



BANK OF ENGLAND

November 2016

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

Responses to Consultation and Statement of Policy



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This document contains the Bank of England's final policy for exercising its power to direct relevant persons to maintain a minimum requirement for own funds and eligible liabilities (MREL) under section 3A(4) of the Banking Act 2009.

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1 Introduction

1.1 The Bank of England (the Bank) published a consultation paper⁽¹⁾ in December 2015 describing its proposed policy for exercising its power, under the EU Bank Recovery and Resolution Directive (2014/59/EU) (BRRD) and associated UK legislation, to direct institutions to maintain a minimum requirement for own funds and eligible liabilities (MREL) and to take other steps for that purpose under section 3A(4) of the Banking Act 2009 (Banking Act). This document sets out the Bank's final Statement of Policy (contained in the Appendix) and provides feedback on responses to the consultation.

1.2 The Bank's power of direction applies to: (i) banks, building societies and certain investment firms⁽²⁾ (institutions) that are authorised by the Prudential Regulation Authority (PRA) or Financial Conduct Authority (FCA); (ii) parent companies of such institutions that are financial holding companies or mixed financial holding companies (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 document, references to an 'institution' should, unless otherwise stated, 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.

The purpose of MREL

1.3 Resolution is the process by which authorities can intervene to manage the failure of an institution. During the financial crisis, governments felt compelled to bail out failing banks, rather than risk the negative consequences their disorderly failure would have on the wider economy and financial system, as there were no effective arrangements for resolution in place.

1.4 Following the financial crisis, there have been a number of legislative changes to build comprehensive resolution frameworks. The Bank has published a document setting out its approach to resolution, which describes the UK resolution regime.⁽³⁾

1.5 Under the BRRD the Bank, as UK resolution authority, must develop a preferred resolution strategy for each institution. For smaller institutions, this strategy may simply involve them entering a modified insolvency process together with a pay-out of covered depositors by the Financial Services

Compensation Scheme (FSCS). For larger institutions, for which the use of a modified insolvency process would not meet the resolution objectives due to the potential scale of disruption that would cause, the strategy is more likely to involve the use of stabilisation powers to maintain the continuity of its critical economic functions. In such cases, a necessary condition for resolution to be effective is that a firm's capital position can be stabilised. Any losses incurred on the institution's assets, both before and in resolution, need to be recognised. Once this has been done, and if required by the institution's resolution strategy, the institution's capital position must be restored to a sufficient level to ensure that the institution (or any successor entities) meets any necessary regulatory requirements and commands market confidence. This puts the institution into a stable position from which a reorganisation to address the underlying causes of its failure can be carried out, while maintaining the institution's critical services to depositors and to the wider economy.

1.6 MREL is a minimum requirement for institutions to maintain equity and eligible debt liabilities. The purpose of MREL is to help ensure that when institutions fail the resolution authority can use these financial resources to absorb losses and recapitalise the continuing business. As a result, MREL is a critical element of an effective resolution strategy.

1.7 The Bank will set MREL for individual institutions by reference to three broad resolution strategies. These strategies reflect our legal obligations, judgement of risk over the potential disruption to critical economic functions and need to apply a proportionate approach.

- **Modified insolvency process** — for small institutions, which we assess do not provide services of a scale considered critical and for which it is considered that a pay-out by the FSCS of covered depositors would meet the Bank's resolution objectives. These institutions will have MREL set at the same level as regulatory capital requirements and so

(1) Bank of England (2015), *The Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL): Consultation on a proposed Statement of Policy*; www.bankofengland.co.uk/financialstability/Documents/resolution/mrelconsultation2015.pdf.

(2) For the purposes of the United Kingdom special resolution regime, the term 'investment firm' means those firms that are required to hold initial capital of €730,000. The majority of such firms are those that deal as principal and are prudentially regulated by the Financial Conduct Authority; the largest, more complex investment firms are prudentially regulated by the Prudential Regulation Authority.

(3) Bank of England (2014), *The Bank of England's approach to resolution*; www.bankofengland.co.uk/financialstability/Documents/resolution/apr231014.pdf.

will meet their MREL simply by meeting their existing regulatory capital requirements.⁽¹⁾

- **Partial transfer** — where institutions are considered to be too large for a modified insolvency process but where there is a realistic prospect that critical parts of the business could be transferred to a purchaser, MREL will be set at a level which permits such a transfer to take place.
- **Bail-in** — the largest and most complex institutions will be required to maintain sufficient MREL resources to absorb losses and, in the event of their failure, be recapitalised so that they continue to meet the PRA's conditions for authorisation. Bail-in is designed to stabilise the institution, providing time to enable it to be restructured in order to address the underlying causes of its failure. The aim is that the institution, or its successor, is able to operate without public support.

1.8 MREL is necessary to make resolution plans credible. It ensures that institutions have a minimum amount of liabilities that can credibly bear losses before and in resolution. Not all types of liabilities are suitable for this purpose. Some are not in scope of all of the Bank's stabilisation powers or may be difficult to apply the powers to in practice. Others are connected to critical economic functions, or will not be reliably available at the point of resolution.

Outline of this document

1.9 The Bank received 21 responses to its consultation from UK and overseas institutions, trade associations and other organisations. This document provides feedback on the main issues raised in consultation responses, sets out where the Bank has made changes to its approach to setting MREL and clarifies the Bank's policy approach where relevant.

1.10 The rest of this document is structured as follows:

- (i) **Summary of policy** provides an overview of the Bank's approach to setting MREL and highlights changes since the consultation;
- (ii) **Context** highlights a number of external factors relevant to the setting of MREL which have changed since the Bank's consultation;
- (iii) **Feedback on consultation** discusses the main themes raised in consultation responses and provides additional information on the Bank's approach where relevant;
- (iv) **Next steps** describes the interaction institutions should expect to have with the Bank on MREL following this publication;
- (v) **Appendix** provides the Bank's Statement of Policy on its approach to setting MREL.

1.11 The PRA has published policy on the interaction between MREL and the PRA's existing regulatory capital framework.⁽²⁾ Readers are advised to read this document alongside the PRA's supervisory statement and policy statement.

(1) References to 'regulatory capital requirements' mean the amount of capital required to meet the (i) overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1 of the PRA Rulebook or IFPRU 2.2.1R of the FCA Rulebook (as applicable) and (ii) (if applicable) minimum leverage ratio in Leverage Ratio 3.1 of the PRA Rulebook. Unless otherwise specified, this refers to Pillar 1 requirements and Pillar 2A add-ons applicable to an institution, or any higher applicable leverage ratio or Basel I floor. Capital and leverage buffers are treated separately.

(2) Bank of England (2016), 'The minimum requirement for own funds and eligible liabilities — buffers and Threshold Conditions', *PRA Policy Statement PS31/16*; www.bankofengland.co.uk/pr/Pages/publications/ps/2016/ps3116.aspx.

2 Summary of policy

Calibration of MREL

2.1 The Bank consulted in December 2015 on its approach to calibrating institutions' minimum requirement for own funds and eligible liabilities (MREL). This reflected the then draft European Banking Authority (EBA) regulatory technical standards (RTS) on MREL (the 'MREL RTS'). The MREL RTS have now entered into force without substantive changes to the approach to the calibration of MREL.⁽¹⁾ Under this approach the Bank is required to calculate and set MREL as the sum of two components — a loss absorption amount and a recapitalisation amount. Both components are calibrated by reference to an institution's regulatory capital requirements.⁽²⁾

2.2 Following review of consultation responses, the Bank will retain the general approach to the calibration of MREL that was proposed in its consultation. Accordingly, while MREL will be set on a case-by-case basis, the Bank currently expects to require institutions that are subject to a bail-in or partial transfer preferred resolution strategy (bail-in/transfer institutions) to meet an end-state MREL based on two times their regulatory capital requirements (ie 2 x (Pillar 1 plus Pillar 2A) or 2 x any applicable leverage ratio requirement). Capital buffers must be met in addition to MREL (ie institutions may not double count the same Common Equity Tier 1 (CET1) resources to both MREL and capital buffers). As set out below, the timetable for meeting MREL will be extended to 2022. The Bank will review its current expectation of the calibration and transition of MREL by the end of 2020, before setting end-state MRELS.

2.3 As proposed in the consultation, the Bank will reduce the recapitalisation component of MREL for institutions with a partial transfer resolution strategy to reflect the proportion of the balance sheet that would be transferred under the resolution strategy. Institutions that are likely to be subject to a modified insolvency process will have no need for MREL resources (regulatory capital resources and eligible liabilities) to recapitalise them, and so will be set an MREL equal to their regulatory capital requirements.

Transitional arrangements

2.4 At the time of consultation, the then-draft MREL RTS permitted a transition period of 48 months (ie until 1 January 2020) during which MREL could be set at levels lower than the full requirements. In the final MREL RTS, the

48-month limit was replaced with a requirement that any transitional period should be 'as short as possible'.

2.5 In light of the removal of the 48-month transition deadline in the MREL RTS, and taking into account consultation responses, which supported a longer transitional period, the Bank has determined that the transitional period to meet end-state MRELS should be extended by two years to 1 January 2022. The Bank will set interim MRELS that differ for global systemically important banks (G-SIBs), domestic systemically important banks (D-SIBs)⁽³⁾ and other institutions that are subject to a bail-in or partial transfer resolution strategy. Capital buffers must be met in addition to MREL.

2.6 Accordingly:

- (a) **From 1 January 2019** G-SIBs with resolution entities⁽⁴⁾ incorporated in the United Kingdom will be required to meet the minimum requirements set out in the FSB total loss-absorbing capacity (TLAC) standard,⁽⁵⁾ being the higher of 16% of risk-weighted assets (RWAs) or 6% of leverage exposures.
- (b) **From 1 January 2020:**
 - a. G-SIBs and D-SIBs with resolution entities incorporated in the United Kingdom will be required to meet an MREL equivalent 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

(1) Regulation (EU) 2016/1450, available at <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:32016R1450&qid=1472865184527>.

(2) References to 'regulatory capital requirements' mean the amount of capital required to meet the overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1 of the PRA Rulebook or IFRU 2.2.1R of the FCA Rulebook (as applicable). Unless otherwise specified, this refers to Pillar 1 requirements and Pillar 2A add-ons applicable to an institution, or any higher applicable leverage ratio or Basel I floor. Capital buffers are treated separately.

(3) 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 (2013/36/EU), and which have a resolution entity in the United Kingdom.

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

(5) Available at www.financialstabilityboard.org/2015/11/total-loss-absorbing-capacity-tlac-principles-and-term-sheet/.

- ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6% if the leverage ratio requirement is 3%).⁽¹⁾
- b. Other bail-in/transfer institutions will be required to meet an MREL of 18% of their RWAs.
- (c) From 1 January 2022, but subject to review by the end of 2020:
- a. G-SIBs with resolution entities incorporated in the United Kingdom will be required to meet an MREL equivalent to the higher of:
 - i. two times the sum of Pillar 1 and Pillar 2A, ie $2 \times (\text{Pillar 1 plus Pillar 2A})$; 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).
 - b. D-SIBs and any other bail-in/transfer institutions will be required to meet an MREL equivalent to the higher of:
 - i. two times the sum of Pillar 1 and Pillar 2A, ie $2 \times (\text{Pillar 1 plus Pillar 2A})$; or
 - ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6% if the leverage ratio requirement is 3%).

2.7 The Bank will adjust MREL downwards for institutions with a partial transfer resolution strategy to reflect the proportion

of the balance sheet that would be transferred under the resolution strategy.

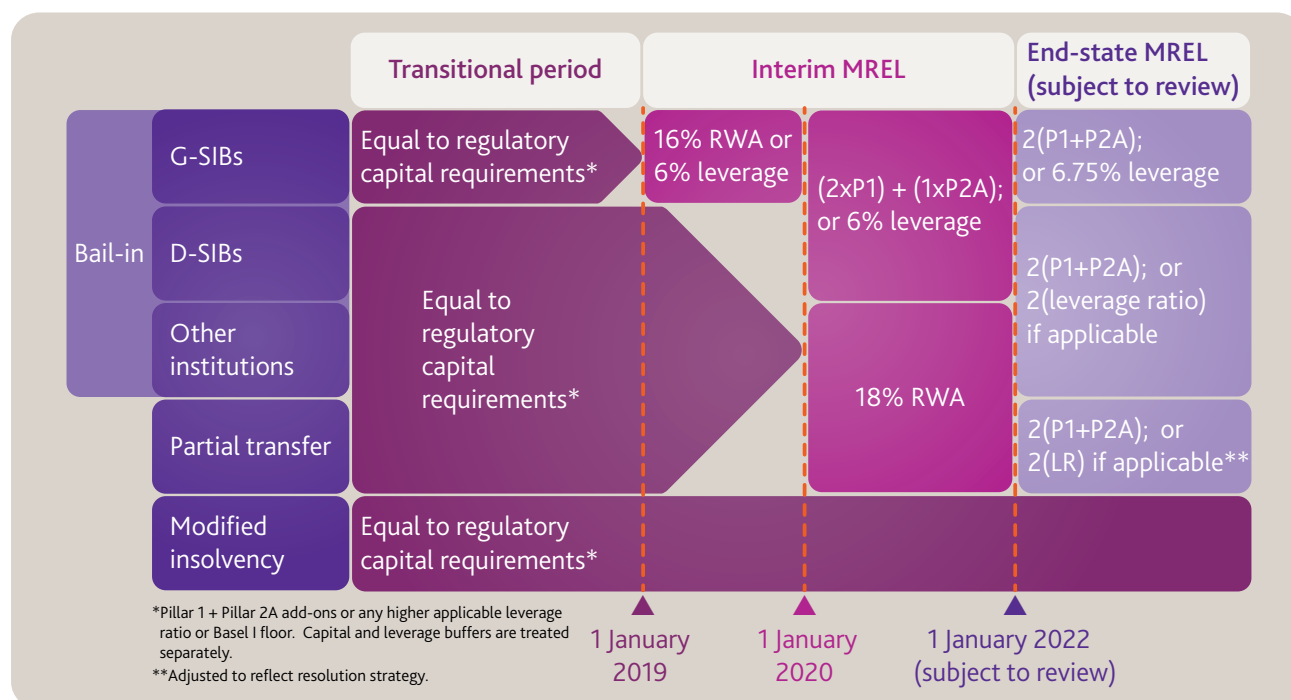
2.8 The Bank will decide whether to make any adjustments to Pillar 2A in the recapitalisation amount when it sets end-state MREs, following the review by the end of 2020. Any adjustments will be made on a case-by-case basis and will take into account any changes to regulatory capital requirements during the transition period. The Bank will not set MREL on a leverage basis for institutions not currently subject to a leverage ratio unless the leverage ratio framework is extended to these institutions.

Review of end-state MREL

2.9 The Bank will, before the end of 2020, review its general approach to the calibration of MREL, and the final transition date, prior to setting end-state MREs. 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 MREL resources to meet their interim MREs. The Bank will also take into account any changes to regulatory capital requirements, including the likely changes to the capital framework arising from the work of the Basel Committee on Banking Supervision (BCBS).

(1) The FPC is due to review the progress on international leverage ratio standards in 2017. 'The Financial Policy Committee's powers over the leverage ratio tools', *FPC Policy Statement*, July 2015; www.bankofengland.co.uk/financialstability/Documents/fpc/policystatement010715ltr.pdf.

Figure 1 Summary of MREL calibration and transition



Indicative thresholds for resolution strategies

2.10 As set out in the consultation, an institution's resolution strategy is an important factor in determining its MREL. UK institutions are likely to be resolved under one of three broad resolution strategies: modified insolvency; partial transfer; and bail-in. The Bank consulted on thresholds which would act as a guide to which resolution strategy was likely to be preferred. As the preferred resolution strategy for an institution is an institution-specific decision, the thresholds provide no more than an indicative guide to the Bank's likely judgement on strategy.

2.11 In establishing the boundary between a modified insolvency process and the use of resolution powers, the Bank consulted on an indicative threshold of 40,000 transactional accounts. In light of feedback from the consultation the Bank has decided to make two changes to this indicative transactional account threshold. First, to clarify the definition of 'transactional' accounts by reference to the frequency of their use (ie at least nine withdrawals over the previous three months). This definition allows the Bank to identify transactional accounts by considering how the accounts are actually being used in practice. Second, to express the indicative threshold as a range of between 40,000 to 80,000 transactional accounts (rather than as a threshold of 40,000 accounts). The Bank did not intend for the 40,000 threshold to be seen as a hard line between resolution strategies. The threshold is an indication of the Bank's likely judgement as to the appropriate institution-specific resolution strategy. The Bank has decided that this judgement is better expressed through a range of 40,000 to 80,000 transactional accounts.

2.12 The Bank consulted on an indicative threshold of £15 billion–£25 billion assets for the use of bail-in resolution strategies. The Bank has decided to leave this threshold unchanged.

MREL eligibility criteria

2.13 The Bank is maintaining the approach to MREL eligibility set out in the consultation, but is providing additional clarification on some issues in light of points raised by respondents.

2.14 The Bank is not changing the approach to subordination of MREL resources set out in the consultation. Structural subordination will be required for institutions subject to bail-in, with the exception of building societies, for which contractual subordination will be required instead. Institutions subject to a partial transfer resolution strategy will not require subordination where the strategy envisages transferring only their preferred deposits.⁽¹⁾

MREL in the context of groups and further issues

2.15 There are a number of issues related to MREL that are not set out in this Statement of Policy. These include reporting, disclosure and the treatment of institutions' holdings of MREL liabilities. The Bank will continue to develop its approach to these issues — as well as its approach to the calibration of MREL within groups (internal MREL) — taking into account international standards including the FSB's proposed guidance on internal TLAC due for consultation later this year. The Bank expects to provide further detail on a number of these issues in due course. As set out in the PRA's policy statement on operational continuity in resolution,⁽²⁾ the Bank will also consider as part of this whether loss-absorbing capacity should be allocated within groups to ensure operational continuity.

(1) The BRRD 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 from natural persons and small and medium-sized enterprises, were they not made through branches located outside the EU.

(2) Bank of England (2016), 'Ensuring operational continuity in resolution', *PRA Policy Statement PS21/16*; www.bankofengland.co.uk/pr/Pages/publications/ps/2016/ps2116.aspx.

3 Context

3.1 The Bank consulted on its approach to setting a minimum requirement for own funds and eligible liabilities (MREL) in December 2015. Since then there have been a number of developments relevant to the MREL framework.

MREL RTS

3.2 The Bank consulted in December 2015 on the basis of the then-draft European Banking Authority (EBA) regulatory technical standards (RTS) on MREL (the MREL RTS). In May 2016 the MREL RTS were adopted, with some modifications, by the European Commission, and in September 2016 entered into force following publication in the Official Journal.

3.3 The Bank must set MREL in accordance with UK law and with the MREL RTS, which further specify the Bank Recovery and Resolution Directive (BRRD) criteria for determining MREL using a institution-specific power of direction. In the consultation the Bank noted that it would review its approach to setting MREL to ensure it is compatible with the MREL RTS as finally adopted.

3.4 The changes made to the MREL RTS by the European Commission did not alter the approach for calibrating MREL based on a loss absorption and recapitalisation amount, with regulatory capital requirements used as a reference point for both. The Bank's view is that none of the changes made would require the Bank to alter the approach to calibrating MREL as set out in the consultation.

3.5 One of the changes made to the MREL RTS was to replace the specific 48-month transitional deadline with a requirement for a transitional period which is 'as short as possible'. In light of consultation responses, market developments and the change to the wording of the MREL RTS, the Bank is making changes to its approach to the MREL transition. These are set out in detail in Section 4 below and Section 7 of the final Statement of Policy.

European Commission TLAC proposal

3.6 The European Commission has proposed to legislate to implement the Financial Stability Board's (FSB's) total loss-absorbing capacity (TLAC) standard in EU law. As set out in the consultation the Bank is committed to implementing the TLAC standard, and will set MREL in such a way as to ensure that the TLAC standard is met by UK G-SIBs.

UK referendum on EU membership

3.7 On 23 June 2016 the United Kingdom held a referendum on its membership of the European Union in which a majority voted for the United Kingdom to leave the European Union.

3.8 The policy contained in this document has been designed in the context of the current UK and EU regulatory framework. The United Kingdom currently remains a full member of the European Union and all the rights and obligations of EU membership therefore remain in force.

3.9 The process of withdrawing from the European Union may introduce additional uncertainty into the market for UK institutions' MREL resources. The Bank has taken this into account in setting out its final approach.

3.10 As noted above, the Bank will, before the end of 2020, review the calibration of MREL and the final transition 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, including as a result of the referendum on 23 June 2016. The Bank will also take into account any changes to regulatory capital requirements, including the likely changes to the capital framework arising from the work of the Basel Committee on Banking Supervision (BCBS).

4 Feedback on consultation

Calibration and transition

Calibration

4.1 The consultation set out a proposed framework for the calibration of MREL. The framework was aligned with the MREL RTS and consists of adding together a 'loss absorption' amount and a 'recapitalisation' amount. The loss absorption amount is an amount equal to an institution's minimum capital requirements to absorb losses. The Bank expects to exclude capital buffers from the loss absorption amount. This is due to the PRA's policy on the interaction of MREL and capital buffers, which sets out that institutions cannot use simultaneously the same CET1 resources to meet both MREL and capital buffers. The effect of this policy is that capital buffers must be met in addition to MREL. The recapitalisation amount is the amount that the resolution authority considers necessary to recapitalise the institution back to a level necessary to enable it to continue to meet conditions for authorisation and command market confidence (if required by the resolution strategy).

4.2 Some respondents argued that the proposed calibration of MREL was too high and that institutions would find it difficult to meet an end-state MREL by 1 January 2020, and that Pillar 2A should not be included in the recapitalisation amount. Another respondent suggested that the regulatory capital requirements were not an appropriate proxy for measuring loss absorption and recapitalisation in resolution. In contrast, several respondents agreed to using Pillar 1 plus Pillar 2A as the loss absorption amount.

4.3 The Bank's view is that the approach to the calibration of MREL remains appropriate. The Bank considers that the regulatory capital requirements set by the competent authority provide a consistent guide to loss absorption and recapitalisation needs in keeping with the MREL RTS.

Transition to full implementation

4.4 The consultation set out the Bank's proposals on the transitional deadline for the setting of MREL. The consultation proposed that for most institutions, the Bank would set a final compliance date of 1 January 2020. This date was in line with the specific maximum 48-month transitional period provided by the then draft MREL RTS.

4.5 A general theme of the responses to the consultation proposals was that the Bank should extend the transitional period. Some respondents argued that the proposed 1 January 2020 deadline would place UK institutions at a disadvantage to their global peers by front-running the

1 January 2022 deadline for the final implementation of the minimum TLAC requirement, and suggested that the Bank should align its approach to transition with the two-stage transition in the TLAC standard.

4.6 As noted in Section 3, one of the changes made to the MREL RTS has been to replace the 48-month transition with a requirement for a transitional period that is 'as short as possible'.

4.7 In light of the removal of the 48-month transition deadline in the MREL RTS, and taking into account consultation responses, **the Bank has determined that the transitional period should be extended by two years to 1 January 2022, but subject to review by the end of 2020.**

4.8 To ensure that institutions make progress towards meeting their end-state requirements, the Bank will set interim MREs that must be met by 1 January 2020 (and for G-SIBs also 1 January 2019).

4.9 The Bank has determined that, while systemic importance is not an appropriate proxy for determining whether an institution is likely to be resolved using stabilisation powers,⁽¹⁾ systemic importance is a relevant factor for determining the appropriate transitional period for setting MREL. The rationale for this differentiation is: (a) that the disorderly failure of systemically important institutions is likely to have a greater impact on the economy and financial system, emphasising the importance of building resources for effective resolution; and (b) some smaller institutions have a more limited history of accessing debt capital markets, which may necessitate a more gradual approach to building MREL resources.

4.10 The Bank will differentiate its approach to transition and calibration based on the following two categories of institutions:

- (a) G-SIBs with resolution entities in the United Kingdom and D-SIBs;⁽²⁾ and
- (b) other bail-in/transfer institutions.

(1) Some institutions may not be designated as systemic before resolution occurs, but this does not mean that their failure would not have systemic effects on the financial system if resolution occurs. The failure of such institutions may also engage other resolution objectives such as the protection of depositors or continuity of banking services.

(2) 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 (2013/36/EU), and which have a resolution entity in the United Kingdom.

4.11 As noted above, the Bank will, before the end of 2020, review the final transition date prior to setting end-state MRELS. In doing so, the Bank will take into account institutions' experience in issuing MREL resources to meet their 2020 interim MRELS.

4.12 The Bank will decide whether to make adjustments to Pillar 2A in the recapitalisation amount when it sets end-state MRELS. Any adjustments will be made on a case-by-case basis and will take into account any changes to regulatory capital requirements during the transition period, including those arising from the PRA's approach to setting Pillar 2A. The Bank will not set MREL on a leverage basis for institutions not currently subject to a leverage ratio requirement unless the leverage framework is extended to these institutions.

Policy for G-SIBs and D-SIBs

4.13 The Bank will adopt the following staged approach to setting MREL for G-SIBs and D-SIBs with resolution entities in the United Kingdom during the transition period:

- (a) **From 1 January 2019** G-SIBs with resolution entities incorporated in the United Kingdom will be required to meet the minimum requirements set out in the FSB TLAC standard, being the higher of 16% of risk-weighted assets (RWAs) or 6% of leverage exposures.
- (b) **From 1 January 2020** G-SIBs and D-SIBs with resolution entities incorporated in the United Kingdom will be required to meet an interim MREL equivalent 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% if the leverage ratio requirement is 3%).
- (c) **From 1 January 2022**, and subject to review before the end of 2020, UK G-SIBs and D-SIBs with resolution entities incorporated in the United Kingdom will be required to meet a MREL equivalent to the higher of:
 - i. two times their regulatory capital requirements, ie 2 x (Pillar 1 plus Pillar 2A); or
 - ii. the higher of the two times the applicable leverage ratio requirement (ie 6% if the leverage ratio is 3% for D-SIBs) or 6.75% of leverage exposures for G-SIBs (in line with the TLAC standard).

4.14 The Bank considers that this provides appropriate flexibility to institutions to meet the end-state MRELS. The interim MRELS ensure that systemic institutions start to build

MREL resources, which is a critical component of ensuring orderly resolution in line with the Bank's statutory resolution objectives prior to meeting the end-state requirements.

Policy for other institutions with a bail-in resolution strategy

4.15 The Bank intends to set different interim MRELS for other institutions to be met from 1 January 2020. The Bank will adopt the following approach to setting MREL for other institutions for which the strategy is likely to be bail-in:

- (a) **From 1 January 2020**, other institutions with a bail-in resolution strategy will be required to meet an MREL of their 18% RWA.
- (b) **From 1 January 2022**, and subject to review before the end of 2020, other institutions for which the strategy is likely to be bail-in will be required to meet an MREL of two times their regulatory capital requirements, ie 2 x (Pillar 1 plus Pillar 2A).

4.16 The interim MREL is different for non-systemic institutions than the requirement of an interim MREL of (2 x Pillar 1) plus (1 x Pillar 2A) that will be applied to systemic institutions. The Bank considers that an 18% RWA provides an appropriate balance between additional flexibility for these institutions in managing the transition to end-state MRELS while ensuring that these institutions start to build a sufficient amount of MREL resources to facilitate orderly resolution.

Policy for institutions with a partial transfer resolution strategy

4.17 In the consultation, the Bank explained that it will adopt the same framework for the calibration of MREL for institutions with a bail-in preferred resolution strategy and institutions with a partial transfer preferred resolution strategy. For partial transfer institutions, the Bank set out that it would adjust the recapitalisation amount of MREL in accordance with the proportion of the balance sheet that the resolution plan for the institution envisages would be transferred. The Bank continues to believe that this approach is appropriate for institutions with a partial transfer strategy.

4.18 The Bank will adopt the same transitional arrangements for partial transfer institutions as for non-systemic bail-in institutions.

Adjustments to Pillar 2A in the recapitalisation amount

4.19 In the consultation, the Bank noted that it may adjust the recapitalisation amount to remove all or part of any components of Pillar 2A that would not apply to the institution following resolution.

4.20 Some respondents asked for further detail on how the Bank will make adjustments to Pillar 2A in the recapitalisation amount. Under the BRRD, the Bank must take into account information received from the PRA, as the competent authority, relating to the institution's business model, funding model and risk profile. Any adjustments will be made on a case-by-case basis. The Bank may only adjust the recapitalisation amount if, having consulted the PRA, the Bank judges it to be feasible and credible that there would be changes to the capital requirement (including any applicable leverage ratio requirement) that might apply immediately as a result of resolution.

4.21 The Bank will decide whether to make adjustments to Pillar 2A in the recapitalisation amount when it sets end-state MRELS at a later date. The calibration of the interim MRELS that must be met by 1 January 2020 (and for G-SIBs also 1 January 2019) will not include the Pillar 2A element in the recapitalisation amount.

MREL over the transitional period

4.22 The Bank will set MRELS on an annual basis. The Bank will require institutions to submit a plan showing how they intend to phase their market issuance to reach their interim MRELS. The Bank will engage with institutions to consider whether the transitional arrangements for the interim or end-state MRELS remain appropriate.

4.23 In the period prior to the interim requirement coming into force, the Bank's general approach will be to set MREL equal to an institution's regulatory capital requirements.

4.24 This general approach does not preclude the Bank from setting an earlier target or higher MRELS for particular institutions in the transitional phase, on a case-by-case basis. The Bank may consider doing so, for example, where action is needed to enhance an institution's resolvability and increasing its MREL resources is needed to advance the Bank's objectives as resolution authority.

4.25 Some respondents asked the Bank to clarify when the Bank might set an earlier target or higher MREL during the transitional phase. Any decision would be on a case-by-case basis. The Bank's decision would be guided by the need to strike an appropriate balance between requiring an institution to build up its MREL resources to enhance resolvability and the challenges that may be associated with this process.

How will the Bank set MREL for institutions when their requirements change?

4.26 Some respondents asked the Bank to clarify the transitional period over which MREL would have to be built for institutions that move to a different preferred resolution strategy, or when their MREL otherwise changes materially. An institution may move strategy from a modified insolvency

strategy to a resolution requiring the use of bail-in or partial transfer powers. Alternatively an institution may move from a partial transfer strategy to a bail-in strategy. Each of these changes are likely to lead to an increase in MREL.

4.27 The Bank will, through ongoing engagement with institutions, consider which institutions are close to the indicative resolution strategy thresholds in order to ensure that they are given sufficient time to build up MREL resources to meet increased requirements caused by a change of resolution strategy. This should reduce the risk that institutions move between thresholds unexpectedly. When institutions do move between thresholds the Bank will revise the MREL that applies to the institution in question.

4.28 The Bank will set MREL on an annual basis following a review of the institution's resolution plan. The Bank will require institutions to submit a forward-looking plan of how they will meet the interim or end-state MREL.

4.29 The TLAC standard sets out that newly designated G-SIBs must meet the minimum TLAC requirements within 36 months of their date of designation. Accordingly, the Bank will require UK institutions that are newly designated as G-SIBs to meet any higher MREL within a 36-month period. For other institutions that move between resolution strategies, or for other reasons face material changes to their MREL, the Bank is required by the MREL RTS to set a transition period for an institution to meet MREL that is 'as short as possible'. The Bank expects to allow at least 36 months for transition in the case of material changes in MRELS, and will make a decision on the appropriate period on a case-by-case basis.

Thresholds/strategies

4.30 The consultation set out the indicative thresholds that the Bank proposed to use as part of its determination of whether an institution should be resolved using a bail-in strategy, a partial transfer strategy, or a modified insolvency process. The choice of resolution strategy will determine whether MREL must be met in relation to the whole balance sheet (bail-in), the part of the balance sheet that will be transferred (partial transfer), or if no MREL is required in excess of regulatory capital requirements (modified insolvency process).

4.31 The PRA has published requirements on operational continuity in resolution (OCIR).⁽¹⁾ As noted in the OCIR policy statement, the PRA is able to waive OCIR rules under certain circumstances and would expect to do so for institutions with a modified insolvency process resolution strategy. Therefore

(1) Bank of England (2016), 'Ensuring operational continuity in resolution', *PRA Policy Statement PS21/16*; www.bankofengland.co.uk/pr/Pages/publications/ps/2016/ps2116.aspx.

institutions that are expected to enter modified insolvency upon failure would generally not be required to comply with OCIR, and will generally not be set an MREL in excess of their regulatory capital requirements.

4.32 The PRA has also published rules on continuity of access (CoA) to FSCS-covered deposits.⁽¹⁾ These rules require institutions to put in place systems to ensure eligible depositors have continued access to FSCS-covered deposits in resolution or insolvency by facilitating a transfer of such deposits. When the PRA's Policy Statement (SS18/15) was published in 2015, the PRA listed a number of factors that would be used to consider individual institution waiver applications in respect of the CoA rules. Reflecting the evolution of the Bank's approach to resolution strategies since the introduction of CoA rules, the PRA announced in October 2016 that a waiver by consent for the CoA rules would be available to a broader set of institutions.⁽²⁾ The Bank will work with the PRA to ensure a co-ordinated approach to these issues.

Bail-in threshold

4.33 The consultation proposed a balance sheet size of between £15 billion–£25 billion as an indicative threshold for use of a bail-in resolution strategy.

4.34 The Bank must consider the feasibility of, and the risks in executing, a resolution strategy when determining which resolution strategy should be preferred. A partial transfer resolution encompasses finding a buyer and undertaking a complex process of splitting up, in a short period of time, an institution that may be highly interconnected. These institutions might be systemically important and might provide critical and non-critical economic functions (from the same legal entities) to the wider economy. Accordingly, where an institution's size or complexity means that the prospects of finding a willing purchaser for significant parts of the business are low, and the technical complexities of carrying out a partial transfer resolution are high, the Bank would expect to select a bail-in resolution strategy.

4.35 Some respondents argued that the Bank should use a higher threshold from an existing regulatory initiative. Responses cited thresholds for ring-fencing (£25 billion core deposits), leverage ratio (£50 billion total assets), and the systemic risk buffer (£175 billion total assets) as possible alternatives.

4.36 The Bank's view is that the proposed bail-in threshold may be distinguished from other thresholds used for different parts of the regulatory framework. The threshold is designed to inform a test against the statutory resolution objectives and to reflect the feasibility of a particular resolution strategy. While some respondents argued that different thresholds for existing regulatory initiatives could be used, the resolution

objectives do not relate solely to an institution's systemic importance. The broader remit of resolution objectives is one reason why we expect the threshold for bail-in to be different from other regulatory thresholds — including where systemic risk buffers are set.⁽³⁾

4.37 One respondent suggested that an institution should meet both the balance sheet definition (ie between £15 billion–£25 billion) and the transactional accounts definition to have a bail-in strategy. The respondent argued that an institution with a balance sheet between £15 billion–£25 billion but fewer than 40,000 transactional accounts (based on the consultation definition) should have a resolution strategy of modified insolvency. As noted above preferred resolution strategies must be determined on an institution-specific basis, and the thresholds only provide an indication of the appropriate strategy. In deciding on an institution's resolution strategy, the Bank will take into account its statutory resolution objectives and the critical economic functions provided by the institution.

4.38 Taking consultation responses into account, the Bank has not changed its view on the appropriate indicative threshold for bail-in. **The Bank has retained the indicative threshold of £15 billion–£25 billion of total assets.**

Partial transfer threshold

4.39 Failing institutions can only be resolved using bail-in or transfer powers if this is deemed necessary by the Bank as resolution authority, having regard to the public interest in advancing one or more of the resolution objectives, and where a modified insolvency process would not achieve the objectives to the same extent.

4.40 The consultation proposed an indicative threshold of 40,000 transactional accounts as a point at which the Bank would generally expect to use partial transfer powers, rather than a modified insolvency process, to resolve an institution. Where the critical economic functions provided by an institution could credibly be transferred to a purchaser, taking into account the factors set out in paragraph 4.6 of the Statement of Policy (in the Appendix), the Bank would expect to set partial transfer as the preferred resolution strategy. The consultation also set out that the Bank was considering whether also to make use of an indicative value threshold exceeding £350 million of sight deposits.

(1) The rules are contained primarily in Chapter 13.4–13.8 in the Depositor Protection Part of the PRA Rulebook.

(2) www.bankofengland.co.uk/pr/Pages/authorisations/waivers/waiversbyconsent.aspx.

(3) The Banking Act 2009 sets out the objectives to which the Bank must have regard when resolving an institution. These are to: (i) ensure the continuity of banking services in the United Kingdom and of critical functions; (ii) protect and enhance the financial stability of the United Kingdom; (iii) protect and enhance public confidence in the stability of the financial system of the United Kingdom; (iv) protect public funds, including by minimising reliance on extraordinary public financial support; (v) protect depositors and investors covered by relevant compensation schemes; (vi) protect, where relevant, client assets; and (vii) avoid interfering in property rights, in contravention of the European Convention on Human Rights.

4.41 The general theme of responses on the indicative threshold for partial transfer was that the Bank should define transactional accounts narrowly, including by reference to regularity of usage, and increase the quantum of the transactional account threshold.

Definition of transactional accounts

4.42 The consultation did not set out a specific preferred definition of 'critical transactional banking services' (transactional accounts). Instead, the Bank invited comments on how transactional accounts should be defined.

4.43 One challenge is that institutions provide accounts which are labelled as 'savings accounts' but which have the functionality of, and may be used as, current accounts. Conversely, some depositors may have 'current accounts' whose main purpose is, in practice, to store value and not to make day-to-day payments.

4.44 During the consultation period, the Bank asked a number of institutions to provide data on the number and value of deposit accounts they provide. These covered both functionality (eg access to payment systems) and depositors' behaviour (eg a certain number of withdrawals in a given time period). These data have allowed the Bank to identify transactional accounts by considering how the accounts are actually being used in practice.

4.45 Some respondents argued that an alternative definition of transactional accounts should be used. One respondent suggested that it would be appropriate to align the threshold with the definition of 'retail transactional accounts' under the Liquidity Coverage Requirement (LCR) in the Capital Requirements Regulation.⁽¹⁾

4.46 Under the LCR rules, 'stable retail deposits' constitute covered deposits that are held in 'transactional accounts' and deposits which are part of an 'established relationship making withdrawal highly unlikely'. Transactional accounts are defined in a European Commission delegated regulation as accounts 'where salaries, income or transactions are regularly credited and debited respectively against that account'.⁽²⁾

4.47 The Bank considers that a similar definition, with further guidance on the actual usage of accounts, would be the most appropriate for identifying deposits that are actually used for transactional purposes.

4.48 The Bank will define transactional accounts by reference to usage. The Bank considers that at least nine withdrawals over the last three months represents an appropriate benchmark to define the necessary usage for an account to be considered a transactional account.

Levels/numbers of transactional accounts

4.49 The consultation proposed an indicative threshold of 40,000 transactional accounts as the point at which the Bank would generally expect to use stabilisation powers, rather than modified insolvency, to resolve an institution.

4.50 Some respondents felt that disclosing any form of indicative threshold could act as a 'cliff-edge' to institutions' growth plans and thereby discourage growth and competition. Several respondents suggested that the Bank could use a higher level for the transactional account threshold. One respondent proposed that a threshold of 0.25% of the current account market could be used, which would result in a threshold of 187,500 accounts.

4.51 The rationale for proposing an indicative threshold of 40,000 transactional accounts was informed by a consideration of the Bank's statutory resolution objectives. For non-systemic firms that are below the bail-in threshold, the most relevant objectives relate to: (i) the protection of depositors and investors covered by relevant compensation schemes; and (ii) the need to ensure the continuity of banking services in the United Kingdom and of critical economic functions. It is important to note that these two examples are not exhaustive. Other resolution objectives may be engaged.

4.52 In the consultation, the Bank used 40,000 transactional accounts as an indicative threshold but gave a relatively broad definition of transactional accounts that could include current accounts that are rarely used in practice for transactional purposes.

4.53 The Bank has considered the arguments raised by respondents to increase the 40,000 threshold of transactional accounts. As explained above, the Bank considers that the change in the definition of a transactional account more accurately identifies those accounts which are being actually used for transactional purposes. As a result, it narrows the number of the accounts that would count towards the threshold and so has a similar effect to raising the threshold.

4.54 It should be noted that the Bank did not intend for the 40,000 level to be seen as a hard line between resolution strategies. The threshold is an indication of the Bank's likely judgement as to the appropriate resolution strategy, and a judgement must still be made on an institution-specific basis taking into account all the resolution objectives and the feasibility of a given resolution strategy.

4.55 To better express this, the Bank has changed the threshold to a range of 40,000 to 80,000 transactional accounts.

(1) Capital Requirements Regulation (575/2013) (CRR).

(2) Article 24 of Commission Delegated Regulation 2015/61.

4.56 In its consultation the Bank also posed the possibility of making use of an indicative value threshold exceeding £350 million of sight deposits. The Bank has decided not to use a value definition to inform the transactional account threshold. The Bank considers that the two changes to the threshold (the definition and use of a range of transactional accounts) mean that the threshold provides an appropriate proxy for an institution's likely resolution strategy. The Bank will nevertheless have regard to the value of sight deposits to determine when the use of stabilisation powers is justified.

4.57 In conclusion, the Bank has **increased the threshold of transactional accounts to a range of 40,000 to 80,000 transactional accounts**. This threshold is an indication of the Bank's likely judgement as to the appropriate resolution strategy. The Bank will make a judgement for institutions in this range on an institution-specific basis. The Bank will take into account all of the resolution objectives and the feasibility of a given resolution strategy. The Bank has decided that this judgement is better expressed through a range of 40,000 to 80,000 transactional accounts.

Eligibility

4.58 Respondents generally accepted the Bank's position on subordination. Several respondents argued that the eligibility criteria for MREL liabilities should be broadened. Some argued that structured notes should be eligible for MREL, or that the Bank should provide more clarity on what sort of derivative features would require exclusion.

4.59 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. This objective is central to the eligibility criteria the Bank has decided to set.

4.60 The Bank is maintaining its approach to subordination. Accordingly structural subordination, involving the issuance of MREL by a holding company, will be required for institutions subject to bail-in. 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 subordinated liabilities to satisfy their MRELS. Institutions subject to partial transfer will not be required to achieve subordination where the strategy envisages transferring preferred deposits only.

4.61 For institutions subject to structural subordination, MREL resources issued externally by the relevant holding company should not rank *pari passu* with significant amounts of other liabilities that do not qualify as MREL. Ideally such holding companies should have 'clean' balance sheets with no

operating liabilities, although in practice some liabilities that are not eligible as MREL may be unavoidable (eg tax liabilities). In line with the FSB's TLAC standard, the threshold for liabilities that do not qualify as MREL (excluding liabilities that previously met the MREL eligibility criteria but no longer meet the minimum maturity requirement) will be set at 5% of the holding company's overall external MREL resources.

4.62 Eligible liabilities must be subject to the governing law of the jurisdiction in which the issuing entity is incorporated, or include legally enforceable contractual write-down provisions.

4.63 In line with the FSB's TLAC standard, externally issued regulatory capital in operating entities can count towards meeting the holding company's MREL, to the extent that such capital would count towards the group's consolidated capital requirements, until the current end-state MREL date of 1 January 2022. After that point, only externally issued CET1 issued by subsidiaries would count towards meeting a group's external MREL.

4.64 Eligible liabilities must have a residual effective maturity of at least one year. The Bank expects institutions to monitor the overall maturity profile of their resources. Institutions will need to observe the following criteria for maturity of MREL-eligible liabilities:

- (a) If a liability confers a right to early reimbursement upon its owner, the maturity date of the liability shall, for the purposes of determining eligibility for MREL, be considered to be the first date at which such a right arises.
- (b) An eligible liability cannot be called, redeemed early, repayed, or repurchased by the institution without the Bank's approval, if this would cause the institution to breach its MREL or if the institution is already in breach of its MREL.⁽¹⁾
- (c) The Bank expects institutions not to structure their MREL resources in such a way as to reduce effective maturity, for example with liabilities which create incentives for the issuer to redeem them ahead of the contractual maturity date (such as liabilities with interest rate step ups coinciding with issuer calls). Where liabilities do contain such incentives, the date at which the incentive arises shall be considered the maturity date for the purposes of MREL eligibility.

4.65 The practicality of the bail-in tool rests on liabilities being straightforward to value rapidly in resolution. In line with the FSB's TLAC standard, liabilities whose value depends on derivatives — such as structured notes — or those which

(1) This is in line with section 12 of the FSB TLAC standard.

are subject to contractual set-off or netting would not qualify as MREL resources.

4.66 In response to questions from respondents about what derivative features would mean a liability was not eligible to meet MREL, the Bank has clarified in the Statement of Policy that instruments which include only put or call options would not be ineligible solely on that basis.

4.67 A number of respondents also asked whether liabilities which had previously been eligible as regulatory capital but which were no longer (or only partially) recognised as capital could count to meeting MREL. The Bank notes that if a liability meets the MREL-eligibility criteria it can be counted in full towards MREL, notwithstanding that it is not eligible as regulatory capital (subject to 4.63 above). Institutions would still need to ensure that all the MREL eligibility criteria are met in any instance.

4.68 The responsibility for ensuring that liabilities are eligible rests with institutions. Institutions will be required to obtain independent legal advice on a liability's eligibility, and provide this to the Bank if required. The Bank may use its powers of direction to further specify MREL eligibility criteria for individual institutions.

4.69 In line with the continuous resolvability assessment process, institutions will be expected to demonstrate compliance with the eligibility criteria on request.

4.70 The Bank will continue to monitor MREL issuance and may choose to issue further generic guidance on liability eligibility, should the Bank consider this necessary.

MREL in the context of groups and further issues

Internal MREL

4.71 In the consultation, the Bank set out its initial views and some guiding principles on how to set MREL within groups.

4.72 A general theme of the responses to the consultation was to request more detail on the scope of application of MREL within groups. The Bank is not setting out its final policy on intragroup MREL in this document, although the principles set out in the consultation will continue to guide the Bank's thinking. The Bank has retained the text on MREL within groups in the final Statement of Policy on this basis.

4.73 The Bank notes that the FSB cross-border crisis management (CBCM) workstream on internal TLAC aims to publish principles for consultation on how to set internal TLAC for G-SIBs by the end of 2016. Several respondents argued that the Bank should take the FSB's work into account. The Bank agrees and has been involved in the development of the FSB principles. The Bank will take account of any FSB work on internal TLAC in determining its final approach for setting MREL within groups.

4.74 The Bank expects to provide further detail on the scope of application of MREL within groups in due course, taking account of international standards. In so doing the Bank may revise the groups section of its MREL Statement of Policy.

Further issues

4.75 In addition to the issues described above, the December 2015 consultation set out the Bank's initial thinking on a number of other issues essential to the MREL framework in the long term, specifically: disclosure; reporting; treatment of MREL holdings; and large exposures.⁽¹⁾

4.76 The Bank has not included material on these issues in its Statement of Policy, but wanted to provide an early insight into its thinking. The Bank expects to revisit these issues, including in light of international standards, and may update its Statement of Policy in due course.

(1) Bank of England (2015), *The Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL): Consultation on a proposed Statement of Policy*, Section 7; www.bankofengland.co.uk/financialstability/Documents/resolution/mrelconsultation2015.pdf.

5 Next steps

Interaction with institutions

5.1 The Bank intends, by the end of 2016, to communicate to institutions the following:

- (a) the 2016/17 MREL for 2016 and for 2017 each bank, building society and '730K' investment firm,⁽¹⁾ which will be set at a level equal to the institution's regulatory capital requirements; and
- (b) an indication of the consolidated interim MREL which the Bank expects to apply to any resolution entity/entities within a group from 1 January 2020 (and for G-SIBs 1 January 2019) on the basis of the Bank's Statement of Policy.

5.2 The Bank will require institutions to submit a plan of how their market issuance will be phased in order for them to reach the interim MREL. This initial forward-looking plan should cover the period up to the relevant interim MREL for the institution.

5.3 As set out above MREL must be set on an annual basis. The Bank will engage with institutions at this time, as well as on an ongoing basis, to consider whether the transitional arrangements for meeting the interim or end-state MRELS remains appropriate.

Legislative obligations

5.4 The Bank has given careful consideration to all responses received and intends to continue to engage with institutions as it performs its statutory functions in relation to resolution.

5.5 This document meets the legislative requirement to prepare a Statement of Policy with regard to section 3B(9) of the Banking Act 2009. The Bank will be entitled to use its powers of direction from the date of publication of this Statement of Policy.

5.6 The Bank will keep the Statement of Policy under review and update it where necessary to reflect any changes in the Bank's approach.

(1) As required pursuant to Part 9 of the Bank Recovery and Resolution (No. 2) Order 2014.

Appendix 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

1.1 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⁽¹⁾ authorised for the purpose of the Financial Services and Markets Act 2000 (FSMA) by the Prudential Regulation Authority (PRA) or Financial Conduct Authority (FCA);⁽²⁾
- (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⁽³⁾ 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 banks, building societies and 730,000 investment firms (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(4) of the Banking Act to set MREL, in consultation with the PRA or FCA.

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 European Commission Delegated Regulation (EU) 2016/1450 (the MREL RTS). The Bank will also consider the Financial Stability Board's total loss-absorbing capacity (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 RTS:

- (a) the need to ensure that the institution can be resolved by the application of the stabilisation powers including, where appropriate, the bail-in tool, in a way that meets the resolution objectives;
- (b) the need to ensure, in appropriate cases, that the institution has sufficient eligible liabilities to ensure that, if the bail-in tool were to be applied, losses could be absorbed and the common equity Tier 1 (CET1) 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 Directive 2013/36/EU or Directive 2014/65/EU 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 Article 44(3) 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 CET1 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 Directive 2013/36/EU or Directive 2014/65/EU;
- (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; and
- (f) the extent to which the failure of the institution would have adverse effects on financial stability, including, due to

(1) For the purposes of this Statement of Policy the term 'institution' means UK-incorporated banks, UK-incorporated building societies and 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'.

(2) The PRA and FCA are the UK competent authorities. According to article 2 of the Bank Recovery and Resolution Directive 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.

(3) The term 'financial institution' has the meaning given by article 4 (1) (26) of Regulation 575/2013/EU.

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.

2 Statutory framework

2.1 The PRA has published a concurrent 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 PRA Threshold Conditions.

2.2 Please consult the PRA's supervisory statement for further details.

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 MREL resources, Section 6 sets out the Bank's principles for setting MRELS within groups and Section 7 sets out the Bank's approach to the transition to final (end-state) MRELS, including interim requirements.

3.2 The No. 2 Order and the MREL RTS provide the framework for the calibration of MREL. The Bank will set MREL in accordance with this framework. The MREL RTS uses the pre-existing CRD IV⁽²⁾ capital requirements (Pillar 1, Pillar 2A and capital buffer requirements), any applicable leverage ratio, and the Basel I floor, as reference points.

3.3 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

3.4 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 RTS is that the loss absorption amount will equal an institution's 'regulatory capital requirements'⁽³⁾ (Pillar 1 plus Pillar 2A or, if higher, the institution's applicable leverage ratio or the Basel I floor) plus its capital buffers (the combined buffer or, where binding, the PRA buffer).⁽⁴⁾

3.5 The MREL RTS 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.

3.6 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.⁽⁵⁾

4 Resolution strategies and MREL

4.1 MREL will be set to ensure that institutions can be resolved in line with the resolution objectives. 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 the MREL that is set for an institution or another relevant person.

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

(1) Capital Requirements Directive (2013/36/EU) (CRD) and Capital Requirements Regulation (575/2013) (CRR) —, jointly 'CRD IV'.

(2) Bank of England (2016), 'The minimum requirement for own funds and eligible liabilities (MREL) — buffers and Threshold Conditions', *PRA Supervisory Statement SS16/16*, available at www.bankofengland.co.uk/pr/Pages/publications/ss/2016/ss1616.aspx.

(3) References to 'regulatory capital requirements' mean the amount of capital required to meet the (i) overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1 of the PRA Rulebook or IFPRU 2.2.1R of the FCA Rulebook (as applicable) and (ii) (if applicable) minimum leverage ratio in Leverage Ratio 3.1 of the PRA Rulebook. Unless otherwise specified, this refers to Pillar 1 requirements and Pillar 2A add-ons applicable to an institution, or any higher applicable leverage ratio or Basel I floor. Capital and leverage buffers are treated separately.

(4) Please see the PRA Policy Statement on Pillar 2 for further details: www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps1715.aspx.

(5) As set out in the MREL RTS, the loss absorption amount may be adjusted in certain circumstances.

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 financial institutions (the bank insolvency procedure (BIP), building society insolvency procedure (BSIP) and the special administration regime (SAR)).⁽¹⁾ Where an institution can enter one of these modified insolvency processes at the point of failure, without adversely affecting the achievement of the resolution objectives, the Bank expects to set the recapitalisation component of MREL to zero. This would mean that an institution's 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 or the Basel I floor).

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; and
- (b) if the institution does not provide significant amounts of transactional banking services or other critical economic 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 economic 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 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 economic 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 of or all of the institution's business, assets and liabilities (particularly those associated with critical economic functions) are reasonably likely to be attractive to a private sector purchaser; and
- (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 balance sheet size 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 MREL will be set taking this into account. The Bank expects to consider the following principal adjustments to 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 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⁽²⁾ represented only a proportion of its total liabilities, the recapitalisation component of 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 transfer resolution strategy assumes that only liabilities benefitting from preference in insolvency⁽³⁾ 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

(1) The special administration regime is set out in the Investment Bank Special Administration Regulations 2011 issued by HM Treasury pursuant to s233 of the Banking Act 2009.

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

(3) The BRRD 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 from natural persons and small and medium-sized enterprises, were they not made through branches located outside the EU.

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 is bail-in. The Bank is likely to make use of a bail-in strategy for institutions with balance sheets above £25 billion, 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 institutions 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. Subordination of MREL resources reduces the risk of breaches of the NCWO safeguard in the event of a bail-in.

4.10 The Bank currently expects to direct institutions to comply with an end-state MREL from 1 January 2022, but subject to review by the end of 2020:

- a. G-SIBs⁽¹⁾ with a resolution entity incorporated in the United Kingdom will be required to meet an MREL equivalent to the higher of:
 - i. two times the sum of Pillar 1 and Pillar 2A, ie $2 \times (\text{Pillar 1 plus Pillar 2A})$; 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).⁽²⁾
- b. D-SIBs⁽³⁾ and any other bail-in institutions will be required to meet an MREL equivalent to the higher of:
 - i. two times the sum of Pillar 1 and Pillar 2A, ie $2 \times (\text{Pillar 1 plus Pillar 2A})$ or
 - ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6% if the leverage ratio is 3%).

5 MREL liability eligibility (external MREL)

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 and/or own funds must meet in order to qualify as MREL resources.⁽⁴⁾ 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 relevant persons to consider the overall maturity profile of their externally issued MREL resources, and to ensure that temporary difficulties in accessing debt issuance markets would not be likely to cause a breach of their MREL. The average maturity of relevant persons' MREL resources may decrease in periods of market stress, and the Bank does not intend to apply a minimum maturity requirement beyond that applicable under the No. 2 Order. The Bank may use its powers of direction to further specify MREL eligibility criteria for individual relevant persons.

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 eligibility for MREL, be considered to be the first date at which such a right arises. The Bank expects relevant persons not to structure their MREL resources 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 eligibility for MREL, be considered to be the date at which the incentive arises.

5.5 A relevant person should not call or redeem an MREL-eligible liability if that would cause it to breach its MREL, or if the relevant person is already in breach of its MREL, unless the Bank approves such a transaction.

5.6 Externally issued regulatory capital in subsidiaries of a resolution entity can count towards meeting that resolution entity's MREL, to the extent that such capital would count towards the group's consolidated capital requirements, until the current end-state MREL date of 1 January 2022. After that point, only externally issued CET1 issued by such subsidiaries would count towards meeting a group's external MREL. Subject to this, liabilities which had previously been eligible as regulatory capital but which were no longer (or only partially) recognised as capital could count to meeting MREL.

(1) The Bank does not expect that setting a level below the internationally agreed minimum for G-SIBs would be sufficient to ensure market confidence.
 (2) Those entities 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.
 (3) 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 (2013/36/EU), and which have a resolution entity in the United Kingdom.
 (4) See in particular Section 123(4).

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

5.8 Liabilities subject to contractual set-off or netting arrangements are not appropriate MREL resources.

5.9 Where a liability is governed by non-EEA law, the Bank will need to be satisfied 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 Handbook and FCA Handbook.⁽¹⁾

5.10 The responsibility for ensuring that instruments are eligible rests with relevant persons. Relevant persons should obtain independent legal advice on a liability's eligibility, and provide this to the Bank where required.

5.11 In line with the continuous resolvability assessment process, relevant persons will also be expected to demonstrate compliance with the eligibility criteria on request.

6 MREL in the context of groups

6.1 This section sets out the framework the Bank will use to determine the intragroup distribution of MREL.

6.2 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 entities⁽²⁾ that are important from a resolution perspective (for example holding companies) on an entity-specific basis.

6.3 The Bank will apply the following principles when setting MREL within groups:

- (a) internal MREL resources must be subordinated to the operating liabilities of the group entities issuing them;
- (b) internal MREL resources must be capable of being written down or converted to equity without or ahead of any use of stabilisation powers in relation to the operating entity which issues them; and
- (c) internal MREL resources must be appropriately distributed within groups.

6.4 The Bank will require institutions subject to a bail-in strategy to structure their liabilities to achieve structural subordination of external MREL resources issued by resolution entities. 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 subordinated liabilities to satisfy their MRELS.

6.5 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. 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.

6.6 Resolution entities will be required to issue external MREL resources at least equal to all the internal MREL qualifying liabilities to be issued to them from their subsidiaries. The proceeds of this external MREL issuance will be invested in the MREL resources of those operating entities within the scope of the individual requirements.

6.7 Internal MREL will be calculated on an individual basis in accordance with the MREL RTS framework (see Section 3). In setting MREL, the Bank will consider the interaction between the consolidated external MREL and the internal MREL. The Bank may adjust the internal MREL set for an individual entity having regard to the consolidated MREL set for the group and to ensure that internal MREL resources are pre-positioned in the appropriate entities. The Bank may adjust downwards the MREL for individual entities within a group relative to the MREL which would be set for an equivalent standalone entity. The Bank does not expect to adjust downwards the internal MREL applicable to ring-fenced bodies (RFBs).

6.8 The write down and/or conversion to equity of internal MREL resources should not lead to unintended changes in the group's internal ownership structure. The Bank will consider subsidiaries' non-equity MREL resources in relation to such potential effects on group structures in resolution.

6.9 Intragroup distribution of internal MREL resources must ensure that sufficient loss-absorbing capacity is pre-positioned at the individual entities within the scope of MREL. The intragroup distribution must ensure that losses can be absorbed and passed up to the resolution entity or entities.

(1) See www.prarulebook.co.uk/rulebook/Content/Part/211722/26-10-2016 and www.handbook.fca.org.uk/handbook/IFPRU/11/6.html?date=2016-06-30.

(2) Specifically, relevant persons referred to in Section 1.2(b) and (c) above.

7 Transitional arrangements

General transitional arrangements

7.1 The MREL RTS allows the Bank to determine an appropriate transitional period for a relevant person to reach its end-state MREL. The transition period must be as short as possible.

7.2 To allow relevant persons flexibility over timing of changes to their liability structures in order to meet MREL, generally the Bank does not expect to direct institutions to hold MREL greater than institutions' regulatory capital requirements prior to the dates set out at 7.4 below. The Bank nevertheless proposes to provide 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 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.

7.3 The Bank currently expects to direct institutions to comply with an end-state MREL (calculated in accordance with the methodology described in Section 3 and 4 above) from 1 January 2022.

7.4 Notwithstanding 7.3 above, to ensure that institutions make progress towards meeting their end-state requirements the Bank expects to direct relevant institutions to meet the following interim MRELS:

- (a) From 1 January 2019 G-SIBs with resolution entities incorporated in the United Kingdom will be required to meet the minimum requirements set out in the Financial Stability Board (FSB) total loss-absorbing capacity (TLAC) standard, being the higher of 16% of risk-weighted assets (RWAs) or 6% of leverage exposures;⁽¹⁾
- (b) From 1 January 2020:
 - a. G-SIBs with resolution entities incorporated in the United Kingdom and 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% if the leverage ratio requirement is 3%);

- b. institutions for which the preferred resolution strategy is use of stabilisation powers, but which are not G-SIBs or D-SIBs, will be required to maintain MREL equal to 18% of risk-weighted assets.

7.5 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.

7.6 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 come into force from the point at which an interim MREL applies to an institution. Please consult the PRA's supervisory statement for further details.

Institution-specific transitional arrangements

7.7 The Bank may on an institution-specific basis set an earlier compliance date and/or MRELS greater than regulatory capital requirements during the transitional period, for example where the Bank has concerns about the resolvability of an institution, or to implement international standards.

7.8 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 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.

7.9 The Bank may also set 'transitional' MREL, 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 where the change in MREL is material.

(1) Leverage exposure shall be calculated on the same basis as the PRA's leverage ratio requirement.