank will calculate an institution's baseline MREL as the sum of two components: a loss absorption amount and a recapitalisation amount.

Loss absorption amount

3.5 The Bank will set the loss absorption amount to cover the losses that would need to be absorbed up to and in resolution. The starting point in the MREL B~~R~~TS is that the loss absorption amount will equal an institution's 'capital requirements'([4]) (Pillar 1 plus Pillar 2A or, if higher, the institution's applicable leverage ratio) plus its capital buffers (the combined buffer or, where relevant~~binding~~, the PRA buffer).([5])

3.6 The MREL B~~R~~TS gives the Bank the discretion to remove capital buffers from the loss absorption amount if they are deemed not to be relevant to absorbing losses in resolution involving stabilisation powers. The Bank must take into account information received from the PRA or FCA, as the competent authority, relating to the institution's business model, funding model and risk profile.

(1) Those institutions within a group in respect of which the use stabilisation powers (other than third country instrument powers) as defined in the Banking Act 2009 is envisaged under the preferred resolution strategy.

(2) See section 3 (1) of The Banking Act.

~~(3) Capital Requirements Directive (2013/36/EU) (CRD) and Capital Requirements Regulation (575/2013) (CRR) – jointly 'CRD 4'.~~

(4) References to 'capital requirements' mean: (i) the amount and quality of own funds the appropriate regulator (PRA or FCA) thinks the institution should maintain at all times under the overall financial adequacy rule (for PRA-authorised persons the Internal Capital Adequacy Assessment 2.1 PRA Rulebook and for FCA-authorised persons IFPRU 2.2.1R of the FCA Handbook) as it applies on a solo or a consolidated level; and (ii) (if applicable) the minimum leverage ratio in Leverage Ratio 3.1 of the PRA Rulebook.

(5) Please see the PRA Statement of Policy 'The PRA's methodologies for setting Pillar 2 capital'~~Statement on Pillar 2~~ for further details: https://www.bankofengland.co.uk/prudential-regulation/publication/2015/the-pras-methodologies-for-setting-Pillar-2-capital.

3.7 In light of the PRA policy on the interaction of MREL and capital buffers, in particular that CET1 cannot be used simultaneously to meet both MREL and capital buffers, the Bank expects to exclude buffers from the loss absorption amount for institutions subject to that policy. This includes those institutions with a modified insolvency resolution strategy, including those for which the FCA is the sole competent authority. Therefore the Bank expects generally to set the loss absorption amount equal to an institution's regulatory capital requirements.([1])

4 Resolution strategies and external MREL

4.1 MREL will be set to ensure that institutions can be resolved in line with the resolution objectives in section 4 of the Banking Act. In particular MREL will be set to enable the preferred resolution strategy for an institution to be effected. This section outlines key factors the Bank will consider when determining the preferred resolution strategy, and how this determination may affect any external MREL that is set for an institution.

4.2 It is important to note that the actual approach taken to resolve an institution will depend on the circumstances at the time of its failure. The preferred resolution strategy may not necessarily be followed if a different approach would better meet the resolution objectives at the time.

Modified insolvency

4.3 The Banking Act provides for a number of modified insolvency regimes for certain institutions (the bank insolvency procedure (BIP), building society insolvency procedure (BSIP) and the special administration regime (SAR)).([2]) Where an institution can enter one of these modified insolvency regimes at the point of failure, without adversely affecting the achievement of the resolution objectives, the Bank expects to set the recapitalisation component of external MREL at zero. This would mean that an institution's external MREL would be set at a level equal to its capital requirements excluding buffers (Pillar 1 plus Pillar 2A or, if higher, any applicable leverage ratio).

4.4 The Bank will consider a number of factors when determining if it is reasonable to assume that an institution can generally be expected to enter modified insolvency upon failure rather than being resolved using stabilisation powers. Factors indicating that an institution is likely to be able to enter modified insolvency include:

(a) if the institution's failure is unlikely to cause disruption to the wider UK financial system, either directly through the cessation of services it provides or indirectly by negatively affecting confidence in the financial system or similar institutions;

(b) if the institution does not provide significant amounts of transactional banking services or other critical functions, particularly those which depend on continuous access to a service which would not be provided in a modified insolvency. The Bank considers that provision of fewer than around 40,000 to 80,000 transactional bank accounts (accounts from which withdrawals have been made nine or more times within a three-month period) is generally likely to indicate that a modified insolvency would be appropriate.

Partial transfer

4.5 In some cases the Bank may determine that, although modified insolvency would not meet the resolution objectives, an institution could feasibly be resolved without use of the bail-in stabilisation power. Where it is feasible for the critical functions of an institution to be transferred to another entity at the point of the institution's failure, the Bank may determine that use of one or more of the Banking Act's transfer powers is appropriate~~the preferred resolution strategy~~ for the institution.

4.6 Factors indicating that it may be possible to rely on a partial transfer~~ strategy~~, rather than ~~assuming that~~ bail-in~~ would be used~~, include:

(a) if the institution's business and asset/liability structure are sufficiently simple so as to make rapidly separating and transferring critical functions feasible using the Bank's statutory powers;

(b) if the institution's systems are able to provide the necessary information to support a transfer within the required timeframe;

(c) if some or all of the institution's business, assets and liabilities (particularly those associated with critical functions) are reasonably likely to be attractive to a private sector purchaser; and

([1]) As set out in the MREL B~~R~~TS, the loss absorption amount may be adjusted in certain circumstances.
([2]) The special administration regime is set out in the Investment Bank Special Administration Regulations 2011 issued by HM Treasury pursuant to section 233 of the Banking Act.

(d) if the institution is of a size such that the number of potential purchasers is reasonably high.

4.7 The Bank considers that above around £15 billion- £25 billion in ~~– £25 billion~~ ~~in balance sheet size~~ total assets a bail-in strategy is more likely to be appropriate, but will make this assessment on an institution-specific basis.

4.8 Where an institution meets the necessary conditions for a partial transfer resolution strategy to be appropriate, its external MREL will be set taking this into account. The Bank ~~expects to~~may consider the following principal adjustments to external MREL for such institutions relative to that set to enable a bail-in strategy for institutions that are D-SIBs:

(a) Quantum: the recapitalisation component of external MREL might be reduced to reflect the fact that less than the entire balance sheet of the institution will need to be recapitalised at the point of resolution. For example, to the extent that an institution's critical liabilities([1]) represent only a proportion of its total liabilities, the recapitalisation component of external MREL may be reduced to reflect this. The Bank will also consider whether any components of Pillar 2A will cease to be relevant as a result of the transfer.

(b) Subordination: where a partial transfer resolution strategy assumes that only liabilities benefitting from preference in insolvency([2]) will be transferred, the Bank may not require MREL resources to be subordinated to senior operating liabilities. This is because the transfer can allow all non-transferred liabilities to receive *pari passu* treatment in a bank administration procedure. This reduces the risk of breaches of the 'no creditor worse off than insolvency' (NCWO) safeguard which might occur if the bail-in stabilisation power had been applied but exclusions were made for certain senior liabilities.

Bail-in

4.9 The stabilisation power that is most likely to be appropriate for large complex institutions and groups is bail-in. The Bank will consider~~is likely to make use of~~ whether a bail-in strategy is appropriate for institutions and groups with ~~balance sheets~~ total assets above £1~~2~~5 billion. The Bank's case-by-case assessment will depend on each institution's business model, scale and complexity~~, and will also consider whether bail-in is appropriate for smaller institutions, in particular those with balance sheets greater than around £15 billion~~. The Bank expects UK resolution entities subject to a bail-in strategy to ensure that their MREL resources are subordinated to operating liabilities, using structural subordination except in the case of building societies which may use contractual subordination or statutory subordination.([3]) Subordination of MREL resources reduces the risk of breaches of the NCWO safeguard in the event of a bail-in. Further detail is provided in Section 6.

4.10 The Bank ~~currently~~ expects to direct UK resolution entities([4]) in respect of which bail-in is the preferred resolution strategy to comply with the following~~an~~ end-state external MREL, as applicable ~~from 1 January 2022, but subject to review by the end of 2020~~:

a. G-SIBs([5]) will be required to meet an external MREL equivalent to the higher of:

   i. two times the sum of Pillar 1 and Pillar 2A, ie 2x(Pillar 1 plus Pillar 2A); or

   ii. the higher of two times the applicable leverage ratio requirement or 6.75% of leverage exposures (in line with the FSB's TLAC standard).([6])

b. D-SIBs([7]) and any other UK bail-in resolution entities will be required to meet an external MREL equivalent to the higher of:

(1) Those liabilities necessary for the continuity of a critical function.

(2) The ~~BRRD~~Insolvency Act 1986 provides for preferential treatment in insolvency of the part of deposits covered by the FSCS ~~or another EEA deposit guarantee scheme~~, and secondary preference for uncovered eligible deposits of natural persons and small and medium-sized enterprises as well as deposits that would be eligible deposits of natural persons and small and medium–sized enterprises were they not made through branches located outside the UK~~EU~~.

(3) ~~Statutory~~As effected by section 176AZA of the Insolvency Act 1986~~subordination is expected to be possible following the UK transposition of the EU Bank Creditor Hierarchy Directive (2017/2399)~~.

(4) Those institutions within a group in respect of which the use stabilisation powers (other than third country instrument powers) as defined in the Banking Act is envisaged under the preferred resolution strategy.

(5) Global systemically important banks (G-SIBs) as identified by the Financial Stability Board in consultation with the Basel Committee on Banking Supervision and national authorities.

(6) The Bank does not expect that setting a level below the internationally agreed minimum for G-SIBs would be sufficient to ensure market confidence.

(7) *Domestic systemically important banks (D-SIBs)* are ~~those~~ institutions ~~that are subject to the PRA leverage ratio requirement (ie~~ with retail deposits over £50 billion~~)~~ and/or any institutions that are designated as an O-SII (other systemically important institution) by the PRA pursuant to article 131(3) of the Capital Requirements Directive (EU Directive 2019/878 amending Directive 2013/36/EU) (CRD) as implemented in the Capital Requirements (Capital Buffers and Macroprudential measures) Regulations 2014~~Capital Requirements Directive (2013/36/EU)~~, and which have a resolution entity in the United Kingdom.

i. two times the sum of Pillar 1 and Pillar 2A, ie 2x(Pillar 1 plus Pillar 2A); or

ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6.5% if the leverage ratio is 3.25%).

5 External MREL instrument eligibility

5.1 In order for MREL resources to fulfil their intended purpose, it must be practically straightforward for the Bank to apply its stabilisation powers to them, including the bail-in stabilisation power.

5.2 The No. 2 Order sets out a number of requirements that liabilities must meet in order to qualify as MREL eligible liabilities.(1) One of these is that the liability must have an effective remaining maturity (taking account of any rights for early repayment available to the investor) of greater than one year.

5.3 In addition, the Bank expects institutions to consider the overall maturity profile of their externally issued MREL eligible liabilities, and to ensure that temporary difficulties in accessing debt capital markets would not be likely to cause a breach of their MREL. The average maturity of institutions' MREL eligible liabilities may decrease in periods of market stress, and the Bank does not intend to apply a minimum maturity requirement to eligible liabilities beyond that applicable under the No. 2 Order. The Bank may use its powers of direction to further specify eligibility criteria for MREL eligible liabilities for individual institutions.

5.4 The No. 2 Order states that where a liability confers a right to early reimbursement upon its owner the maturity date of the liability shall, for the purposes of determining whether it is an MREL eligible liability be considered to be the first date at which such a right arises. The Bank expects institutions not to structure their MREL eligible liabilities in such a way as to reduce their effective maturity, for example liabilities which create incentives for the issuer to redeem them ahead of the contractual maturity date. An increase in the interest rate payable on a liability (a 'step up') coinciding with an issuer call option is an example of an incentive to redeem in this context. Where liabilities do include such an incentive, the maturity date of the liability shall, for the purposes of determining whether it is an MREL eligible liability, be considered to be the date at which the incentive arises.

(1) See in particular article 123(4).

5.5 An institution should not call or redeem an MREL-eligible liability if that would cause it to breach its MREL, or if the institution is already in breach of its MREL, unless the Bank approves such a transaction. UK resolution entities of G-SIBs and material subsidiaries of non-UK G-SIBs are subject to additional requirements set by the CRR.

5.6 The Bank does not consider liabilities the value of which is dependent on derivatives to be appropriate to qualify as MREL eligible liabilities. The Bank does not consider liabilities which only include put or call options to be dependent on derivatives for this purpose.

5.7 Liabilities subject to contractual set-off or netting arrangements are not appropriate MREL eligible liabilities.

5.8 Where a liability is governed by non-UK~~EEA~~ law,(2) institutions will need to ensure that the liability could absorb losses and contribute to recapitalisation costs in resolution, having regard to the terms of the contract and legal opinions, in line with ~~the BRRD and~~ the contractual recognition of bail-in rules in the PRA Rulebook and FCA Handbook.(3)

5.9 MREL eligible liabilities should be issued externally from the resolution entity, subject to the provision in paragraph 6.6 permitting internal issuance for MPE resolution entities.

5.10 The Bank's view is that institutions should consider whether having non-CET1 own funds instruments that do not meet the eligibility criteria, as described above, could create difficulties for resolution. The resolution authority will want assurance about the quantum of loss-absorbing capacity that will be available should the institution find itself in stress. In cases (either outside or in the course of resolution proceedings) where it is not possible to write down and/or convert the non-CET1 own funds instruments to CET1 using statutory powers,(4) for example instruments governed by non-UK~~EEA~~ law where there is no statutory or contractual recognition of UK bail-in rules, the Bank could determine

(2) As regards liabilities governed by EEA law that were made before the IP completion date, as defined in section 39(1) of the European Union (Withdrawal Agreement) Act 2020, all references in this SoP to liabilities governed by non-UK law should be considered in line with Rules 2.1B and 2.1C of the Contractual Recognition of Bail-in Part of the PRA Rulebook.

(3) See https://www.prarulebook.co.uk/rulebook/Content/Part/211722/09-07-2021~~http://www.prarulebook.co.uk/rulebook/Content/Part/211722/26-10-2016~~ and ~~https://www.handbook.fca.org.uk/handbook/IFPRU/11/6.html?date=2016-06-30~~ https://www.handbook.fca.org.uk/handbook/IFPRU/11/6.html

(4) Under sections 6A to 6D of the Banking Act.

that it needs to use its powers under section 3A of the Banking Act to direct relevant persons to address impediments to resolution, in particular through a direction to endeavour to renegotiate instruments under section 3A(4-5). The Bank may consider the challenges to resolvability presented by such instruments as part of assessing institutions' resolvability, including, where relevant, through the Resolvability Assessment Framework.(1)

5.11 Where own funds instruments issued externally by non-resolution entity subsidiaries count towards group consolidated capital, ~~under BRRD~~ such instruments can count towards group consolidated MREL. The FSB's TLAC standard provides that such externally issued non-CET1 own funds instruments should not count towards TLAC from 1 January 2022. Institutions should consider whether the location of external MREL outside the resolution entity could create difficulties for resolution. The Bank may consider any challenges to resolvability presented by such instruments as part of assessing institutions' resolvability, including, where relevant, through the Resolvability Assessment Framework. ~~The existence f~~From 1 January 2022 ~~of~~ outstanding non-CET1 own funds instruments issued from non-resolution entity subsidiaries to holders outside the group will not be eligible to count towards external or internal MREL~~, that are counted as MREL, may lead the Bank to set higher end-state MREL to compensate for those issuances~~.

5.12 The responsibility for ensuring that liabilities, including own funds instruments, are eligible as MREL rests with institutions. Institutions should obtain independent legal advice on a liability's eligibility, and provide this to the Bank where required.

5.13 In line with the continuous resolvability assessment process and, where relevant, the Resolvability Assessment Framework, institutions will also be expected to demonstrate compliance with the eligibility criteria on request.

6 MREL in the context of groups

6.1 The Bank will set an external MREL at the group consolidated level. In addition, the Bank will set individual MRELs for all institutions within the group. The Bank may also set individual MRELs for relevant persons that are important from a resolution perspective (for example holding companies) on an entity-specific basis. The individual MRELs may be determined on the basis of consolidated or sub-consolidated balance sheets, in addition to an entity's own balance sheet (see paragraphs 7.4-7.5 below).

6.2 The Bank will require groups or institutions in respect of which bail-in is the preferred resolution strategy to structure their liabilities to achieve structural subordination of external MREL resources issued by resolution entities. MREL resources which are structurally subordinated may also be contractually or statutorily~~(2)~~ subordinated. Mutually owned institutions such as building societies may not be able to operate with holding companies without changes to their form of incorporation, limiting their ability to achieve structural subordination of MREL resources. In such cases the Bank expects institutions with a bail-in strategy to issue contractually or statutorily subordinated liabilities to satisfy their MRELs.

6.3 For institutions subject to structural subordination, MREL resources issued externally by resolution entities should not rank *pari passu* with significant amounts of other liabilities that do not meet the MREL eligibility criteria set out in the No. 2 Order and this Statement of Policy. Accordingly, the sum of a resolution entity's liabilities that do not qualify as MREL (excluding liabilities that previously met the MREL eligibility criteria but no longer meet the minimum maturity requirement as referred to in paragraph 5.2 above) should not exceed 5% of the resolution entity's overall external MREL resources. In addition, the sum of those liabilities that do not qualify as MREL in each creditor class should not exceed 10% of the resolution entity's MREL resources in that same creditor class.

Availability of surplus MREL in groups

6.4 Resolution entities will be required to issue external MREL resources at least equal to all the internal MREL resources that are issued to them from their subsidiaries or, in other jurisdictions, equivalent subordinated instruments that can absorb losses and recapitalise a subsidiary, such as through being written down and/or converted to equity, without the use of stabilisation or resolution powers at the subsidiary level ('internal loss-absorbing resources'). For groups with UK resolution entities, the Bank expects that any 'surplus MREL' – the difference in requirements between external MREL and the sum of what must be issued to the resolution entity as internal loss-absorbing resources – should be readily

(1) See 'The Bank of England's Approach to Assessing Resolvability', in particular Chapter 4.

~~(2) Statutory subordination is expected to be possible following the UK transposition of the EU Bank Creditor Hierarchy Directive (2017/2399).~~

available to recapitalise any direct or indirect subsidiary as necessary to support the execution of the resolution strategy and there should be no legal or operational barriers to this. The Bank thinks it is appropriate to consider in more detail the issues relating to surplus MREL, in consultation with other authorities in crisis management groups (CMGs), and may review its approach as part of assessing institutions' resolvability.

External MREL for MPE resolution entities

6.5 For groups with an MPE strategy, the Bank expects that each resolution entity will be set an external MREL or an equivalent requirement if applicable in non-E~~U~~EA jurisdictions. The Bank will set MREL for any UK resolution entity, based on the balance sheet of the local resolution group, in line with the calibration framework set out in this Statement of Policy. As this is external MREL, there will be no scaling of the requirement applicable at a resolution entity even if it issues MREL instruments to another member of its group. This is because each resolution group needs to have sufficient MREL to be self-sufficient in resolution.

6.6 The Bank proposes to permit the resolution entities of UK headquartered groups with an MPE resolution strategy to issue MREL eligible liabilities either to investors outside the group or, alternatively, to another entity higher up in the group provided the Bank is given sufficient assurance that any issuance strategy proposed by an MPE group supports a feasible and credible resolution plan. Where MREL of a resolution entity is issued internally, the Bank will require this internally issued MREL to meet the same eligibility criteria as internal MREL of a material subsidiary.

6.7 A UK resolution entity should not double count MREL resources. In order to achieve this, the Bank expects that the external MREL for a UK MPE resolution entity will be increased by the amount of any MREL or equivalent investments its resolution group has made in its other resolution groups or entities or sub-groups located outside these resolution groups, where the investments are not covered by arrangements that ensure this outcome (such as a capital deductions regime for investments in own funds instruments in subsidiaries).

Group consolidated MREL for MPE groups

6.8 Where it is the home authority for the ultimate parent company of an MPE banking group, the Bank expects to set a consolidated external MREL that the group as a whole must meet, in addition to any requirement that it imposes on the UK resolution entity in respect of its resolution group (which would be calibrated in accordance with Section 4). This is consistent with the FSB's TLAC standard for G-SIBs. It reduces the risk that there will be insufficient MREL if losses arise in parts of the group that have no or low levels of MREL resources.

6.9 Accordingly, where the Bank is the home authority for the ultimate parent of a G-SIB, the Bank proposes that in end-state the group consolidated MREL that would apply to the parent ~~between 2019 and 2022 should~~ reflect the FSB's TLAC standard and therefore constitute the highest of: (i) 18~~6~~% of RWAs; (ii) 6.75% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups and entities or sub-groups located outside these resolution groups. The 'sum of requirements' is the sum of the binding MREL (or equivalent requirement) or capital requirement for each of the resolution groups or other entities or sub-groups outside these resolution groups. ~~From 1 January 2022 it should reflect the highest of: (i) 18% of RWAs; (ii) 6.75% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups and other entities or sub-groups located outside these resolution groups.~~

7 Internal MREL

Scope

7.1 Internal MREL above capital requirements is likely to be necessary only where the Bank considers that the insolvency of the institution would put the Bank's resolution objectives at risk.(1) The Bank expects to set internal MREL above capital requirements for a 'material subsidiary' of a group where either (a) there is a UK resolution entity in the same group which is or will become subject to an external MREL above its capital requirements or (b) in the case of UK subsidiaries of overseas groups, the subsidiary delivers critical functions in the United Kingdom.~~(2)~~

7.2 The Bank expects to set internal MREL equal to capital requirements (where applicable) for institutions that are not material but for which the Bank is required to set MREL.

(1) For example, paragraph 4.4 provides an indicative threshold that institutions with below 40,000-80,000 transactional accounts would have a modified insolvency resolution strategy.
~~(2) See section 3(1) of the Banking Act.~~

7.3 An institution is a 'material subsidiary' if it is incorporated in the United Kingdom, is not a UK resolution entity, and it meets at least one of the following criteria:

a. has more than 5% of the consolidated risk-weighted assets of the group; or

b. generates more than 5% of the total operating income of the group; or

c. has a total leverage exposure measure larger than 5% of the group's consolidated leverage exposure measure; or

d. exceptionally, is otherwise 'material', either directly or through its subsidiaries, to the delivery of a group's critical functions. The Bank will continue to review groups' structures and critical functions to judge if this criterion applies to any entities.

7.4 Internal MREL will generally apply to the parent institution in an existing prudential consolidation or sub-consolidation – where the consolidated or sub-consolidated regulatory group meets the criteria in paragraphs 7.1-7.3 – which will be calculated with reference to its consolidated or sub-consolidated prudential requirements. The consolidation or sub-consolidation which is used to calculate internal MREL in such cases is referred to as a 'material sub-group'. A material subsidiary that heads up such a sub-group will be bound by the higher of its internal MREL calculated on an individual or consolidated /sub-consolidated balance sheet basis.

7.5 Where no prudential sub-consolidation currently exists for a material subsidiary, the Bank reserves the right to require the institution to draw up a sub-consolidated balance sheet to enable the Bank to calculate internal MREL for that material subsidiary on a consolidated or sub-consolidated basis. Such circumstances might arise if the material subsidiary owned a group of subsidiaries that did not meet the conditions for internal MREL themselves but together constituted a significant proportion of the group's risk-weighted assets. This is independent from any decision by the PRA or FCA on whether to set prudential requirements for the material subsidiary on a consolidated or sub-consolidated basis.

Calibration

7.6 The intra-group distribution of internal MREL resources must ensure that sufficient loss-absorbing capacity is pre-positioned within the group to ensure that losses can be absorbed and passed up to the resolution entity or entities from material subsidiaries.

7.7 The Bank expects that internal MREL for a material subsidiary will be scaled in the range of 75% to 90% of the full amount of external MREL that it would otherwise be required to maintain if the material subsidiary were itself a UK resolution entity and its external MREL were set in accordance with Section 4. In deciding whether to set internal MREL for a material sub-group or subsidiary above 75% scaling, the Bank will take into account the following considerations:

- The resolution strategy applicable to the group and the credibility of the resolution plan for delivering it.
- The availability of other uncommitted resources within the group that could be readily deployed to support the material subsidiary.
- The scaling of internal loss-absorbing resources applied by overseas authorities to material subsidiaries located in their jurisdiction.

7.8 These factors allow the Bank to set internal MREL based on discussion with other authorities in CMGs – as envisaged in the TLAC standard, ~~resolution colleges – as required by BRRD,~~ or other forums.

7.9 The largest banking groups in the United Kingdom are subject to legislation([1]) which will require them to carry out their core UK financial services and activities within a ring-fenced body (RFB) and separate these from certain other activities of the wider group. Where an RFB is part of a material sub-group (see paragraph 7.4), the Bank expects to scale the internal MREL for the top entity of the material sub-group at 90%, as a starting point, unless the Bank is satisfied that the wider group has sufficient readily-deployable resources to justify moving to a lower calibration in the 75% to 90% range.([2]) This approach is intended to ensure that the setting of internal MREL for RFBs is in line with the range

(1) The Financial Services and Markets Act 2000, as amended by the Financial Services (Banking Reform) Act 2013.
(2) This may not apply in certain cases, including: (1) where the top entity within an RFB's material sub-group is a resolution entity, it will be subject to external MREL and so scaling will not apply to it; and (2) where the RFB's group has a simple structure, the Bank would not expect to adjust downwards the internal MREL (see paragraph 7.11).

set out in the FSB's TLAC standard while minimising the RFB's dependence on the rest of the group, consistent with the PRA's ring-fencing objectives. The Bank is committed to working with overseas resolution authorities to build confidence in each other's resolution regimes. This could help contribute towards circumstances in which this scaling can be reduced in future.

7.10 Within an RFB's material sub-group, the Bank intends to set internal MREL for individual RFBs in line with the approach for setting internal MREL for other types of material subsidiary.

7.11 For UK groups with a simple structure – for example, a single material subsidiary that sits below a UK resolution entity with few, if any other, subsidiaries – the Bank would not expect to adjust downwards the internal MREL for that UK material subsidiary. This means the internal MREL would be set at 100% of the external MREL that would have applied to the material subsidiary if it were a resolution entity. The Bank would also apply this approach for the top entity of material sub-groups containing an RFB or for an RFB which is not part of a material sub-group if the RFB's group has a simple structure. The Bank's approach will be judgement-based, and decided on a case-by-case basis, giving due consideration to the relationship between the risk profile of a material subsidiary and its wider group. The Bank reserves the right to take appropriate steps using its statutory powers to ensure that MREL is distributed within groups in such a way as to support the group resolution strategy, including, in the case of MPE groups, so as to ensure that a resolution group has sufficient MREL to be self-sufficient in resolution.

7.12 In the case of an institution that is a material subsidiary of a banking group that is not headquartered in the United Kingdom, the Bank will set the amount of internal MREL following discussion with the home authority in CMGs~~, resolution colleges~~ or other forums.

7.13 The Bank expects to propose a quantum for internal MREL for non-UK material subsidiaries – where the host authority has not published regulations or regulatory proposals. In doing so, the Bank expects to be guided by the principles set out in this Statement of Policy.

7.14 A subsidiary or sub-group should only count the internal MREL resources that it issues towards meeting its own internal MREL. Where an institution has subsidiaries that also have internal MREL or equivalent resources, it should ensure that it has sufficient internal MREL resources to match both its own individual MREL as well as the internal MREL or equivalent resources of its subsidiaries. In order to achieve this, the Bank expects that internal MREL for an institution will be increased by the amount of any internal MREL or equivalent investments it has made in other entities in the same group, where the investments are not covered by arrangements that ensure this outcome (such as a capital deductions regime for investments in own funds instruments in subsidiaries).

8 Internal MREL instrument eligibility

8.1 All the eligibility criteria set out in paragraphs 5.2–5.8 that apply to external MREL eligible liabilities apply equally to internal MREL eligible liabilities. The considerations in paragraph 5.10 apply to non-CET1 own funds instruments in respect of internal MREL.

8.2 In addition to these eligibility criteria, internal MREL eligible liabilities will be subject to some additional eligibility criteria in order to achieve their purpose. In summary, these are eligibility criteria relating to:

(1) subordination;

(2) the holder of the instrument;

(3) contractual triggers; and

(4) mismatching of internal and external MREL.

Subordination

8.3 As in the case of eligibility for external MREL liabilities, internal MREL resources must be subordinated to the operating liabilities of the group entities issuing them. This is necessary to ensure that, in converting internal MREL, the Bank is not required to bail-in liabilities that might otherwise rank *pari passu* and which may either be difficult to bail in or would result in a change of ownership of the entity if converted into equity. Internal MREL eligible liabilities will need to be contractually or statutorily~~[1]~~ subordinated. However, if the entity is a holding company, it may be permitted to issue internal MREL instruments as senior liabilities provided that the sum of its liabilities that do not meet the other internal MREL eligibility criteria (excluding liabilities that previously met the internal MREL eligibility criteria but no longer meet the minimum maturity requirement referred to in paragraph 5.2

~~(1) Statutory subordination is expected to be possible following the UK transposition of the EU Bank Creditor Hierarchy Directive (2017/2399).~~

above) do not exceed 5% of the entity's overall internal MREL resources (see Section 6). In addition, the sum of those liabilities that do not qualify as internal MREL in each creditor class should not exceed 10% of the entity's internal MREL resources in that same creditor class.

The holder of the instrument

8.4 Institutions and groups should ensure that the issuance of internal MREL by a material subsidiary or sub-group credibly supports the resolution strategy and the passing of losses and recapitalisation needs to the resolution entity. Internal MREL eligible liabilities must be issued either directly or indirectly via other entities in the same resolution group to the parent resolution entity. The Bank generally expects to accept issuance indirectly to the resolution entity along the chain of ownership, as long as there are no technical obstacles to the resolution entity becoming exposed to losses through this chain. Direct issuance, or indirect issuance to the resolution entity that is not along the chain of ownership, could also be acceptable unless this poses a technical obstacle; for example, there are circumstances in which writing down or converting internal MREL could result in a change of control or if there were significant governance or tax issues as a result.

8.5 As part of resolution planning, the Bank will consider the extent to which subsidiaries' non-CET1 MREL resources are issued to group entities other than their direct parent in relation to their potential effects on a group resolution as well as on post-resolution restructuring options. The Bank will discuss the distribution of MREL resources generally with institutions as part of the process of setting MREL.

8.6 Internal MREL eligible liabilities should be issued internally from non-resolution entity subsidiaries. Where own funds instruments issued externally by a non-resolution entity subsidiary count towards that subsidiary's individual capital requirement,~~ under the BRRD~~ such instruments can count towards that subsidiary's individual internal MREL. The FSB's TLAC standard provides that such externally issued non-CET1 own funds instruments should not count towards internal TLAC from 1 January 2022. Institutions should consider whether the conversion to CET1 of externally issued non-CET1 own funds instruments counting towards MREL could lead to a change in control of a subsidiary. The Bank may consider any challenges to resolvability presented by such instruments as part of assessing institutions' resolvability, including, where relevant, through the Resolvability Assessment Framework. ~~The existence f~~From 1 January 2022,~~ of~~ outstanding non-CET1 own funds instruments issued from non-resolution entity subsidiaries to holders outside the group~~, that are counted as MREL, may lead the Bank to set higher end-state MREL to compensate for those issuances~~ will not be eligible to count towards external or internal MREL.

Contractual triggers

8.7 Internal MREL eligible liabilities must be capable of being written down and/or converted to equity without or ahead of any use of stabilisation or other statutory powers in relation to the entity which issues them.

8.8 As a general matter, the trigger for an internal MREL eligible liability will need to provide the Bank as resolution authority of the material subsidiary with the opportunity to direct an immediate write-down or conversion to CET1 of the instrument, to an extent (which could be in full) determined by the Bank at the time of the triggering, where:

1. any own funds instruments of the material subsidiary have been written down and/or converted into equity pursuant to any statutory or regulatory power linked to the financial condition or viability of the institution; provided that, in the case of eligible liability instruments issued by subsidiaries of non-UK groups, the Bank includes in its direction a statement that the home resolution authority has either consented or has not, within 24 hours of the Bank having given it notice, objected to the write-down or conversion; or

2. a resolution entity in the material subsidiary's group, which is a direct or indirect parent of the material subsidiary, is subject to resolution proceedings in the United Kingdom or elsewhere.(1)

8.9 The contractual trigger should provide the resolution authority of the material subsidiary with the opportunity to direct either a write down or a conversion (as directed by the resolution authority) in the circumstances specified in paragraph 8.8 above. However, the contractual trigger may be limited to provide for only write down or only conversion if institutions can demonstrate to the Bank that this credibly supports the group resolution strategy and the

(1) 'Resolution proceedings' mean the exercise ~~of a resolution tool by a EEA resolution authority (including the use~~ by the Bank of a stabilisation power under the Banking Act~~)~~ or a third country resolution action taken by a third-country resolution authority.

passing of losses and recapitalisation needs to the resolution entity. Institutions should consider whether the specification of only write down or only conversion in the contractual trigger could pose a technical obstacle to resolution; for example, if there are circumstances in which writing down or converting internal MREL instruments could result in a change of control or significant governance or tax issues as a result. The Bank may consider any challenges to resolvability presented by the specification of contractual triggers as part of assessing institutions' resolvability, including, where relevant, through the Resolvability Assessment Framework.

8.10 With respect to non-CET1 own funds instruments, institutions should consider whether the absence of such contractual triggers, covering the circumstances described in (b) in paragraph 8.8 above could create difficulties for resolution. Such contractual triggers support the ability to co-ordinate the write-down and/or conversion of internal MREL instruments across other subsidiaries, where this is deemed helpful to supporting the group resolution, so that all relevant subsidiaries are well-capitalised. In cases (either outside or in the course of resolution proceedings)(1) where it is not possible to write down and/or convert the non-CET1 own funds instruments to CET1 using statutory powers, for example instruments governed by non-UK~~EEA~~ law where there is no statutory or contractual recognition of UK bail-in rules, the Bank may use its powers under section 3A of the Banking Act to direct relevant persons to address impediments to resolution, in particular through a direction to endeavour to renegotiate instruments under section 3A(4-5). The Bank may consider any challenges to resolvability presented by such instruments as part of assessing institutions' resolvability, including, where relevant, through the Resolvability Assessment Framework.

8.11 In the Bank's opinion, there is likely to be significant merit in including the contractual trigger features in a single 'umbrella' agreement. This approach has the benefit of providing greater simplicity, transparency and assurance on the circumstances under which a group's internal MREL or equivalent instruments in other jurisdictions will trigger.

8.12 The particular features of the contractual terms of an institution's internal MREL may depend on the group's or institution's resolution strategy and may require discussion between the group and the Bank. Having confirmed these features, the responsibility for ensuring that instruments, including own funds instruments, are eligible as MREL rests with the institution. Institutions should obtain independent legal advice on a liability's eligibility, and provide this to the Bank where required. Institutions are expected to notify the Bank where they do not intend to include the additional contractual provisions in own funds instruments. In line with the continuous resolvability assessment process and, where relevant, the Resolvability Assessment Framework, institutions will also be expected to demonstrate compliance with the eligibility criteria on request.

Mismatching of internal and external MREL

8.13 The Bank will periodically review the extent to which internal MREL resources of a material subsidiary differ in form – such as equity or debt, currency, maturity, interest rate, and other terms and covenants – from the MREL issued externally from the resolution entity where this may pose risks to the resilience and resolvability of the group. Institutions should notify the Bank if they expect there to be any material change in the form of their internal MREL resources. Institutions should not change the form of their internal MREL resources in any way, such as through cancellation or conversion to equity, that reduces the amount of MREL eligible liabilities, unless the Bank approves such a transaction.

8.14 Where the Bank identifies instruments, including those that are *pari passu* with internal MREL resources, or features or mismatches, that constitute an impediment to successful resolution, the Bank may consider using its powers under section 3A of the Banking Act to direct relevant persons to address impediments to resolvability. The Bank will consult with the competent authority on any actions that the Bank proposes to take under section 3A.

9 Transitional arrangements

~~9.1 General transitional arrangements~~

9.1 The MREL B~~R~~TS allows the Bank to determine an appropriate transitional period for an institution to reach its end-state MREL. The transition period must be as short as possible.

9.2 End-state external MRELs (calculated in accordance with the methodology described in Sections 3 and 4 above) and internal MRELs (calculated in accordance with the methodology described in Section 7 above) will

(1) Under sections 6A and/or 12A of the Banking Act.

apply from the following dates, unless the Bank has notified institutions that a later deadline will apply to them:

a. 1 January 2022 for UK resolution entities of G-SIBs and D-SIBs, as well as material subsidiaries of G-SIBs or D-SIBs that are incorporated in the United Kingdom.

b. 1 January 2023 for UK resolution entities which are not G-SIBs or D-SIBs, as well as material subsidiaries of these institutions that are incorporated in the United Kingdom.

~~9.2~~ 9.3 The clean holding company requirements described in 6.3 will also apply from the same dates.

~~9.3~~ 9.4 ~~To allow institutions flexibility over timing of changes to their capital structures in order to meet MREL, generally the Bank does not expect to direct institutions to maintain MREL greater than its regulatory capital requirements prior to the dates set out in paragraph 9.4 below. The Bank has however provided UK resolution entities (on a bilateral basis) with an indication of the external MREL that is likely to apply at the consolidated level at the end of the relevant transitional period (in the first instance the interim MRELs). The Bank also proposes to provide institutions with an indication of the internal MREL that is likely to apply at the end of the relevant transitional period.~~

The Bank expects institutions to produce a plan for how they intend to meet their MRELs, and to discuss this plan with the Bank and the relevant competent authority (the PRA or the FCA) at the earliest possible opportunity. Relevant persons may also be asked to discuss their plans to meet clean holding company requirements with the Bank and the relevant competent authority (the PRA or the FCA).

~~The Bank currently expects to direct institutions to comply with an end-state external MREL (calculated in accordance with the methodology described in Sections 3 and 4 above) and internal MREL (calculated in accordance with the methodology described in Section 7 above) from 1 January 2022. The clean holding company requirements described in 6.3 will also apply from 1 January 2022. Before that date, relevant persons are expected to make progress towards meeting the clean holding company requirements and may be asked to discuss their plans to achieve this with the Bank and the relevant competent authority (the PRA or the FCA).~~

~~9.4 Notwithstanding paragraph 9.3 above, to ensure that institutions make progress towards meeting their end-state requirements the Bank expects to direct institutions to meet the following interim MRELs and internal MRELs:~~

~~(a) From 1 January 2019 UK resolution entities that are G-SIBs will be required to meet the minimum requirements set out in the FSB TLAC standard, being the higher of 16% of RWAs or 6% of leverage exposures.([1]) At the same time, material subsidiaries of G-SIBs that are incorporated in the United Kingdom will need to meet these minimum requirements multiplied by an institution -specific scalar that is determined by the Bank.([2])~~

~~(b) From 1 January 2020:~~

~~a. UK resolution entities that are G-SIBs or D-SIBs will be required to maintain MREL equal to the higher of:~~

~~i. two times their Pillar 1 capital requirements and one times their Pillar 2A add-ons, ie (2 x Pillar 1) plus (1 x Pillar 2A); or~~

~~ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6.5% if the leverage ratio requirement is 3.25%). G-SIBs in any case must meet a requirement of at least 6% of leverage exposures.~~

~~At the same time, material subsidiaries of G-SIBs or D-SIBs that are incorporated in the United Kingdom will need to meet these minimum requirements multiplied by an institution-specific scalar that is determined by the Bank.~~

~~b. UK resolution entities which are not G-SIBs or D-SIBs, will be required to maintain MREL equal to 18% of RWAs. At the same time, material subsidiaries of these institutions that are incorporated in the United Kingdom will need to meet this minimum requirement multiplied by an institution-specific scalar that is determined by the Bank.~~

~~(1) Leverage exposure shall be calculated on the same basis as the PRA's leverage ratio requirement.~~
~~(2) 'Scalar' refers to the 75%–90% scaling adjustment that the Bank proposes to apply to the MREL calibration that would otherwise apply. This scalar may be 100% for groups with a simple structure.~~

~~9.5 The Bank will, before the end of 2020, review the calibration of MREL, and the final compliance date, prior to setting end-state MRELs. In doing so, the Bank will have particular regard to any intervening changes in the UK regulatory framework as well as institutions' experience in issuing liabilities to meet their interim MRELs.~~

9.5 As set out in the PRA's supervisory statement on the interaction of MREL and the capital framework, the PRA's policies on the interaction of MREL and capital buffers and Threshold Conditions ~~will~~ apply with respect to both interim and end-state MRELs. Please consult Chapter 4 of the PRA supervisory statement for further details.

9.6 The MREL B~~R~~TS allows the MREL applicable to an institution to be reduced where that institution has entered resolution and been subject to stabilisation powers. This allows MREL resources to be 'used' in resolution and for the institution (or its successor entities) to rebuild these resources over time. The Bank expects to reduce the external and/or internal MREL applicable to an institution which has been resolved as necessary, such that the institution would not be in breach of MREL immediately following resolution.

~~**Institution-specific transitional arrangements**~~

~~9.7 The Bank may on an institution-specific basis set an earlier compliance date during the transition period for interim (external and internal) MRELs and/or end-state MRELs greater than capital requirements, for example where the Bank has concerns about the resolvability of a group or institution, or to implement international standards.~~

~~9.8 1.1 The MREL RTS allows the MREL applicable to an institution to be reduced where that institution has entered resolution and been subject to stabilisation powers. This allows MREL resources to be 'used' in resolution and for the institution (or its successor entities) to rebuild these resources over time. The Bank expects to reduce the external and/or internal MREL applicable to an institution which has been resolved as necessary, such that the institution would not be in breach of MREL immediately following resolution.~~

9.7 Institutions and groups forecasting, at any point in time, that their total assets will exceed £15bn in the following three years should inform the Bank. The Bank will notify each of these institutions of the point in time at which their MREL transition will start (T), which will be determined on a case-by-case basis. The Bank may set T as a point in time at or after the firm expects to surpass £15bn total assets, but would generally not expect to do so before it, other than in exceptional circumstances. Ordinarily, this would give institutions an effective three year notice period before their transition to MREL is expected to start. The Bank will also notify each institution of the indicative MRELs that will likely apply to it as it gradually transitions into end-state MREL. These are expected to be set according to a stepped approach:

(1) Step 1 (T + 2 years): two years after an institution enters the MREL transition, MREL steps up to P1+P2A + 33%x(P1+P2A);

(2) Step 2 (T + 4 years): two years after Step 1 (ie four years after T), MREL steps up to P1+P2A + 66%x(P1+P2A).

(3) Step 3 (T + 6 years): two years after Step 2 (ie six years after T), MREL steps up to its end-state of 2x(P1+P2A).

9.8 In addition to the three steps outlined above, once an institution has entered its MREL transition, it may request a maximum of two additional years of transition time (the 'flexible add-on'), which may be granted, in full or in part, at the Bank's discretion. In deciding whether or not to grant any such add-on, the Bank may consider a number of factors which may justify an extension in the context of the Bank's objectives and legal obligations, including that the transitional period for a firm is as short as possible. These include:

a. whether the institution has taken all necessary steps and actions to meet its target by the relevant deadline, including whether it has already benefitted from an add-on;

b. whether there is market dislocation which impacts debt issuance conditions; and

c. whether the institution's business model faces idiosyncratic challenges which justify an extension ~~in the context of the Bank's legal obligations and objectives.~~

9.9 In relation to institutions that exceed, or expect they will exceed, 40,000-80,000 transactional accounts, the Bank will make a case-by-case judgement when setting their resolution strategy and will consider a number of factors, including if the institution provides significant amounts of transactional banking services or other critical functions. The Bank will provide institutions with a notice period, whose length may depend on their transactional accounts' growth rate, and set the point in time (T) at which they would need to start their transition to meeting MREL, as well as the length of the transition itself. The transition will be set on an institution specific basis, taking into account relevant factors, such as the institution's ability to access funding markets. As a starting point the Bank expects, where possible, to adopt a similar transitional approach to institutions that exceed, or expect they will exceed, 40,000-80,000 transactional accounts as institutions that exceed, or expect they will exceed, £15bn of total assets.

9.10 Institutions which are not G-SIBs or D-SIBs that, as at 1 January 2022, have been notified by the Bank that their end-state MREL is expected to exceed capital requirements may also request the flexible add-on mentioned in paragraph 9.8. The Bank may grant the add-on at its discretion, acting in accordance with its legal obligations, including the obligation that the transitional period for an institution is as short as possible. The Bank does not expect to grant the flexible add-on to institutions who have met their end-state MRELs.

9.11 The Bank reserves the right, on an institution-specific basis, to set an earlier compliance date during the transition period for interim and/or end-state MRELs, for example where the Bank has concerns about the resolvability of a group or institution, or set a shorter notice period to T, if an institution is unable to provide the Bank with sufficient notice of when it expects to exceed 40,000-80,000 transactional accounts or total assets of £15bn.

~~9.9~~ 9.12 The Bank may ~~also~~ set further 'transitional' MRELs, including after the end of the initial transitional period, if the necessary MREL for an institution changes. This might occur, for example, if the resolution strategy applicable to the institution changes, or if the regulatory requirements for the institution change in a way that affects its MREL. The Bank will determine the appropriate transitional period on an institution-specific basis~~, and expects to allow at least 36 months for transition for external MREL where the change in MREL is material~~. The Bank would expect to determine similar transitional arrangements for a group's internal MREL as for its external MREL. However, where groups are already subject to external MREL in excess of capital requirements, the Bank will determine the appropriate transitional period to meet internal MREL on an institution-specific basis for any subsidiaries that are newly designated as material.