



BANK OF ENGLAND

October 2017

# Internal MREL — the Bank of England’s approach to setting a minimum requirement for own funds and eligible liabilities (MREL) within groups, and further issues

Consultation on a proposed updated Statement of Policy





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## Consultation on a proposed updated Statement of Policy

This consultation paper sets out amendments to the Bank of England's 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.

The Bank of England reserves the right to publish any information which it may receive as part of this consultation.

Information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure, in accordance with access to information regimes under the Freedom of Information Act 2000 or the Data Protection Act 1998 or otherwise as required by law or in discharge of our statutory functions.

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The Bank of England welcomes comments on the proposed Statement of Policy by 2 January 2018. Please provide those comments by email to the address below:

[MRELfeedback@bankofengland.co.uk](mailto:MRELfeedback@bankofengland.co.uk)

Alternatively you may provide comments by post to:

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# 1 How internal MREL is needed to help solve 'too big to fail'

1.1 The financial crisis showed the damage that can be caused to the economy if banks are unable to fail without disrupting the financial system and the wider economy. Left with the prospect that people and businesses would not be able to withdraw cash, make payments or get the loans they needed if large banks were allowed to go into insolvency, governments were forced to rescue those that were failing. This resulted in the costs of failure falling on the public rather than on the banks' shareholders and creditors.

1.2 Both in the United Kingdom and globally, public authorities have taken steps to ensure that in the future the critical functions of failing banks can be maintained without having to bail them out. In particular the tools are now in place to ensure that the losses and recapitalisation needs of a firm are borne by the shareholders and creditors of a firm without disrupting the critical functions the firm provides to the economy. This is known as 'resolving' a bank, and avoids taxpayers having to inject funds.

1.3 Last year, the Bank published a response to our consultation and a Statement of Policy<sup>(1)</sup> setting out the methodology and framework that the Bank will generally apply when calculating the amount of capital instruments and debt liabilities that banks, building societies and investment firms and in-scope holding companies would be required to maintain. Requiring such entities to maintain a minimum amount of these resources is intended to provide assurance that there is sufficient loss-absorbing capacity (known as 'MREL') that can be exposed to losses or converted in a resolution while ensuring that the critical functions that the firm performs continue to be provided.

1.4 In the response to the MREL consultation, the Bank made clear that the focus of the consultation was on MREL that should be maintained by UK resolution entities<sup>(2)</sup> (referred to as 'external MREL'). In addition, the Bank made clear that it was continuing to develop its thinking in relation to other areas related to MREL and in particular how MREL should be distributed within banking groups.<sup>(3)</sup> Banking groups will often be composed of many subsidiaries sometimes located in, and operating across, different countries. It is in these operating companies that losses are likely to occur. In order to ensure that resolution tools can be used effectively, it is important that the financial resources needed to absorb these losses are appropriately distributed within the group. Putting these resources (referred to as 'internal MREL') into the right parts of the group reduces the risk that if a subsidiary makes

substantial losses, the rest of the group is unwilling or unable to inject additional resources. In an international group, it also helps provide comfort to overseas regulators and resolution authorities that there will be sufficient resources to meet losses in their local subsidiaries as well as at the group level to make the resolution credible and to avoid the need for authorities in these host jurisdictions to have to take independent resolution action in respect of the subsidiaries.

1.5 Setting appropriate external MREL means that banking groups as a whole will have enough loss-absorbing capacity to be resolvable. If internal MREL were set in exactly the same way as external MREL, the sum of the internal requirements could exceed the external requirement. This is because subsidiaries in a group often have exposures to each other which net out at the group level. Instead, the Bank proposes to scale down the amount of internal MREL that applies to subsidiaries in line with standards for internal loss absorbency agreed internationally at the Financial Stability Board (FSB). This provides clarity and comfort that there is loss-absorbing capacity to maintain critical functions at subsidiaries. And through scaling internal MREL, there is more likely to be a surplus of external MREL over the sum of internal MREL which can be made readily available to support failing subsidiaries if pre-positioned internal MREL resources are not sufficient. This can bolster the overall resolvability of the group.

1.6 This consultation explains how the Bank plans to set internal MREL to ensure that resources are located in the right parts of a banking group to facilitate the preferred resolution strategy. It also proposes amendments to the Statement of Policy to address operational continuity requirements and the setting of external MREL for multiple point of entry (MPE) groups. In addition, it provides an update on how the Bank intends to develop its policy on requiring firms to disclose and report their MREL resources, and on restrictions on firms investing in each other's loss-absorbing resources.

1.7 Firms will need some time in order to meet these requirements. Once in place, MREL should deliver a sufficient level of assurance that the operating entities can continue to

(1) Available at [www.bankofengland.co.uk/financialstability/Documents/resolution/mrelpolicy2016.pdf](http://www.bankofengland.co.uk/financialstability/Documents/resolution/mrelpolicy2016.pdf).

(2) 'UK resolution entity' means those firms 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.

(3) See paragraph 2.15 of the Responses to Consultation, available at [www.bankofengland.co.uk/financialstability/Documents/resolution/mrelpolicy2016.pdf](http://www.bankofengland.co.uk/financialstability/Documents/resolution/mrelpolicy2016.pdf).

meet their regulatory resource requirements and help to ensure that the critical functions of a firm or group will not be disrupted in resolution. Published alongside this consultation paper is an update of *The Bank of England's approach to resolution*, which sets out the resolution process in detail and the Bank's general approach towards ensuring that banks can be resolved in a safe and orderly manner.<sup>(1)</sup>

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(1) [www.bankofengland.co.uk/financialstability/Documents/resolution/aproct17.pdf](http://www.bankofengland.co.uk/financialstability/Documents/resolution/aproct17.pdf).

## 2 Executive summary

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2.1 The minimum requirement for own funds and eligible liabilities (MREL) is a requirement for firms to maintain a minimum amount of loss-absorbing resources. MREL helps to ensure that when firms fail, the resolution authority can use a firm's own financial resources to absorb losses and recapitalise the business so it can continue to provide critical functions without the need to rely upon public funds. MREL resources can take the form of regulatory capital (own funds) and certain types of debt liabilities (eligible liabilities) that the Bank would expect to write down and/or convert to equity if a firm fails.

2.2 The MREL Statement of Policy published in November 2016 focused on the Bank's approach to 'external MREL': calibrating the MREL of UK resolution entities. This consultation paper explains the Bank of England's proposals in respect of 'internal MREL' — instruments that are issued to the resolution entity from other legal entities in a group — and sets out proposed additions and amendments to the MREL Statement of Policy that would be needed to address them. It also proposes amendments to the Statement of Policy to address operational continuity requirements and the setting of external MREL for multiple point of entry (MPE) groups. In addition, it provides an update on how the Bank intends to develop its policy on requiring firms to disclose and report their MREL resources, and on restrictions on firms investing in each other's loss-absorbing resources.

2.3 The Bank proposes that the transition period to meet internal MREL should be the same as for external MREL. Interim internal MREs will apply from 1 January 2019 for material subsidiaries of G-SIBs and from 1 January 2020 for other firms. End-state internal MREs will apply from 1 January 2022. The Bank will communicate to firms annually their resolution strategies, the critical functions (if any) that they or their group provide, and their internal MREL (if any).

2.4 Internal MREL is intended to cover UK-headquartered banking groups as well as UK subsidiaries of overseas banking groups. Internal MREL above capital requirements is likely to be necessary only where it is considered that insolvency of the

group would put the Bank's resolution objectives at risk. The Bank proposes to set internal MREL above capital requirements for 'material subsidiaries' of such groups, which represent at least 5% of a group's risk-weighted assets, operating income or leverage exposures. Internal MREL above capital requirements may also be calculated on a consolidated or sub-consolidated basis (known as a material sub-group).

2.5 The Bank expects that internal MREL for a material subsidiary will be scaled in the range of 75% to 90% of the full amount of external MREL that would apply if the subsidiary were itself a UK resolution entity. In deciding whether to set internal MREL for a material subsidiary above 75% scaling, the Bank will take into account the credibility of the resolution plan, the availability of other resources in the group that could be readily deployed to support the material subsidiary, and the scaling of internal loss-absorbing resources applied by overseas authorities to material subsidiaries located in their jurisdiction. Surplus MREL — the difference in requirements between group consolidated external MREL and the sum of what must be issued to the resolution entity as internal MREL or equivalent instruments in other jurisdictions — should be readily available to recapitalise any subsidiary.

2.6 Instruments will need to meet certain criteria to qualify as internal MREL eligible liabilities. These include the same criteria as external MREL eligible liabilities. In particular, internal MREL eligible liabilities must be subordinated to operating liabilities. They must be issued directly or indirectly to the resolution entity. And they must contain contractual provisions that enable the Bank to convert them to equity or write them down without placing the subsidiary into resolution.

2.7 The Bank proposes that critical service providers supporting the delivery of the group's critical functions must maintain loss-absorbing capacity for operational continuity in resolution equivalent to at least 25% of the annual operating costs of providing services. This is in addition to resources meeting any internal MREL.

# 3 Introduction

3.1 In setting out its Statement of Policy on MREL, the Bank identified a number of other policy issues relating to MREL that it would consult on in due course. Those issues included policy around internal MREL as well as the approach to disclosure and reporting of MREL and to the cross-holding of MREL within the banking system.

3.2 There are two categories of MREL referred to in this document: 'external MREL' and 'internal MREL' (see Box 1 for a summary).

3.3 This consultation paper explains the proposals in respect of internal MREL and sets out proposed additions and amendments to that Statement of Policy that would be needed to address them. It also proposes amendments to the Statement of Policy to address operational continuity requirements and the setting of external MREL for multiple point of entry (MPE) groups. In addition, it provides an update on how the Bank intends to develop its policy on requiring firms to disclose and report their MREL resources, and on restrictions on firms investing in each other's loss-absorbing resources.

3.4 The Statement of Policy applies to: (i) banks, building societies and certain investment firms ('firms') that are authorised by the Prudential Regulation Authority (PRA) or Financial Conduct Authority (FCA); (ii) parent companies of such firms that are financial holding companies or mixed financial holding companies (holding companies); and (iii) PRA or FCA-authorised financial firms that are subsidiaries of such firms or such holding companies. For the purposes of this document, references to a 'firm' should, unless otherwise stated, be taken to include an entity referred to in (i) to (iii) and 'group' or 'banking group' should, unless otherwise stated, be interpreted as any group comprising one or more entities referred to in (i) to (iii) whether located and authorised in the United Kingdom or elsewhere. The Bank is the United Kingdom's resolution authority, and the PRA or FCA is the competent authority.

3.5 The PRA has previously noted<sup>(1)</sup> that it is considering its general approach on the interaction of prudential requirements at different levels of application in a banking group, as part of its wider work on groups-related issues. This consultation paper complements the PRA's work on groups-related issues and should provide clarity to firms as they define their group resource allocation strategies to meet the expectations of post-crisis financial reforms.

## The purpose of MREL

3.6 MREL is a requirement for firms (either on an individual or consolidated basis) to maintain a minimum amount of loss-absorbing resources.

3.7 These resources can be either in the form of equity or of certain types of debt liabilities that the Bank would expect to write down and/or convert to equity if a firm fails so that losses and recapitalisation needs are met by a firm's shareholders and creditors.

3.8 The purpose of MREL is therefore to help ensure that when firms fail, the resolution authority can use a firm's own financial resources to absorb losses and recapitalise the business so it can continue to provide critical functions without the need to rely upon public funds. Setting MREL is a critical element of establishing effective resolution strategies for UK banking groups that the Bank determines are of a scale or importance to the financial system that their critical functions cannot be left to be wound up in insolvency.

## SPE and MPE group resolution strategies

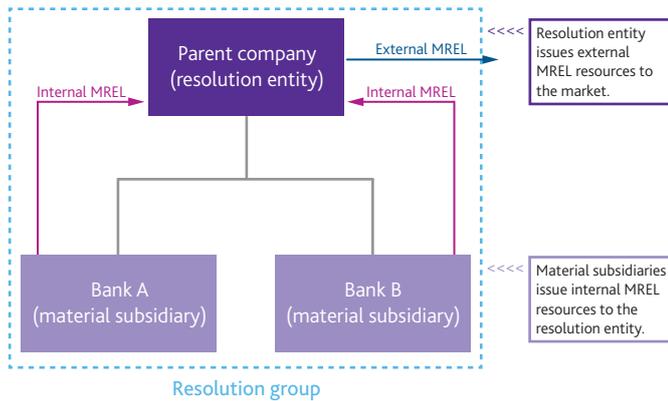
3.9 In the case of banking groups with cross-border operations, the group will have a group resolution strategy that is agreed between the resolution authority of the parent company in the group (the 'home authority') and the relevant authorities of the material subsidiaries located in other jurisdictions ('host authorities').

3.10 The group resolution strategy may either rely upon the use of resolution powers only at the parent of the group — known as a single point of entry (SPE) (**Figure 1**) — or may depend upon resolution powers being used at more than one entity within the group — known as a multiple point of entry (MPE) (**Figure 2**). Under SPE, the internal MREL will be issued by other entities in the group to the resolution entity either directly or indirectly.<sup>(2)</sup> In resolution, the write-down and/or conversion to equity of internal MREL will always result in the whole banking group remaining together as a group during the resolution, although parts of it may in time be wound down or

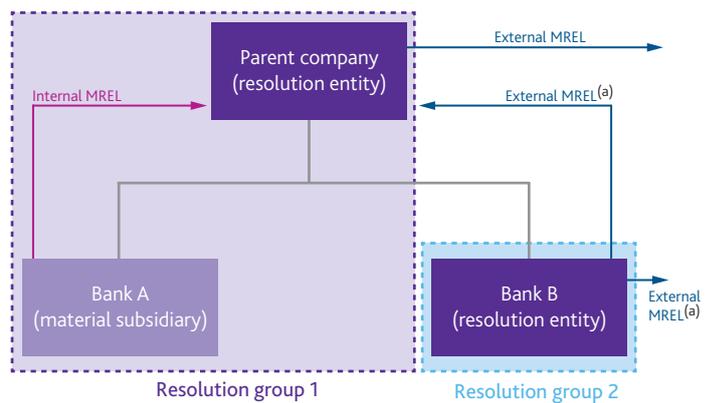
(1) See Prudential Regulation Authority (2016), 'The implementation of ring-fencing: reporting and residual matters', *PRA Consultation Paper CP25/16*, paragraph 7.9; [www.bankofengland.co.uk/pradocuments/publications/cp/2016/cp2516.pdf](http://www.bankofengland.co.uk/pradocuments/publications/cp/2016/cp2516.pdf).

(2) With the exception before 1 January 2022 of external issuance from subsidiaries of regulatory capital, as set out in Section 8 of the Statement of Policy.

**Figure 1** Single point of entry (SPE) resolution strategy



**Figure 2** Multiple point of entry (MPE) resolution strategy



(a) External MREL includes regulatory capital and eligible liabilities. See Section 9 for further details on how MREL may be issued for MPE resolution entities.

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

## General considerations in developing the internal MREL policy

3.11 In the November 2016 MREL Statement of Policy, the Bank noted that it 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 entity which issues them; and
- (c) internal MREL resources must be appropriately distributed within groups.

3.12 In developing its policy approach to setting internal MREL and in line with the above principles, the Bank has had particular regard to the following considerations.

### (1) Internal MREL should implement the FSB's TLAC standard for UK G-SIBs and support cross-border co-operation on resolution issues

3.13 The Bank is implementing the Financial Stability Board's (FSB's) total loss-absorbing capacity (TLAC) standard through setting external and internal MREL.<sup>(1)</sup> The TLAC standard

represents international agreement on the common minimum standard for loss-absorbing capacity that should apply to G-SIBs. Meeting international standards should support cross-border co-operation, providing comfort to other authorities that the resolution plans and strategies for UK banks are credible. The Bank's internal MREL framework builds on the TLAC standard in certain areas, for example by applying internal MREL to a wider set of firms than the G-SIBs that are covered by the TLAC standard.

### (2) Internal MREL should contribute towards delivering feasible and credible group resolution plans and support the use of resolution tools

3.14 As explained above, internal MREL is critical to supporting the continuity of critical functions at operating entities. By pre-positioning internal MREL resources at subsidiaries, losses and recapitalisation needs are passed up to the resolution entity without the operating entity needing to enter resolution. Resolution tools, such as bail-in, can then be applied at the resolution entity, as envisaged in the resolution plans.

### (3) The sum of internal MRELS should not exceed external MREL and so a surplus of MREL should be readily available at group level

3.15 Internal MREL calibration will aim to strike a balance between providing sufficient clarity and comfort for counterparties and other authorities that there are sufficient resources pre-positioned to support the resolution strategy, while recognising that the appropriate calibration of external MREL is in place on a consolidated basis which nets out exposures between subsidiaries and sub-groups. By scaling down internal MREL, a resolution entity should be left with sufficient external MREL resources to cover all the 'internal

(1) See [www.fsb.org/wp-content/uploads/TLAC-Principles-and-Term-Sheet-for-publication-final.pdf](http://www.fsb.org/wp-content/uploads/TLAC-Principles-and-Term-Sheet-for-publication-final.pdf).

## Box 1

### External and internal MREL

**External MREL instruments are issued from a 'resolution entity' in a group**, that is to say, the entity that would be subject to the use of resolution powers under the preferred resolution strategy. The Statement of Policy published in November 2016 focused on the Bank's approach to calibrating the MREL of resolution entities that are incorporated in the United Kingdom.

**Internal MREL instruments are issued from legal entities in a group that are not themselves resolution entities.** They are issued directly or indirectly to the resolution entity in their group (Figure A). Like external MREL, these resources can be in the form of equity or debt. Unlike external MREL, these internal MREL instruments are designed to be written down or converted to equity to recapitalise the entity that issues them without the need to use resolution powers on that entity.

Internal MREL instruments have the effect of passing losses within the group so that they can then be absorbed by the shareholders and creditors of the resolution entity through use of the resolution tools. Where a group is made up of operating entities that are material to the delivery of critical functions provided by the banking group, it is important that these operating entities have internal MREL resources so that they can be recapitalised without having to place each of them into a resolution process.

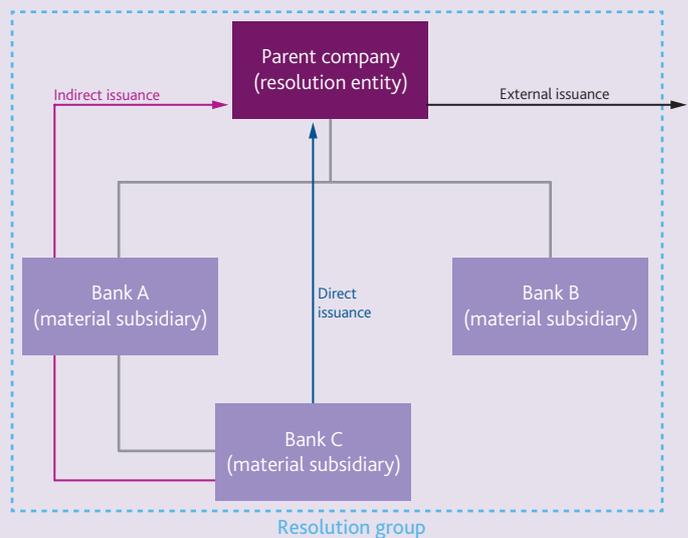
In developing the preferred resolution strategies, the Bank will identify the legal entity within the group to which the Bank would expect to apply its resolution powers (if any) and which would therefore be the UK resolution entity for which

loss-absorbing resources<sup>(1)</sup> it has invested in (including internal MREL to support operational continuity in resolution). Scaling also supports a surplus of external MREL over the sum of internal MREL which can be made readily available to support failing subsidiaries if pre-positioned internal MREL resources are not sufficient.

#### (4) MREL eligibility criteria specified by the Bank should be common to both regulatory capital instruments and eligible liabilities

3.16 MREL comprises regulatory capital instruments and eligible liabilities meeting certain criteria. In the Bank's view there are resolvability benefits where both regulatory capital and eligible liabilities comply with the same criteria to ensure that they are available to absorb losses and/or recapitalise entities as needed in order to support the group resolution strategy. Therefore the internal MREL eligibility criteria specified by the Bank should be common to both regulatory

Figure A Direct and indirect issuance of internal MREL



'external MREL' is set (see 'SPE and MPE resolution strategies' above).

Placing sufficient internal MREL resources at subsidiaries (referred to as 'pre-positioning') should reduce the risk that the wider group is unable or unwilling to commit the funds to support it. By doing so, it provides greater clarity and confidence to that subsidiary's financial counterparties, customers and creditors about how losses of the company will be addressed by a group resolution strategy. Similarly, pre-positioning provides assurance to overseas authorities that subsidiaries in their jurisdiction will be recapitalised. Aligning incentives between authorities in this way helps international co-operation in a cross-border resolution. In doing so, it offers comfort for host authorities who might otherwise set higher capital requirements.

capital instruments<sup>(2)</sup> and eligible liabilities that comprise an entity's internal MREL.

### Legislative context

3.17 The Bank must set internal MREL in line with relevant statutory requirements. The principal requirements arise from:

- (a) **The Banking Act 2009 ('Banking Act') and associated legislation.** The Banking Act and associated secondary legislation, including the Bank Recovery and Resolution (No. 2 Order) 2014 ('No. 2 Order'), transpose the EU Bank Recovery and Resolution Directive 2014/59/EU ('BRRD') into UK law. The No. 2 Order requires the Bank to set

(1) 'Internal loss-absorbing resources' is used to mean internal MREL resources or, in other jurisdictions, equivalent subordinated instruments that can absorb losses and recapitalise a subsidiary, such as through being written down and/or converted to equity, without the use of stabilisation or resolution powers at the subsidiary level.

(2) Except CET1 in respect of certain internal MREL eligibility criteria.

MREL, specifies the criteria that the Bank must consider when setting MREL, sets out the scope of entities and groups for which MREL must or may be set, sets certain eligibility requirements for MREL resources and imposes procedural requirements.

- (b) **Regulatory Technical Standards on MREL.** The European Banking Authority's (EBA) RTS on MREL (the 'MREL RTS') further specify the criteria which the Bank must consider when setting MREL. The MREL RTS are binding on the Bank.<sup>(1)</sup>

3.18 The No. 2 Order requires the Bank to set MREL on the basis of criteria set out in the BRRD and reproduced below, which are further specified in the MREL RTS:

- the need to ensure that the firm can be resolved by the application of the resolution tools including, where appropriate, the bail-in tool, in a way that meets the resolution objectives;
- the need to ensure, in appropriate cases, that the firm 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 firm 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 the Capital Requirements Directive 2013/36/EU (CRD4) or Directive 2014/65/EU (MiFID2) and to sustain sufficient market confidence in the firm;
- 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) of the BRRD or that certain classes of eligible liabilities might be transferred to a recipient in full under a partial transfer, the firm has sufficient other eligible liabilities to ensure that losses could be absorbed and the common equity Tier 1 ratio of the firm could be restored to a level necessary to enable it to continue to comply with the conditions for authorisation and to continue to carry out the activities for which it is authorised under CRD4 or MiFID2;
- the size, the business model, the funding model and the risk profile of the firm;
- the extent to which the Deposit Guarantee Scheme could contribute to the financing of resolution in accordance with Article 109 of the BRRD; and
- the extent to which the failure of the firm would have adverse effects on financial stability, including due to its interconnectedness with other firms or with the rest of the financial system through contagion to other firms.

3.19 The Bank's proposed changes to the Statement of Policy describe how the Bank will set internal MREL in line with the relevant statutory requirements; it does not reproduce or describe these requirements in detail. Readers should refer to the relevant legislative requirements where necessary. It should also be noted that the European Commission has proposed a package of amendments in November 2016 to legislation that is relevant to MREL, including to BRRD, CRD4 and the Capital Requirements Regulation (575/2013) ('CRR'). The outcome and timing of any amendments is uncertain. The Bank will assess as necessary whether to change its MREL framework as a result.

3.20 As noted in the November 2016 MREL Statement of Policy, 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 firms' experience in issuing liabilities to meet their interim MRELS.

## Outline of this document

3.21 The rest of this document is structured as follows:

- (1) **Scope of internal MREL** describes the subsidiaries that are likely to be subject to internal MREL greater than capital requirements;<sup>(2)</sup>
- (2) **Calibration of internal MREL** discusses how the size of the requirements will be determined;
- (3) **Internal MREL instrument eligibility** sets out the criteria instruments should meet to qualify as internal MREL resources;
- (4) **Transitional arrangements for internal MREL** sets out the timeframe over which entities will need to meet internal MREL;
- (5) **Loss-absorbing capacity for operational continuity** covers loss-absorbing capacity requirements for critical service providers;
- (6) **External MREL for banking groups with MPE resolution strategies** describes how MREL will be determined for MPE resolution and on a group consolidated basis;
- (7) **Other changes to the MREL Statement of Policy** notes other changes that are proposed to the existing Statement of Policy;

(1) Available at <https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2976-EN-F1-1.PDF>.

(2) 'Capital requirements' means the higher of (1) the amount and quality of own funds the appropriate regulator (PRA or FCA) thinks the firm should hold at all times under the overall financial adequacy rule (for PRA-authorized persons Internal Capital Adequacy Assessment 2.1 PRA Rulebook and for FCA-authorized persons IFPRU 2.2.1R of the FCA Handbook) as it applies on a solo or a consolidated level; (2) (if applicable) minimum leverage ratio in Leverage Ratio 3.1 of the PRA Rulebook; and (3) (if applicable) the Basel I floor.

- (8) **Other issues regarding the Bank's policy approach to MREL** contains the Bank's thinking on a number of additional policy areas related to MREL, including:
  - (a) **Restrictions on banks' ability to hold each other's MREL;**
  - (b) **Disclosure of MREL resources by firms;** and
  - (c) **MREL reporting.**
- (9) **Impact assessment** provides an updated impact assessment of the MREL framework;
- (10) **Next steps** sets out the Bank's questions for respondents to the consultation and the process for submitting responses;
- (11) **Appendix 1** shows the proposed updated Statement of Policy;
- (12) **Appendix 2** shows the proposed changes to the Statement of Policy relative to the Statement of Policy that was published in November 2016.

# 4 Scope of internal MREL

## Communication to firms

4.1 The Bank will communicate to firms or their holding company annually their resolution strategies, the critical functions (if any) that they or their group provide, and their internal MREL (if any).<sup>(1)</sup>

## Material subsidiaries

4.2 Internal MREL is intended to cover UK-headquartered banking groups as well as UK subsidiaries of overseas banking groups (it does not apply to resolution entities). In each case internal MREL above capital requirements is likely to be necessary only where it is considered that insolvency of the firm would put the Bank's resolution objectives at risk.<sup>(2)</sup> Accordingly, the Bank proposes to set internal MREL above capital requirements for a 'material subsidiary' of a group where either (a) there is a UK resolution entity which is or will become subject to an external MREL above its capital requirements; or (b), in the case of UK subsidiaries of overseas groups, the subsidiary delivers critical functions in the United Kingdom.<sup>(3)</sup>

4.3 A subsidiary is a 'material subsidiary' if it is incorporated in the United Kingdom, is not a resolution entity, and is:

- (1) 'material' in terms of its size relative to the rest of the group; or
- (2) otherwise 'material', either directly or through its subsidiaries, to the delivery of a banking group's critical functions in the United Kingdom.

4.4 'Critical functions' are broadly defined as activities, services or operations that, if a firm stopped providing them, could disrupt the economy or financial stability due to the firm's size or market share.<sup>(4)</sup> Critical functions may include retail banking, corporate banking, wholesale banking, payment and settlement services, and other financial services.

4.5 Whether or not a subsidiary in the United Kingdom is 'material' is a decision that the Bank will take on a case-by-case basis having regard to the particular circumstances of the group. The Bank expects that a subsidiary will, however, be material if it meets at least one of the following criteria, consistent with the FSB's TLAC standard:

- (a) has more than 5% of the consolidated risk-weighted assets of the group; or
- (b) generates more than 5% of the total operating income of the group; or
- (c) has a total leverage exposure measure larger than 5% of the group's consolidated leverage exposure measure.

4.6 The materiality criteria above reflect that once subsidiaries are above a certain size, it becomes more likely that — in the event of failure — the group resolution plan will be engaged, with the resolution entity entering resolution. Also, it will become more difficult for a group to provide support if the entity gets into difficulty even if it were in the interests of the group to do so.

4.7 Exceptionally, there may be subsidiaries that are essential to carrying out critical functions in the United Kingdom and so should have internal MREL above capital requirements even though they do not meet the materiality criteria (a) to (c). The Bank will continue to review firms' structures and critical functions to judge if this applies to any entities. Decisions about which subsidiaries should have internal MREL above capital requirements will be informed by discussions with other relevant resolution authorities and through crisis management groups and resolution colleges as appropriate.

4.8 For branches of foreign banks that operate in the United Kingdom and which perform critical functions, the Bank will look at the adequacy of the group resolution plan in such cases, covering the amount and distribution of the group's loss-absorbing resources and how the branch will be treated. This includes whether the entity which the branch forms a part of is subject to MREL or equivalent requirements. In cases where the Bank has concerns about the resolution plan, it will engage with the home authority to deal with the issue.

(1) Firms which form part of a group for which the Bank is not the EU group level resolution authority will receive communication via the relevant EU group level resolution authority.

(2) For example, the Statement of Policy provides an indicative threshold that firms with below 40,000–80,000 transactional accounts would have a modified insolvency resolution strategy.

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

(4) See section 3(1) of the Banking Act and Prudential Regulation Authority (2013), 'Resolution planning', PRA Supervisory Statement SS19/13; [www.bankofengland.co.uk/pradocuments/publications/policy/2013/resolutionplanning1913.pdf](http://www.bankofengland.co.uk/pradocuments/publications/policy/2013/resolutionplanning1913.pdf).

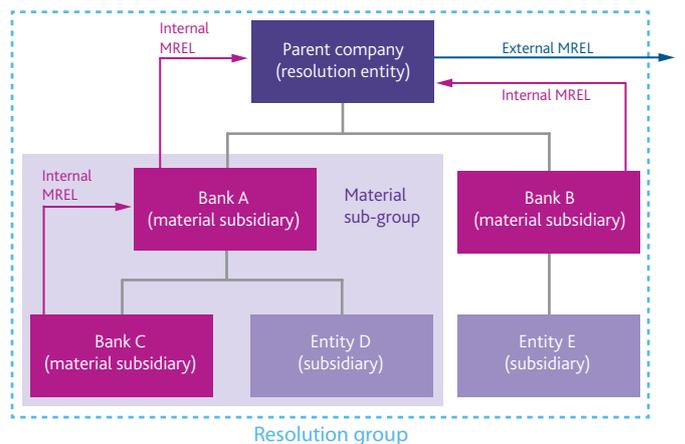
## Material sub-groups

4.9 The Bank generally expects to set internal MREL above capital requirements for material subsidiaries based on their solo (individual) or, where applicable, solo consolidated balance sheets.

4.10 Internal MREL will apply to the parent entity in existing prudential consolidation or sub-consolidation — where the consolidated or sub-consolidated regulatory group meets the criteria in paragraphs 4.2–4.5 — which will be calculated with reference to its consolidated or sub-consolidated prudential requirements. The consolidation or sub-consolidation which is used to calculate internal MREL in such cases is referred to as a ‘material sub-group’ (Figure 3). A material subsidiary that heads up such a sub-group will be bound by the higher of its internal MREL calculated on an individual or consolidated/ sub-consolidated balance sheet basis.

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

Figure 3 Material sub-groups



- External MREL above capital requirements
- Internal MREL above capital requirements
- No internal or external MREL above requirements

**Bank A:** internal MREL set on a sub-consolidated basis and an individual basis

**Bank B:** internal MREL set on an individual basis

**Bank C:** internal MREL set on an individual basis

**Entities D and E:** internal MREL equal to capital requirements where applicable

# 5 Calibration of internal MREL

5.1 In line with the TLAC standard, the Bank expects that internal MREL for a material subsidiary will be scaled in the range of 75% to 90% of the full amount of external MREL that it would otherwise be required to maintain if the material subsidiary were itself a UK resolution entity and its external MREL were set in accordance with the Statement of Policy (see Box 2 for a summary). This is consistent with the BRRD requirement that the individual MREL set for firms takes account of the group consolidated requirement.<sup>(1)</sup>

5.2 In deciding whether to set internal MREL for a material subsidiary above 75% scaling, the Bank will take into account the following considerations:

## The resolution strategy applicable to the group and the credibility of the resolution plan for delivering it

5.3 A resolution strategy that anticipates maintaining the continuity of critical functions of the UK subsidiaries and which is credible in terms of execution should facilitate an internal MREL towards the bottom of the range. Substantive impediments to the resolvability of the group or of the UK subsidiary, or where resources are insufficient for a solvent wind-down, may mean that the internal MREL needs to be scaled at a higher level than 75% of the full MREL amount.

## The availability of other uncommitted resources within the group that could be readily deployed to support the material subsidiary

5.4 Where uncommitted resources such as surplus MREL are readily available, this would facilitate scaling towards the bottom of the range. In considering the availability of resources, the Bank will have regard to the type of financial resource, including the ease and certainty with which resources can be transferred in order to recapitalise the material subsidiary. This would take into account certainty of valuations, legal, regulatory, operational or other impediments to deployment. In particular, the Bank's view is that the absence of contractual language, in both non-CET1 regulatory capital instruments and eligible liabilities, described in Section 6 as regards triggering of write-down and/or conversion to equity is likely to constitute an impediment to resolution.

## The scaling of internal loss-absorbing resources applied by overseas authorities to material subsidiaries located in their jurisdiction

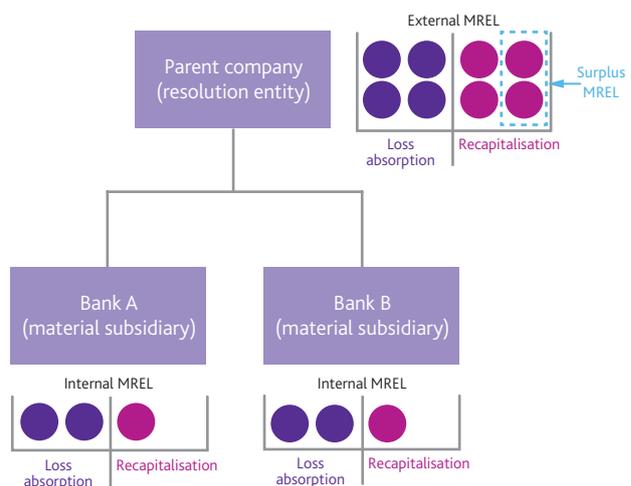
5.5 Where other resolution authorities set requirements at the upper end of the 75% to 90% range, this may reduce the availability of extra resources that would be available to

UK entities and may signal concerns about the credibility of the resolution strategy and cross-border co-operation. The Bank would need to take this into account in setting its own internal MREL and it may lead to the Bank scaling at the upper end of the range for specific UK firms.

## Availability of surplus MREL in groups

5.6 As noted above, the availability of other uncommitted resources is a relevant factor in the calibration of internal MREL. Where there is less assurance that surplus MREL — the difference in requirements between external MREL and the sum of what must be issued to the relevant resolution entity as internal loss-absorbing resources (**Figure 4**) — is readily available, the Bank may view this as a factor supporting a higher scaling of internal MREL. For groups with UK resolution entities, the Bank expects that any such surplus MREL should be readily available to recapitalise any direct or indirect subsidiary as necessary to support the execution of the resolution strategy and there should be no legal or operational barriers to this.

**Figure 4** Internal MREL scaling and surplus MREL



Note: The filled circles represent the amount of MREL resources. These are shown as 'loss absorption' and 'recapitalisation' amounts (see Box 2 for an explanation of these terms).

5.7 One way in which it would be possible to make surplus MREL readily available is for groups to use the surplus MREL to invest in high-quality liquid assets which would be maintained at the relevant resolution entity.<sup>(2)</sup> This would constitute a

(1) Article 45(10) of the BRRD.

(2) High-quality liquid assets as defined in Part Six (Liquidity) of CRR and the European Commission Delegated Act with regards to the liquidity coverage requirement (LCR) for credit institutions.

## Box 2 Summary of external MREL calibration

The Bank's MREL Statement of Policy sets out a framework for calibrating the external MREL that a firm must meet. The Bank calculates MREL as the sum of two components: a 'loss absorption' amount and a 'recapitalisation' amount. The loss absorption amount reflects the losses that would need to be absorbed up to and in resolution. The Bank generally expects to set the loss absorption amount equal to a firm's capital requirements. The recapitalisation amount reflects the capital that a firm, or the entity to which the firm's assets and liabilities are transferred, is likely to require to meet capital requirements and command market confidence after the resolution. The recapitalisation amount will depend on the preferred resolution strategy applicable to a firm. The Bank generally expects to set the recapitalisation amount equal to a firm's capital requirements for bail-in firms. The recapitalisation amount might be reduced in the case of partial transfer firms where less than the entire balance sheet would

need to be recapitalised in resolution. For modified insolvency firms, the Bank expects to set the recapitalisation amount to zero.

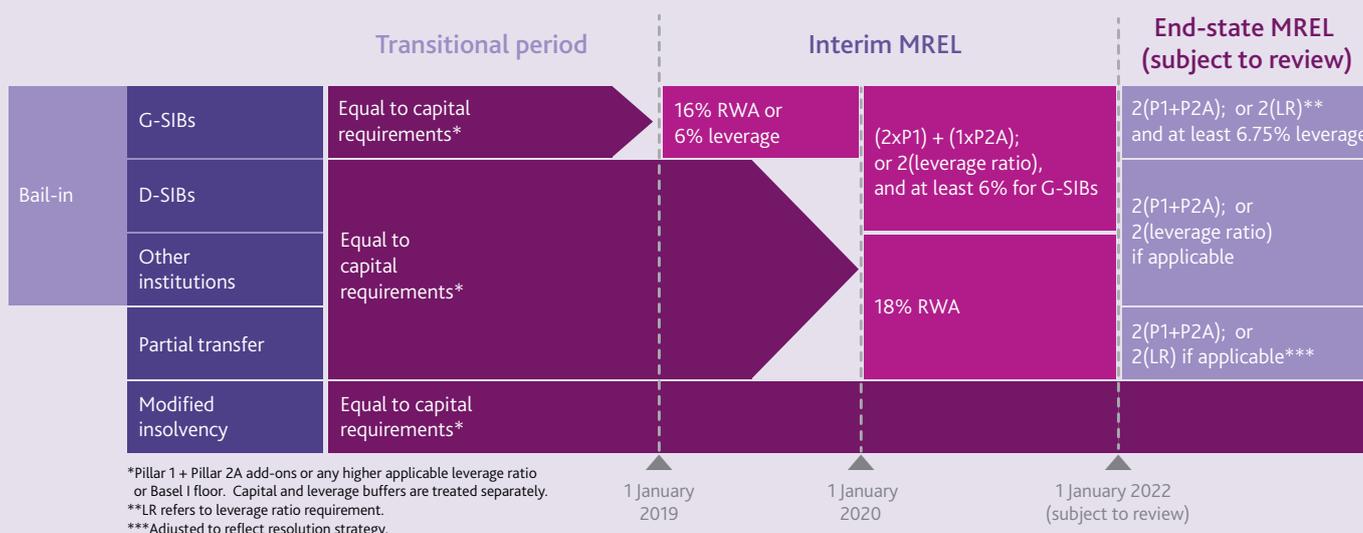
For UK firms that have a resolution strategy that involves the use of bail-in, the resolution entity must have an end-state external MREL by 1 January 2022 equal to the higher of:

- two times the sum of Pillar 1 and Pillar 2A capital requirements;<sup>(1)</sup> or
- the higher of two times their leverage ratio requirement (if applicable) or, for G-SIBs, 6.75% of leverage exposures.

There are interim requirements in 2019 for G-SIBs and for all bail-in firms in 2020 (Figure A). The end-state external MREL calibration will be subject to review by the end of 2020. As the calibrations of external and internal MREL are closely related, the review will also be relevant to internal MREL.

(1) Or, if higher and should it continue to apply after 31 December 2017, the Basel I floor.

Figure A Summary of external MREL calibration and transition



'central reserve' of MREL which could be made available to material subsidiaries as needed, on the agreement of home and host authorities.

## Internal MREL for ring-fenced bodies

5.8 The largest banking groups in the United Kingdom are subject to legislation<sup>(1)</sup> which will require them to carry out their core UK financial services and activities within a ring-fenced body (RFB) and separate these from certain other activities of the wider group. Where an RFB is part of a material sub-group, the Bank proposes to scale the internal MREL for the top entity of the material sub-group at 90%, as a starting point, unless the Bank is satisfied that the wider group

has sufficient readily-deployable resources to justify moving to a lower calibration in the 75% to 90% range.<sup>(2)</sup> This approach is intended to ensure that the setting of internal MREL for RFBs is in line with the range set out in the FSB's international standard while minimising the RFB's dependence on the rest of the group, consistent with the PRA's ring-fencing objectives. The Bank is committed to working with overseas resolution authorities to build confidence in each other's resolution regimes. This should help contribute towards the ability to

(1) The Financial Services and Markets Act 2000, as amended by the Financial Services (Banking Reform) Act 2013.  
 (2) This may not apply in certain cases, including: (1) where the top entity within an RFB's material sub-group is a resolution entity, it will be subject to external MREL and so scaling will not apply to it; and (2) where the RFB's group has a simple structure, the Bank would not expect to adjust downwards the internal MREL (see paragraph 5.10).

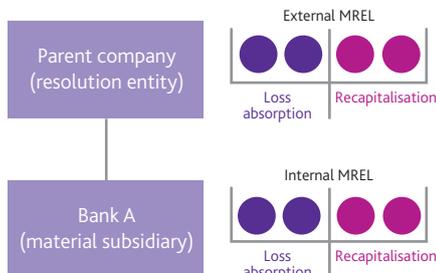
make reductions over time in the internal MREL in material sub-groups that contain an RFB.

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

## UK groups with a simple structure

5.10 For UK groups with a simple structure — for example, a single material subsidiary that sits below a UK resolution entity with few, if any other, subsidiaries — the Bank would not expect to adjust downwards the internal MREL for that UK material subsidiary. This means the internal MREL would be set at 100% of the external MREL that would have applied to the material subsidiary if it were a resolution entity (Figure 5). The Bank would also apply this approach for the top entity of material sub-groups containing an RFB or for an RFB which is not part of a material sub-group if the RFB's group has a simple structure. Scaling down in this situation could simply result in the externally issued MREL being used to fund the material subsidiary in a form that was not eligible for internal MREL. The Bank's approach to not applying scaling would be judgement-based, and decided on a case-by-case basis, giving due consideration to the relationship between the risk profile of a material subsidiary and its wider group.

**Figure 5** Internal MREL for UK groups with a simple structure



## Process for setting internal MREL for UK material subsidiaries of foreign banking groups

5.11 In the case of a UK firm that is a material subsidiary of a banking group that is not headquartered in the United Kingdom, the Bank will set the amount of internal MREL following discussion with the home authority in a crisis management group or other forum. In the case of EU banking groups, the determination of the quantum of internal MREL and indeed external MREL will take place through a joint decision-making process in resolution colleges. In either forum, the Bank expects to be guided by the principles set out in this consultation and Statement of Policy.

## Internal MREL for non-UK material subsidiaries of UK banking groups

5.12 The responsibility for setting internal MREL or equivalent requirements for non-UK material subsidiaries of UK banking groups lies with the host authorities in consultation with the Bank as home authority. However, if requirements are not set by host authorities, the Bank may reach a determination that this is likely to constitute an impediment to the resolvability of the group. As a result, the Bank expects to propose a quantum for internal MREL for non-UK material subsidiaries where the host authority has not published regulations or regulatory proposals. In doing so, the Bank expects to be guided by the principles set out in this consultation and Statement of Policy.

## Avoidance of double counting of MREL resources in groups

5.13 A subsidiary or sub-group should only count the internal MREL resources that it issues towards meeting its own internal MREL. Where a subsidiary or sub-group has subsidiaries that also have internal MREL resources, it should ensure that it has sufficient internal MREL to match both its own individual MREL as well as the internal MREL of its subsidiaries. In order to achieve this, the Bank proposes that internal MREL for a material subsidiary or sub-group will be increased by the amount of any internal MREL (or loss-absorbing capacity for operational continuity) investments it has made in other entities in the same group.

5.14 An entity's investments in a subsidiary's MREL resources that are not deducted from its own capital resources according to prudential requirements may also be subject to large exposure limits. The Bank is working with the PRA to ensure that any interactions between the large exposures framework and MREL are managed appropriately.

## 6 Internal MREL instrument eligibility

6.1 The MREL Statement of Policy sets out the conditions which eligible liabilities must meet to qualify as external MREL resources. The Bank proposes all the eligibility criteria set out in paragraphs 5.2–5.8 of the Statement of Policy that apply to external MREL resources apply equally to internal MREL eligible liabilities. These include:

- (1) they must have a minimum effective remaining maturity of one year (where liabilities include an incentive to redeem, the maturity date of the liability shall, for the purposes of determining eligibility for internal MREL, be considered to be the date at which the incentive arises);
- (2) they must not be able to be called by the issuer or cancelled or redeemed by the holder prior to their maturity if that would cause the entity to breach its internal MREL, or if the entity is already in breach of its internal MREL, unless the Bank approves such a transaction;
- (3) they must not depend on derivatives for their value (liabilities which only include put or call options are not considered to be dependent on derivatives for this purpose);
- (4) they must not be subject to contractual set-off or netting arrangements; and
- (5) where they are governed by non-EEA law, firms will need to ensure that the liability could absorb losses and contribute to recapitalisation costs in resolution, having regard to the terms of the contract and legal opinions, in line with the BRRD and the contractual recognition of bail-in rules in the PRA Rulebook and FCA Handbook.<sup>(1)</sup>

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

- (1) subordination;
- (2) the holder of the instrument;
- (3) contractual triggers; and
- (4) mismatching of internal and external MREL.

### Subordination

6.3 As in the case of eligibility for external MREL eligible liabilities, internal MREL resources must be subordinated to the operating liabilities of the group entities issuing them. This is necessary to ensure that, in converting internal MREL, the Bank is not required to bail in other liabilities that might rank *pari passu* and which may either be difficult to bail in or would result in a change of ownership of the entity if converted into equity. Internal MREL eligible liabilities will need to be contractually or statutorily subordinated. However, if the entity is a holding company, it may be permitted to issue internal MREL instruments as senior liabilities provided that the sum of its liabilities that do not meet the other internal MREL eligibility criteria (excluding liabilities that previously met the internal MREL eligibility criteria but no longer meet the minimum maturity requirement referred to in paragraph 5.2 of the Statement of Policy) do not exceed 5% of the entity's overall internal MREL resources (see Section 6 of the Statement of Policy).

### The holder of the instrument

6.4 Firms should ensure that the issuance of internal MREL by a material subsidiary or sub-group credibly supports the resolution strategy and the passing of losses and recapitalisation needs to the resolution entity. Internal MREL eligible liabilities must therefore be issued either directly or indirectly via other entities in the same resolution group to the parent resolution entity (**Figure A** in Box B). The Bank generally expects to accept issuance indirectly to the resolution entity along the chain of ownership, as long as there are no technical obstacles to the resolution entity becoming exposed to losses through this chain. Direct issuance could also be acceptable unless there are circumstances in which converting internal MREL to equity could result in a change of control that could be an impediment to resolution — for example if there were significant governance or tax issues as a result.

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

<sup>(1)</sup> See [www.prarulebook.co.uk/rulebook/Content/Part/211722/26-10-2016](http://www.prarulebook.co.uk/rulebook/Content/Part/211722/26-10-2016) and <https://www.handbook.fca.org.uk/handbook/IFPRU/11/6.html?date=2016-06-30>.

discuss the distribution of MREL resources generally with firms as part of the process of setting MREL.

6.6 The Bank's view is that external issuance of internal MREL from non-resolution entity subsidiaries in both regulatory capital instruments and eligible liabilities is likely to constitute an impediment to resolution. In line with this, externally issued regulatory capital in subsidiaries of a resolution entity may be used to meet that subsidiary's internal MREL to the extent that it qualifies as regulatory capital until the current end-state MREL date of 1 January 2022. After that point, only externally issued CET1 issued by such subsidiaries should be used to meet a subsidiary's internal MREL and only then if external issuance of CET1 is required by local regulations.

## Contractual triggers

6.7 One of the principal purposes of internal MREL is to avoid the need to use statutory resolution powers on material subsidiaries that sit below the resolution entity. By being able to limit the use of stabilisation powers to the level of the resolution entity, internal MREL removes the execution risk in co-ordinating the use of tools simultaneously across multiple jurisdictions and entities as well as reducing the risk that counterparties of a material subsidiary seek to close-out or terminate arrangements at operating subsidiaries. To achieve this, internal MREL eligible liabilities must be capable of being written down or converted to equity without or ahead of any use of resolution powers in relation to the entity that issues them. Internal MREL eligible liabilities must therefore contain a contractual clause that allows the Bank to write down and/or convert the instrument to equity when certain conditions are met.

6.8 As a general matter, the trigger for an internal MREL instrument will need to provide the resolution authority of the material subsidiary with the right to exercise a write-down or conversion where:

- the resolution authority determines that the subsidiary is failing or likely to fail and will, disregarding any write-down and/or conversion of the instruments, continue to be so; and for internal MREL for subsidiaries of non-UK groups, the home resolution authority consents or does not object to the write-down or conversion following 24 hours' notice; or
- a resolution entity in the group, which is a direct or indirect parent of the subsidiary, is subject to resolution proceedings in the United Kingdom or elsewhere.<sup>(1)</sup>

6.9 The Bank's view is that the absence of contractual triggers described above in both non-CET1 regulatory capital instruments and MREL eligible liabilities is likely to constitute an impediment to resolution on the grounds that (i) the joint

home-host trigger envisaged by the contractual trigger provides the mechanism for the home and host authorities to agree whether additional resources are required by the relevant subsidiary in addition to the capital provided by the conversion of the internal MREL and (ii) the ability to trigger all internal MREL simultaneously provides assurance that all relevant subsidiaries are well-capitalised and ensures that the surplus resources are available to the subsidiaries (if any) that require additional resources. The Bank therefore expects firms to include those terms in any internal MREL resources (including any non-CET1 regulatory capital).

6.10 The particular features of the contractual terms of an entity's internal MREL may depend on the specific resolution strategy for a firm and may require discussion between the firm and the Bank. Having confirmed these features, the responsibility for ensuring that instruments are MREL eligible rests with the firm. Firms should obtain independent legal advice on a liability's eligibility, and provide this to the Bank where required. Firms are expected to notify the Bank where they do not intend to include the additional contractual provisions in regulatory capital investments. In line with the continuous resolvability assessment process, firms will also be expected to demonstrate compliance with the eligibility criteria on request.

## Mismatching of internal and external MREL

6.11 The Bank proposes periodically to review the extent to which internal MREL resources of a material subsidiary differ in form — such as equity or debt, currency, maturity, interest rate, and other terms and covenants — from the MREL issued externally from the resolution entity where this may pose risks to the resilience and resolvability of the group. Differences in the form of internal and external MREL may weaken the resilience and resolvability of a group. For example, the resolution entity may be reliant on dividend payments with which to service externally or internally issued debt. Firms should notify the Bank if they expect there to be any material change in the form of their internal MREL resources; for example firms should not change the form of their internal MREL resources in a way, such as through cancellation or conversion to equity, that reduces the amount of MREL eligible liabilities, unless the Bank approves such a transaction.

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

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

# 7 Transitional arrangements for internal MREL

7.1 The Bank proposes that the transition period to meet internal MREL should be the same as for external MREL (Figure 6).

7.2 The Bank may on a firm-specific basis set an earlier compliance date during the transitional period for interim and/or end-state external or internal MREs greater than regulatory capital requirements, for example where the Bank has concerns about the resolvability of a firm, or to implement international standards.

**Figure 6** Summary of internal MREL calibration and transition<sup>(a)(b)</sup>

Internal MREL for material subsidiaries and sub-groups of:	1 January 2019	1 January 2020	1 January 2022 (subject to review)
G-SIBs	(16% RWA or 6% LR) x scalar	$([2xP1]+[1xP2A])$ or 2 x LR if applicable and at least 6%) x scalar	$(2x[P1+P2A])$ or 2 x LR if applicable and at least 6.75%) x scalar
D-SIBs	Equal to regulatory capital requirements	$([2xP1]+[1xP2A])$ or 2 x LR if applicable) x scalar	$(2x[P1+P2A])$ or 2 x LR if applicable) x scalar
Other bail-in firms	Equal to regulatory capital requirements	18% RWA x scalar	$(2x[P1+P2A])$ or 2 x LR if applicable) x scalar
Partial transfer	Equal to regulatory capital requirements	18% RWA x scalar	$(2x[P1+P2A])$ or 2 x LR if applicable) x scalar*
Modified insolvency (does not have material subsidiaries or sub-groups)	Equal to regulatory capital requirements	Equal to regulatory capital requirements	Equal to regulatory capital requirements

\*Note: may be further adjustment to reflect the resolution strategy.

(a) 'Scalar' refers to the 75%–90% scaling adjustment that the Bank proposes to apply to the MREL calibration that would otherwise apply. This scalar may be 100% for groups with a simple structure.

(b) 'LR' refers to the leverage ratio requirement.

# 8 Loss-absorbing capacity for operational continuity

8.1 A banking group's operations should be set up in a way that ensures that the services necessary to support critical functions can be continued during and following resolution, in accordance with the preferred resolution strategy. For example, these services may include data processing and software development.

8.2 The Bank considers that a lack of effective arrangements to ensure operational continuity for a group is likely to constitute an impediment to resolution. The Bank is working with the PRA to ensure effective arrangements for operational continuity are put in place. In doing so, the Bank and PRA are implementing the FSB's guidance on arrangements to ensure operational continuity in resolution.<sup>(1)</sup>

8.3 Accordingly, the PRA has published rules and a supervisory statement that set out the arrangements firms should have in place to achieve operational continuity in resolution.<sup>(2)</sup> Where a critical services provider is located in the group, the PRA expects (where critical services are provided from within a business unit of a firm) the service provider to have sufficient financial resources to cover all risks, including the provider's financial resilience. Generally, financial resilience is achieved by the critical services provider being able to absorb losses and having adequate liquidity.

8.4 Under the PRA's policy, firms will:

- identify services that are critical to support functions deemed critical by the Bank, and the entities that provide those services;
- map the costs of critical services for each critical function within each provider; and
- be required to maintain liquid assets to ensure they can be provided in resolution.<sup>(3)</sup>

8.5 While the PRA's policy dealt specifically with the quantum of liquidity, it did not address the amount of loss-absorbing resources needed to support continuity in the provision of services. The Bank of England, as resolution authority, and the PRA have agreed that this loss-absorbing capacity can be satisfied as part of the gone-concern regime.

8.6 During resolution and any post-resolution restructuring, the Bank may require a group to wind down or sell off some of its businesses. Critical service providers may need to resize

their operations in line with this and may incur additional costs in doing so, for example redundancy payments. They may also incur losses as revenues decline more rapidly than costs, or for other reasons.

8.7 The Bank will require the group to ensure that each provider of critical services within the group maintains sufficient loss-absorbing resources to continue providing critical services during resolution, and after resolution.

8.8 With respect to calibration of loss-absorbing capacity for operational continuity, the Bank proposes that critical service providers supporting delivery of the group's critical functions, must maintain resources equivalent to at least 25% of the annual operating costs of providing services.<sup>(4)</sup> The Bank may determine, based on an analysis of individual circumstances, that a larger amount of resources is warranted to absorb costs and ensure continuity in critical service provision through any resolution restructuring.

8.9 Where a critical service provider is itself a UK firm subject to external or internal MREL, the Bank expects to increase the quantum of external or internal MREL that it requires the firm to maintain at all times in order to provide for loss-absorbing capacity for operational continuity. Where a critical service provider in a UK group is not itself a firm (ie it is an unregulated provider of services) the Bank expects its parent to downstream the relevant amounts to the critical service provider (in the form specified below) unless it can demonstrate that the critical service provider already has the resources in the required form. Where UK firms are part of non-UK groups and rely on critical services providers in the group that are outside the United Kingdom, the Bank will seek assurance in discussion with other authorities that appropriate arrangements are in place for loss-absorbing capacity for operational continuity.

(1) See [www.fsb.org/wp-content/uploads/Guidance-on-Arrangements-to-Support-Operational-Continuity-in-Resolution1.pdf](http://www.fsb.org/wp-content/uploads/Guidance-on-Arrangements-to-Support-Operational-Continuity-in-Resolution1.pdf)

(2) Prudential Regulation Authority (2016), 'Ensuring operational continuity in resolution', *PRA Policy Statement PS21/16*, paragraph 1.6; [www.bankofengland.co.uk/pradocuments/publications/ps/2016/ps2116.pdf](http://www.bankofengland.co.uk/pradocuments/publications/ps/2016/ps2116.pdf).

(3) *PRA Rulebook: CRR firms: operational continuity instrument 2016*, [www.bankofengland.co.uk/pradocuments/publications/ps/2016/ps2116app2.pdf](http://www.bankofengland.co.uk/pradocuments/publications/ps/2016/ps2116app2.pdf); and Prudential Regulation Authority (2016), 'Ensuring operational continuity in resolution', *PRA Supervisory Statement SS9/16*; [www.bankofengland.co.uk/pradocuments/publications/ss/2016/ss916.pdf](http://www.bankofengland.co.uk/pradocuments/publications/ss/2016/ss916.pdf).

(4) For 'annual operating costs of providing services', the Bank will use 'Total operational cost' reported for each provider of critical services under PRA operational continuity policy: column 150 of Part 1 of PRA reporting template 109, or as updated from time to time, available at [www.bankofengland.co.uk/pradocuments/crdiv/prat109template.pdf](http://www.bankofengland.co.uk/pradocuments/crdiv/prat109template.pdf).

8.10 The Bank proposes that the form of the operational continuity loss-absorbing capacity will depend on the type of entity that is providing the critical services. Where the entity is a material subsidiary that is already subject to internal MREL above capital requirements, the loss-absorbing capacity would need to meet the same eligibility criteria as would be needed to meet internal MREL. Where the entity is not subject to internal MREL above capital requirements, the loss-absorbing

capacity requirement can be satisfied by capital or by debt instruments meeting the same eligibility criteria as internal MREL eligible liabilities. If the critical services provider is an unregulated service company that is part of a sub-group of other unregulated service companies the Bank may permit the loss-absorbing capacity to be maintained at the parent entity within the service-providing group.

# 9 External MREL for banking groups with MPE resolution strategies

## External MREL for MPE resolution entities

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

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

9.3 A UK resolution entity should not double count MREL resources. Accordingly, the Bank proposes that the external MREL for a UK MPE resolution entity will be increased by the amount of any MREL investments its resolution group has made in other resolution groups in the same group.

## Group consolidated MREL for MPE groups

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

9.5 Accordingly, where the Bank is the home authority for the ultimate parent of a G-SIB, the Bank proposes that the group consolidated MREL that would apply to the relevant firm between 2019 and 2022 should reflect the TLAC standard and therefore constitute the highest of: (i) 16% of RWAs; (ii) 6% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups. From 1 January 2022 it should reflect the higher of: (i) 18% of RWAs; (ii) 6.75% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups.

# 10 Other changes to the MREL Statement of Policy

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10.1 The Bank is proposing some other changes to the text in the Statement of Policy. These are generally of a minor nature and are not intended to change the policy on external MREL. Appendix 1 shows the proposed updated Statement of Policy. Appendix 2 shows the proposed changes in the Statement of Policy relative to the version that was published in November 2016.

# Other issues regarding the Bank's policy approach to MREL

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In addition to proposals, regarding MREL within groups, this consultation contains the Bank's thinking on a number of additional areas of policy that we are developing in order to complete the Bank's approach to setting MREL.

# 11 Restrictions on firms' ability to hold each other's MREL

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11.1 Resolution is designed to ensure losses and recapitalisation needs fall on investors rather than taxpayers. Where a firm has invested in the MREL or TLAC of another firm that is resolved, the investing firm could incur losses which could cause it, too, to fail. As a bank failure may have been caused by a problem affecting other banks in the wider banking system this interdependency could lead to contagion within the financial system and make the resolution regime less effective.

11.2 The risk was identified in the FSB's TLAC standard which proposed constraints on banks holding the TLAC issued by G-SIBs. Since then the BCBS (Basel Committee on Banking Supervision) has published a TLAC holdings standard in October 2016.<sup>(1)</sup> The BCBS standard requires all internationally active banks (G-SIBs and non-G-SIBs) to deduct, from their Tier 2 capital, holdings of non-capital TLAC issued by G-SIBs, from 1 January 2019 onwards. If the investing bank owns more than 10% of its common equity, it must deduct the full investment from Tier 2. Where the

ownership is less than 10%, a bank may invest in TLAC instruments without deducting them from capital (but instead risk-weighting) up to the equivalent of 10% of the investing bank's common equity. In addition, a bank may invest a further amount up to the equivalent of 5% of its common equity in non-capital TLAC instruments subject to certain further restrictions — including for G-SIBs that such holdings are in the investing bank's trading book and are sold within 30 days of acquisition.

11.3 In the European Union, the European Commission has proposed amendments to the CRR which would introduce a narrower deductions regime for EU G-SIBs that would require them to deduct TLAC they hold from their TLAC resources. The Bank expects to clarify its policy proposals for MREL deductions once there is greater clarity as to the timing and final content of the EU proposals.

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(1) TLAC holdings standard: [www.bis.org/bcbs/publ/d387.htm](http://www.bis.org/bcbs/publ/d387.htm).

# 12 Disclosure of MREL resources by firms

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12.1 Adequate and timely disclosure of MREL resources is essential to providing greater transparency for investors on the overall loss-absorbing capacity of a firm and its distribution in a group. It should better inform investors of the risks they are assuming by investing in MREL and thereby help to realise the benefits of market discipline.

12.2 BCBS published Pillar 3 disclosure standards covering TLAC in March 2017, which apply from 1 January 2019.<sup>(1)</sup> The disclosures provide information on TLAC resources at the resolution group level. In addition, they require firms to set out creditor rankings at legal entity level, including for material sub-group entities which have issued internal TLAC to one or more resolution entities.

12.3 BCBS Pillar 3 disclosure standards provide for the disclosure of TLAC resources by G-SIBs. In the Bank's view as resolution authority, there is merit in extending the use of the

BCBS Pillar 3 TLAC disclosures to all firms in scope of MREL above capital requirements (that is those firms with a bail-in or transfer strategy). Moreover, the Bank might consider requiring further disclosures beyond those specified by Basel, for example, for G-SIBs with an MPE strategy disclosing MREL resources on a group consolidated basis for the banking group given that MREL will also apply at this level.

12.4 In the European Union, the European Commission intends to introduce MREL disclosure requirements through amendments to the CRR (for G-SIBs) and the BRRD (for other firms). The timing and scope of the amendments are uncertain. The Bank therefore expects to set out its policy on MREL disclosure once there is greater clarity on the European amendments. In the meantime, the Bank will explore the scope for voluntary disclosure by UK G-SIBs and D-SIBs in line with the BCBS Pillar 3 standard from January 2019.

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(1) Pillar 3 disclosure requirements: [www.bis.org/bcbs/publ/d400.pdf](http://www.bis.org/bcbs/publ/d400.pdf).

# 13 MREL reporting

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13.1 To enable the Bank to monitor and assess compliance with MREL, arrangements for firms to report the amounts of MREL resources they are maintaining should be in place before 2019. In the Bank's view, this can be achieved through enhancing the existing information firms submit to the PRA to facilitate resolution planning. The European Commission intends to implement reporting requirements through amendments to the CRR (for G-SIBs) and the BRRD (other firms), although it is not yet clear when these would come into effect.

13.2 The PRA intends to consult on MREL reporting in due course. In doing so, the PRA recognises the need to give firms certainty over future reporting with sufficient time to develop their regulatory reporting systems, balanced against the need for comparability with any future regulation reporting rules that might apply under the CRR and the BRRD.

# 14 Impact assessment

14.1 In December 2015, the Bank of England published an impact assessment in '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'. This impact assessment analysed the costs and benefits of MREL with respect to banking groups and the economy as a whole.

14.2 The Bank views the implementation of internal MREL and the proposals outlined in this consultation document as contributing to the benefits of the overall MREL framework, set out in the December 2015 consultation. Consequently, the Bank has updated and reproduced the key findings from the previous impact assessment in this document.<sup>(1)</sup>

14.3 Given this cost-benefit analysis captures overall costs to a group, this consultation on internal MREL does not propose to isolate further and quantify the specific costs and benefits for individual subsidiaries on a standalone basis. Such a cost analysis would have to concentrate on transfer pricing arrangements between a UK subsidiary and its parent to measure the changes in the internal borrowing cost. The Bank does not consider it feasible to estimate these costs accurately. Hence these entities are not included in the cost-benefit analysis. Instead, the Bank has considered the additional costs related to internal MREL on a qualitative basis for individual subsidiaries. The Bank considers it unlikely that these costs are material:

- The proceeds of externally issued MREL are already distributed to operating companies within groups. To qualify as internal MREL the nature and distribution of these intragroup claims may change. But the amount and cost of external MREL should not.
- The administrative costs of implementing internal MREL may vary across firms. But these should be one-off costs which are likely to fall within the scope of business-as-usual procedures for managing intragroup funding flows and could be absorbed by banking groups accordingly. Groups already have procedures in place to price, allocate and downstream external funding to subsidiaries across the group. Internal MREL policy would be making use of these existing procedures.

The analysis starts from firms' balance sheets as of end-2016 and uses financial market prices as of the past three months.

## Baseline for calculations

14.4 The analysis in this impact assessment compares the costs and benefits of the MREL framework to a counterfactual in which firms do not have to satisfy any MREs.

14.5 In 2015 the Bank published analysis of the costs and benefits of going-concern capital requirements, which informed the FPC's judgement on the medium-term capital framework. The MREL impact assessment methodology is based on the analysis on going-concern requirements and the approach taken in the December 2015 consultation.

## Estimated shortfalls and costs of MREL

14.6 The impact assessment estimates the private costs of MREL to groups subject to stabilisation powers. Indicative MREs for these firms were disclosed by the Bank in May 2017.<sup>(2)</sup>

14.7 The private cost estimates in the analysis arise from the direct funding costs of issuing particular liabilities to meet indicative end-state 2022 MREs, as per the MREL Statement of Policy. The cost estimates do not include one-off and ongoing costs for IT systems, reporting, staff, management time and other relevant costs such as potential set-up costs.

14.8 These funding costs were estimated by measuring the shortfalls between the end-state 2022 requirements and the existing eligible resources which firms maintained as of December 2016. The analysis is 'static' and does not take into account changes in institutions' assets or liabilities, or going-concern capital requirements during the period to 2022 and is based on end-state 2019 capital requirements as set out in CRR.

14.9 The 'long-term debt restructuring' in **Table A** is the shortfall between current MREL-eligible resources and 2022 requirements. The 'net shortfall' is the remaining gap to 2022 requirements if firms can convert to MREL resources their liabilities that are structurally similar to MREL resources but do not meet all of the eligibility criteria. For example, group operating companies may have long-term senior unsecured

(1) The impact analysis in the 2015 MREL consultation also considered the impact of MREL on competition. That analysis still applies and is not repeated here.

(2) Available at [www.bankofengland.co.uk/financialstability/Pages/role/risk\\_reduction/srr/mrel.aspx](http://www.bankofengland.co.uk/financialstability/Pages/role/risk_reduction/srr/mrel.aspx).

debt. If this debt were issued from a holding company, it would be structurally subordinated and MREL-eligible.

14.10 The costs were estimated as follows:

- The cost of long-term debt restructuring is based on the estimated ongoing cost of replacing current near-eligible MREL term debt with MREL-eligible term debt — in line with the FSB's approach to measuring the cost of TLAC requirements.
- The cost of closing any net shortfalls that may remain for some institutions after the restructuring of term debt is measured by issuance of new debt which results in balance sheet expansion, with proceeds of issuance invested in assets earning a yield of 1.2% (average yield on ten-year gilts over the past three months).

**Table A** Summary of MREL shortfalls and cost estimates for UK-headquartered institutions

Estimated long-term debt restructuring		Estimated net shortfall	
£ billions	Total assets (per cent)	£ billions	Total assets (per cent)
116	2.4	4	0.1

Estimated upper-bound ongoing costs	
£ billions per annum	CET1 (per cent)
0.7	0.4

14.11 Although the impact assessment excludes one-off and ongoing operational costs, the cost estimates are conservative and represent the upper end of possible ongoing costs. This is for several reasons:

- The costs are calculated on a static basis. An increase in the amount of subordinated liabilities should reduce the riskiness and hence the cost of both senior debt and existing subordinated debt. These effects are not reflected in our analysis.
- It is assumed that where institutions need to issue new liabilities to meet MREL they invest the proceeds in UK government bonds. However in reality, institutions may choose to invest in more profitable opportunities, or replace existing funding rather than expand their balance sheets, this would reduce the net cost of MREL.
- Further developments in the market for MREL-eligible debt and other similar instruments may reduce the overall cost of issuing such debt.
- Where limited data were available on institutions' cost of wholesale funding, conservative cost assumptions have been used based on the debt of institutions with the highest costs. This may overstate the funding costs for these institutions.

## Macroeconomic costs

14.12 Any increase in a firm's funding cost represents a private cost of MREL to firms. Given this is simply the result of a transfer from one party to another, it does not in and of itself constitute a social cost, and should not be included in an assessment of macroeconomic costs.

14.13 However, it is generally accepted that increases in bank funding costs impose some social costs. This is by increasing the cost of bank credit to the real economy, which may have a negative effect on investment and the level of GDP.

14.14 To estimate the macroeconomic cost of MREL, two different macroeconomic models were used that translate changes in bank lending rates into changes in GDP. The approach used is consistent with the one used in Brooke *et al* (2015),<sup>(1)</sup> that informed the Financial Policy Committee's assessment of the appropriate medium-term capital framework. To avoid making any judgements on the appropriate model, a simple average was taken of the two models used in that work.

14.15 In order to derive the increase in lending rates, it was assumed that each bank and building society increases its lending rates so as to offset its increases in funding costs in a way that leaves its return on equity unaffected.

14.16 It was assumed that for each bank, loans that will be repriced constitute 40% of its total assets. This is in line with the assumptions made in Brooke *et al* (2015) and implies that a 0.01 percentage point increase in an institution's weighted average cost of funding translates into a 0.025 percentage point increase in that institution's lending rates. Furthermore, the analysis abstracts from substitution effects between different banks and assumes that the increase in lending rates faced by a representative borrower is in line with the average increase in individual banks' lending rates (weighted using current balance sheet sizes).

14.17 Using this approach gives the result that setting MREL increases the cost of credit to a representative borrower by around 0.04 percentage points per annum. Using standard macroeconomic models, this translates into a reduction in the level of GDP by 0.02%. That is, in any given year GDP would be 0.02% lower due to MREL.

(1) Brooke, M, Bush, O, Edwards, R, Ellis, J, Francis, B, Harimohan, R, Neiss, K and Siegert, C (2015), 'Measuring the macroeconomic costs and benefits of higher UK bank capital requirements', *Bank of England Financial Stability Paper No. 35*; [www.bankofengland.co.uk/financialstability/Documents/fpc/fspapers/fs\\_paper35.pdf](http://www.bankofengland.co.uk/financialstability/Documents/fpc/fspapers/fs_paper35.pdf).

## Macroeconomic benefits

14.18 Ensuring that institutions have sufficient loss-absorbing capacity in resolution is necessary to make resolution credible without public capital support and therefore to end the 'too big to fail' problem. It can also ensure the continuity of critical functions and reduce uncertainty associated with institution failures.

14.19 While MREL is necessary to deliver a credible resolution regime, its effectiveness is predicated on other elements of a credible resolution framework being in place, such as the appropriate legal powers and safeguards, operational continuity, structural reform, and arrangements for funding in resolution. Purely for the purpose of this impact assessment, we make the simplifying assumption that all other elements of a credible resolution regime are in place and MREL is hence necessary and sufficient to deliver the benefits associated with making banks resolvable. This approach means that we attribute most if not all of the benefits of a credible resolution regime to MREL.

14.20 The estimates are based on the assumption that, without MREL, systemically important institutions would be bailed out in the case of failure.

14.21 Conceptually, there are at least two key benefits of MREL. First, MREL can affect the probability of institution failures and of any financial crises that may be triggered by such failures. By ensuring that the cost of institution failures is borne by creditors rather than public funds we ensure that creditors have stronger incentives to provide market discipline, for example by charging interest rates that reflect the underlying riskiness of an institution, or by otherwise exerting pressure on the management to curb risk-taking. This should

reduce moral hazard and provide incentives for the management of these institutions not to take excessive risks. This effect is likely to be particularly relevant for systemically important institutions that in the past would have been most likely to have been bailed out using public funds. For smaller institutions whose funding comes mostly from deposits, MREL can reduce the distortion introduced by collective deposit insurance that may reduce the risk-sensitivity of institutions' funding costs. This effect is not captured in the estimates of the benefits of MREL set out below.

14.22 Second, sufficient loss-absorbing capacity may reduce the cost of bank failures and financial crises should they nevertheless occur. Where a systemically important institution fails (that in the past might have been bailed out), the presence of MREL avoids losses being borne by the government and therefore has fiscal benefits, including increasing the scope, all else equal, for the use of a countercyclical fiscal policy. In addition, MREL can ensure more timely recapitalisations, support the continuity of critical economic functions, and avoid the uncertainty associated with bailouts or disorderly liquidations. These benefits should depend on all institutions (rather than just systemically important ones) having sufficient MREL to support an appropriate resolution strategy.

14.23 More underlying detail on the approach taken is set out in Brooke *et al* (2015) and the December 2015 MREL consultation paper. However, based on the approach outlined above, the annual gross benefits associated with MREL are likely to be within a range from 0.3% to 0.9% of annual GDP. These benefits exceed the estimated macroeconomic costs of MREL (0.02% of GDP) by a considerable margin.

# 15 Next steps

15.1 The Bank invites feedback on the proposals set out in this paper by 2 January 2018. Please provide those comments by email to the address below:

MRELfeedback@bankofengland.co.uk

Alternatively you may provide comments by post to:

Richard Williams  
Resolution Directorate  
Bank of England  
Threadneedle Street  
London  
EC2R 8AH

15.2 Respondents may wish to respond by answering the following questions.

- (1) Do you agree with the proposed approach to determining the entities within scope of internal MREL?
- (2) Do you agree with the proposed approach to calibrating internal MREL and the factors that will be considered?
- (3) What challenges do you see with the proposed policy that surplus MREL should be readily available to be deployed to material subsidiaries? Do you agree that this could be achieved through maintaining a central reserve of high-quality liquid assets at the resolution entity? Are there other methods that you think should be acceptable?
- (4) Do you agree that firms should not be able to double count resources to meet internal MREL for both their individual balance sheets and those of their subsidiaries?
- (5) Do you agree that instruments eligible for internal MREL should be subject to a contractual trigger?
- (6) Do you agree with the proposed approach to the loss-absorbing capacity for operational continuity in resolution?
- (7) Are there any tax and accounting implications that we should be aware of in setting our internal MREL policy?
- (8) What other implications does internal MREL have for the operation of banking groups that the Bank should be aware of?
- (9) Do you agree with the Bank's proposed policy for setting consolidated MREL for UK multiple point of entry groups?
- (10) Do you agree with the Bank's impact assessment of MREL?
- (11) Do you have any comments on the Bank's thinking on the treatment of cross-bank MREL holdings and MREL disclosure?
- (12) Are there any other comments which you would like to make which are relevant to this consultation and which you think the Bank should be aware of?

# Appendix 1: Proposed updated 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<sup>(1)</sup> authorised for the purpose of the Financial Services and Markets Act 2000 (FSMA) by the Prudential Regulation Authority (PRA) or Financial Conduct Authority (FCA);<sup>(2)</sup>
- (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<sup>(3)</sup> authorised by the PRA or FCA; and (ii) is established in, or formed under the law of any part of, the United Kingdom.

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

1.4 MREL must be set in line with the provisions of the No. 2 Order, the Bank Recovery and Resolution Directive (BRRD) and the 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 the Capital Requirements Directive 2013/36/EU (CRD4) or the Markets in Financial Instruments Directive 2014/65/EU (MiFID2) and to sustain sufficient market confidence in the institution or entity;
- (c) the need to ensure that, if the resolution plan anticipates that certain classes of eligible liabilities might be excluded from bail-in under article 44(3) of the BRRD or that certain classes of eligible liabilities might be transferred to a recipient in full under a partial transfer, the institution has sufficient other eligible liabilities to ensure that losses could be absorbed and the common equity Tier 1 ratio of the institution could be restored to a level necessary to enable it to continue to comply with the conditions for authorisation and to continue to carry out the activities for which it is authorised under CRD4 or MiFID2;
- (d) the size, the business model, the funding model and the risk profile of the institution;
- (e) the extent to which the Deposit Guarantee Scheme could contribute to the financing of resolution in accordance with article 109 of the BRRD;
- (f) the extent to which the failure of the institution would have adverse effects on financial stability, including due to its interconnectedness with other institutions or with the

(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.

rest of the financial system, through contagion to other institutions.

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

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

### Interaction of MREL and the capital framework

1.8 The PRA has published a supervisory statement on the interaction of MREL and the capital framework.<sup>(1)</sup> 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.

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

## 2 Definitions and interpretation

2.1 'Own funds' have the same meaning as in article 4(1)(118) of Regulation 575/2013/EU (CRR).

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

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

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

2.5 External MREL instruments are issued from a 'resolution entity' in a group, that is to say, the entity that would be subject to the use of resolution powers under the preferred resolution strategy.

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

2.7 In developing the preferred resolution strategies, the Bank will identify the institution within the group (if any) to which the Bank would expect to apply its resolution powers and which would therefore be the UK resolution entity<sup>(2)</sup> for which 'external MREL' is set.

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

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

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

## 3 Framework for setting MREL

3.1 This section sets out the framework the Bank uses to inform the calibration of an institution's MREL. Section 4 describes additional adjustments which may be made on the basis of the preferred resolution strategy for an institution, Section 5 describes additional criteria which liabilities must meet in order to qualify as external MREL resources, Section 6 sets out the Bank's principles for setting MRELS within groups, Section 7 describes internal MREL scope and calibration, Section 8 sets out internal MREL instrument eligibility, Section 9 covers loss-absorbing capacity for operational continuity, and Section 10 sets out the Bank's approach to the transition to final (end-state) MRELS, including interim requirements.

3.2 The Bank will communicate to institutions or their parent companies annually their resolution strategies, the critical

(1) PRA (2016), 'The minimum requirement for own funds and eligible liabilities (MREL) — buffers and Threshold Conditions', *Supervisory Statement SS16/16*, available at [www.bankofengland.co.uk/pr/Pages/publications/ss/2016/ss1616.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ss/2016/ss1616.aspx). The PRA has consulted on updating *Supervisory Statement SS16/16* to clarify that the expectations set out in *SS16/16* are not intended to create a different buffer requirement from that which is usable in the going-concern regime, available at [www.bankofengland.co.uk/pr/Documents/publications/cp/2017/cp1517.pdf](http://www.bankofengland.co.uk/pr/Documents/publications/cp/2017/cp1517.pdf).

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

functions<sup>(1)</sup> (if any) that they or their group provide, and their external and internal MREL (if any).<sup>(2)</sup>

3.3 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 CRD4<sup>(3)</sup> capital requirements (Pillar 1, Pillar 2A and capital buffer requirements), any applicable leverage ratio, and, should it continue to apply after 31 December 2017, the Basel I floor, as reference points.

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

### Loss absorption amount

3.5 The Bank will set the loss absorption amount to cover the losses that would need to be absorbed up to and in resolution. The starting point in the MREL RTS is that the loss absorption amount will equal an institution's 'capital requirements'<sup>(4)</sup> (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).<sup>(5)</sup>

3.6 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.

3.7 In light of the PRA policy on the interaction of MREL and capital buffers, in particular that CET1 cannot be used simultaneously to meet both MREL and capital buffers, the Bank expects to exclude buffers from the loss absorption amount for institutions subject to that policy. This includes those institutions with a modified insolvency resolution strategy, including those for which the FCA is the sole competent authority. Therefore the Bank expects generally to set the loss absorption amount equal to an institution's regulatory capital requirements.<sup>(6)</sup>

## 4 Resolution strategies and external MREL

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

4.2 It is important to note that the actual approach taken to resolve an institution will depend on the circumstances at the

time of its failure. The preferred resolution strategy may not necessarily be followed if a different approach would better meet the resolution objectives at the time.

### Modified insolvency

4.3 The Banking Act provides for a number of modified insolvency regimes for certain institutions (the bank insolvency procedure (BIP), building society insolvency procedure (BSIP) and the special administration regime (SAR)).<sup>(7)</sup> 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 external MREL to zero. This would mean that an institution's external MREL would be set at a level equal to its capital requirements excluding buffers (Pillar 1 plus Pillar 2A or, if higher, any applicable leverage ratio 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;
- (b) if the institution does not provide significant amounts of transactional banking services or other critical functions, particularly those which depend on continuous access to a service which would not be provided in a modified insolvency. The Bank considers that provision of fewer than around 40,000 to 80,000 transactional bank accounts (accounts from which withdrawals have been made nine or more times within a three-month period) is generally likely to indicate that a modified insolvency would be appropriate.

(1) See section 3(1) of the Banking Act and PRA (2013), 'Resolution planning', *Supervisory Statement SS19/13*; [www.bankofengland.co.uk/pradocuments/publications/policy/2013/resolutionplanning1913.pdf](http://www.bankofengland.co.uk/pradocuments/publications/policy/2013/resolutionplanning1913.pdf).

(2) For institutions which form part of a group for which the Bank is not the EU group-level resolution authority, the institution will receive the communication via the relevant EU group-level resolution authority.

(3) Capital Requirements Directive (2013/36/EU) (CRD) and Capital Requirements Regulation (575/2013) (CRR) — jointly 'CRD4'.

(4) 'Capital requirements' means the higher of (1) the amount and quality of own funds the appropriate regulator (PRA or FCA) thinks the firm should hold at all times under the overall financial adequacy rule (for PRA-authorized persons Internal Capital Adequacy Assessment 2.1 PRA Rulebook and for FCA-authorized persons IFPRU 2.2.1R of the FCA Handbook) as it applies on a solo or a consolidated level; (2) (if applicable) minimum leverage ratio in Leverage Ratio 3.1 of the PRA Rulebook; and (3) (if applicable) the Basel I floor.

(5) Please see the PRA Policy Statement on Pillar 2 for further details: [www.bankofengland.co.uk/pradocuments/publications/ps/2015/ps1715.aspx](http://www.bankofengland.co.uk/pradocuments/publications/ps/2015/ps1715.aspx).

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

(7) 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.

## Partial transfer

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

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

- (a) if the institution's business and asset/liability structure are sufficiently simple so as to make rapidly separating and transferring critical functions feasible using the Bank's statutory powers;
- (b) if the institution's systems are able to provide the necessary information to support a transfer within the required timeframe;
- (c) if some or all of the institution's business, assets and liabilities (particularly those associated with critical functions) are reasonably likely to be attractive to a private sector purchaser; and
- (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 external MREL will be set taking this into account. The Bank expects to consider the following principal adjustments to external MREL for such institutions relative to that set to enable a bail-in strategy for institutions that are D-SIBs:

- (a) **Quantum:** the recapitalisation component of external MREL might be reduced to reflect the fact that less than the entire balance sheet of the institution will need to be recapitalised at the point of resolution. For example, to the extent that an institution's critical liabilities<sup>(1)</sup> represented only a proportion of its total liabilities, the recapitalisation component of external MREL may be reduced to reflect this. The Bank will also consider whether any components of Pillar 2A will cease to be relevant as a result of the transfer.
- (b) **Subordination:** where a transfer resolution strategy assumes that only liabilities benefitting from preference in insolvency<sup>(2)</sup> will be transferred, the Bank may not require

MREL resources to be subordinated to senior operating liabilities. This is because the transfer can allow all non-transferred liabilities to receive *pari passu* treatment in a bank administration procedure. This reduces the risk of breaches of the 'no creditor worse off than insolvency' (NCWO) safeguard which might occur if the bail-in stabilisation power had been applied but exclusions were made for certain senior liabilities.

## Bail-in

4.9 The stabilisation power that is most likely to be appropriate for large complex institutions and groups is bail-in. The Bank is likely to make use of a bail-in strategy for institutions and groups 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 UK resolution entities subject to a bail-in strategy to ensure that their MREL resources are subordinated to operating liabilities, using structural subordination except in the case of building societies which may use contractual subordination. Subordination of MREL resources reduces the risk of breaches of the NCWO safeguard in the event of a bail-in. Further detail is provided in Section 6.

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

- a. G-SIBs<sup>(3)</sup> will be required to meet an external MREL equivalent to the higher of:
  - i. two times the sum of Pillar 1 and Pillar 2A, ie  $2 \times (\text{Pillar 1 plus Pillar 2A})$ ;<sup>(4)</sup> 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).<sup>(5)</sup>
- b. D-SIBs<sup>(6)</sup> and any other UK bail-in resolution entities will be required to meet an external MREL equivalent to the higher of:

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(1) Those liabilities necessary for the continuity of a critical function.  
 (2) 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.  
 (3) Global systemically important banks (G-SIBs) as identified by the Financial Stability Board in consultation with the Board Committee on banking supervision and national authorities.  
 (4) Or, if higher and to the extent it applies after 31 December 2017, the Basel I floor.  
 (5) The Bank does not expect that setting a level below the internationally agreed minimum for G-SIBs would be sufficient to ensure market confidence.  
 (6) Domestic systemically important banks (D-SIBs) are those institutions that are subject to the PRA leverage ratio requirement (ie with retail deposits over £50 billion) and/or any institutions that are designated as an O-SII (other systemically important institution) by the PRA pursuant to article 131(3) of the Capital Requirements Directive (2013/36/EU), and which have a resolution entity in the United Kingdom.

- i. two times the sum of Pillar 1 and Pillar 2A, ie  $2 \times (\text{Pillar 1} + \text{Pillar 2A})$ ;<sup>(1)</sup> or
- ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6.5% if the leverage ratio is 3.25%).

## 5 External MREL instrument eligibility

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

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

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

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

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

5.6 The Bank does not consider liabilities the value of which is dependent on derivatives to be appropriate to qualify as MREL eligible liabilities. The Bank does not consider liabilities which

only include put or call options to be dependent on derivatives for this purpose.

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

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

5.9 The Bank's view is that the failure to meet the eligibility criteria, as described above, in both non-CET1 own funds instruments and MREL eligible liabilities is likely to constitute an impediment to successful resolution, as the resolution authority must have certainty as to the quantum of loss-absorbing capacity that will be available should the institution find itself in stress. The Bank therefore expects institutions to ensure that non-CET1 own funds instruments and MREL eligible liabilities comply with the eligibility criteria set out above.

5.10 The Bank's view is that external issuance of MREL from subsidiaries in both own funds instruments and MREL eligible liabilities is likely to constitute an impediment to successful resolution. In line with this, externally issued regulatory capital in subsidiaries of a resolution entity may be used to meet that resolution entity's MREL to the extent that such capital qualifies as regulatory capital at the group consolidated level until the current end-state MREL date of 1 January 2022. After that point, only externally issued CET1 issued by such subsidiaries should be used to meet a resolution entity's external MREL and only then if the external issuance of CET1 is required by local regulations.

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

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

## 6 MREL in the context of groups

6.1 The Bank will set an external MREL at the group consolidated level.

6.2 The Bank will require groups or institutions in respect of which bail-in is the preferred resolution strategy to structure

(1) Or, if higher and to the extent it applies after 31 December 2017, the Basel I floor.

(2) See in particular section 123(4).

(3) See [www.prulebook.co.uk/rulebook/Content/Part/211722/26-10-2016](http://www.prulebook.co.uk/rulebook/Content/Part/211722/26-10-2016) and [www.handbook.fca.org.uk/handbook/IFPRU/11/6.html?date=2016-06-30](http://www.handbook.fca.org.uk/handbook/IFPRU/11/6.html?date=2016-06-30).

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 MREs.

6.3 For institutions subject to structural subordination, MREL resources issued externally by resolution entities should not rank *pari passu* with significant amounts of other liabilities that do not meet the MREL eligibility criteria set out in the No. 2 Order. 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.

### Availability of surplus MREL in groups

6.4 Resolution entities will be required to issue external MREL resources at least equal to all the internal MREL resources or, in other jurisdictions, equivalent subordinated instruments that can absorb losses and recapitalise a subsidiary, such as through being written down and/or converted to equity, without the use of stabilisation or resolution powers at the subsidiary level ('internal loss-absorbing resources') that are to be issued to them from their subsidiaries. For groups with UK resolution entities, the Bank expects that any 'surplus MREL' — the difference in requirements between external MREL and the sum of what must be issued to the resolution entity as internal loss-absorbing resources — should be readily available to recapitalise any direct or indirect subsidiary as necessary to support the execution of the resolution strategy and there should be no legal or operational barriers to this. For example, the surplus MREL could be used to invest in high-quality liquid assets which would be maintained at the UK resolution entity.<sup>(1)</sup> This would constitute a 'central reserve' of MREL which could be made available to material subsidiaries as needed, on the agreement of home and host authorities.

### External MREL for MPE resolution entities

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

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

6.7 A UK resolution entity should not double count MREL resources. Accordingly, the external MREL for a UK MPE resolution entity will be increased by the amount of any MREL or equivalent investments its resolution group has made in other resolution groups in the same group.

### Group consolidated MREL for MPE groups

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

6.9 Accordingly, where the Bank is the home authority for the ultimate parent of a G-SIB, the Bank proposes that the group consolidated MREL that would apply to the relevant institution between 2019 and 2022 should reflect the TLAC standard and therefore constitute the highest of: (i) 16% of RWAs; (ii) 6% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups. From 1 January 2022 it should reflect the higher of: (i) 18% of RWAs; (ii) 6.75% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups.

## 7 Internal MREL

### Scope

7.1 Internal MREL above capital requirements is likely to be necessary only where it is considered that insolvency of the institution would put the Bank's resolution objectives at risk.<sup>(2)</sup> The Bank expects to set internal MREL above capital requirements for a 'material subsidiary' of a group where either (a) there is a UK resolution entity in the same group

(1) High-quality liquid assets as defined in Part Six (Liquidity) of CRR and the European Commission Delegated Act with regards to the liquidity coverage requirement (LCR) for credit institutions.

(2) For example, paragraph 4.4 above provides an indicative threshold that institutions with below 40,000–80,000 transactional accounts would have a modified insolvency resolution strategy.

which is or will become subject to an external MREL above its capital requirements or (b), in the case of UK subsidiaries of overseas groups, the subsidiary delivers critical functions in the United Kingdom.<sup>(1)</sup>

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

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

- a. has more than 5% of the consolidated risk-weighted assets of the group; or
- b. generates more than 5% of the total operating income of the group; or
- c. has a total leverage exposure measure larger than 5% of the group's consolidated leverage exposure measure; or
- d. exceptionally, is otherwise 'material', either directly or through its subsidiaries, to the delivery of a group's critical functions. The Bank will continue to review groups' structures and critical functions to judge if this criterion applies to any entities.

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

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

## Calibration

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

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

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

7.8 These factors allow the Bank to set internal MREL based on discussion with other authorities in crisis management groups — as envisaged in the TLAC standard, and resolution colleges — as required by BRRD.

7.9 The largest banking groups in the United Kingdom are subject to legislation<sup>(2)</sup> which will require them to carry out their core UK financial services and activities within a ring-fenced body (RFB) and separate these from certain other activities of the wider group. Where an RFB is part of a material sub-group (see paragraph 7.4), the Bank expects to scale the internal MREL for the top entity of the material sub-group at 90%, as a starting point, unless the Bank is satisfied that the wider group has sufficient readily-deployable resources to justify moving to a lower calibration in the 75% to 90% range.<sup>(3)</sup> This approach is intended to ensure that the setting of internal MREL for RFBs is in line with the range set out in the FSB's international standard while minimising the RFB's dependence on the rest of the group, consistent with the PRA's ring-fencing objectives. The Bank is committed to

(1) See section 3(1) of the Banking Act and PRA (2013), 'Resolution planning', *Supervisory Statement SS19/13*; [www.bankofengland.co.uk/prd/Documents/publications/policy/2013/resolutionplanning1913.pdf](http://www.bankofengland.co.uk/prd/Documents/publications/policy/2013/resolutionplanning1913.pdf).

(2) The Financial Services and Markets Act 2000, as amended by the Financial Services (Banking Reform) Act 2013.

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

working with overseas resolution authorities to build confidence in each other's resolution regimes. This should help contribute towards the ability to make reductions over time in the internal MREL in material sub-groups that contain an RFB.

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

7.11 For UK groups with a simple structure — for example, a single material subsidiary that sits below a UK resolution entity with few, if any other, subsidiaries — the Bank would not expect to adjust downwards the internal MREL for that UK material subsidiary. This means the internal MREL would be set at 100% of the external MREL that would have applied to the material subsidiary if it were a resolution entity. The Bank would also apply this approach also for the top entity of material sub-groups containing an RFB or for an RFB which is not part of a material sub-group if the RFB's group has a simple structure. The Bank's approach to not applying scaling would be judgement-based, and decided on a case-by-case basis, giving due consideration to the relationship between the risk profile of a material subsidiary and its wider group.

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

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

7.14 A subsidiary or sub-group should only count the internal MREL resources that it issues towards meeting its own internal MREL. Where an institution has subsidiaries that also have internal MREL or equivalent resources, it should ensure that it has sufficient internal MREL to match both its own individual MREL as well as the internal MREL or equivalent resources of its subsidiaries. In order to achieve this, the Bank expects that internal MREL for an institution will be increased by the amount of any internal MREL or equivalent (or loss-absorbing capacity for operational continuity) investments it has made in other entities in the same group.

## 8 Internal MREL instrument eligibility

8.1 All the eligibility criteria set out in paragraphs 5.2–5.8 that apply to external MREL resources apply equally to internal MREL eligible liabilities.

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

- (1) subordination;
- (2) the holder of the instrument;
- (3) contractual triggers; and
- (4) mismatching of internal and external MREL.

### Subordination

8.3 As in the case of eligibility for external MREL liabilities, internal MREL resources must be subordinated to the operating liabilities of the group entities issuing them. This is necessary to ensure that, in converting internal MREL, the Bank is not required to bail in other liabilities that might rank *pari passu* and which may either be difficult to bail in or would result in a change of ownership of the entity if converted into equity. Internal MREL eligible liabilities will need to be contractually or statutorily subordinated. However, if the entity is a holding company, it may be permitted to issue internal MREL instruments as senior liabilities provided that the sum of its liabilities that do not meet the other internal MREL eligibility criteria (excluding liabilities that previously met the internal MREL eligibility criteria but no longer meet the minimum maturity requirement referred to in paragraph 5.2 above) do not exceed 5% of the entity's overall internal MREL resources (see Section 6).

### The holder of the instrument

8.4 Institutions and groups should ensure that the issuance of internal MREL by a material subsidiary or sub-group credibly supports the resolution strategy and the passing of losses and recapitalisation needs to the resolution entity. Internal MREL eligible liabilities must be issued either directly or indirectly via other entities in the same resolution group to the parent resolution entity. The Bank generally expects to accept issuance indirectly to the resolution entity along the chain of ownership, as long as there are no technical obstacles to the resolution entity becoming exposed to losses through this chain. Direct issuance could also be acceptable unless there are circumstances in which converting internal MREL to equity could result in a change of control that could be an impediment to resolution — for example if there were significant governance or tax issues as a result.

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

8.6 The Bank's view is that external issuance of MREL from non-resolution entity subsidiaries in both own funds instruments and eligible liabilities is also likely to constitute an impediment to resolution. In line with this, externally issued regulatory capital in subsidiaries of a resolution entity may be used to meet internal MREL to the extent that such capital qualifies as regulatory capital until the current end-state MREL date of 1 January 2022. After that point, only externally issued CET1 issued by such subsidiaries should be used to meet a subsidiary's internal MREL and only then if the externally issued CET1 is required by local regulations.

### Contractual triggers

8.7 Internal MREL resources must be capable of being written down or converted to equity without or ahead of any use of resolution powers in relation to the entity which issues them.

8.8 As a general matter, the trigger for an internal MREL instrument will need to provide the resolution authority of the material subsidiary with the right to exercise a write-down or conversion where:

- the resolution authority determines that the institution is failing or likely to fail and will, disregarding any write-down and/or conversion of the instruments, continue to be so; and for internal MREL for subsidiaries of non-UK groups, the home resolution authority consents or does not object to the write-down or conversion following 24 hours' notice; or
- a resolution entity in the group, which is a direct or indirect parent of the institution, is subject to resolution proceedings in the United Kingdom or elsewhere.<sup>(1)</sup>

8.9 The Bank's view is that the absence of contractual triggers in both non-CET1 own funds instruments and MREL eligible liabilities is likely to constitute an impediment to resolution on the grounds that: (1) the joint home-host trigger envisaged by the contractual trigger provides the mechanism for the home and host authorities to agree whether additional resources are required by the relevant subsidiary in addition to the capital provided by the conversion of the internal MREL and; (2) the ability to trigger all internal MREL simultaneously provides assurance that all relevant subsidiaries are well-capitalised and ensures that the surplus resources are available to the subsidiaries (if any) that require additional resources. The Bank therefore expects institutions to include those terms in any internal MREL resources (including non-CET1 own funds).

8.10 The particular features of the contractual terms of an institution's internal MREL may depend on the group's or institution's resolution strategy and may require discussion between the group and the Bank. Having confirmed these features, the responsibility for ensuring that instruments, including own funds instruments, are MREL eligible rests with the institution. Institutions should obtain independent legal

advice on a liability's eligibility (including on whether relevant own funds instruments contain the additional contractual provisions referred to above), and provide this to the Bank where required. Institutions are expected to notify the Bank where they do not intend to include the additional contractual provisions in own funds instruments. In line with the continuous resolvability assessment process, institutions will also be expected to demonstrate compliance with the eligibility criteria on request.

### Mismatching of internal and external MREL

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

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

## 9 Loss-absorbing capacity for operational continuity

9.1 The Bank will require institutions within the group to ensure that each provider of critical services within the group maintains sufficient loss-absorbing resources to continue providing critical services during resolution, and after resolution.

9.2 With respect to calibration of loss-absorbing capacity for operational continuity, the Bank proposes that critical service providers supporting the delivery of the group's critical functions must maintain resources equivalent to at least 25% of the annual operating costs of providing services.<sup>(2)</sup> The Bank may determine, based on an analysis of individual circumstances, that a larger amount of resources is warranted

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

(2) For 'annual operating costs of providing services', the Bank will use 'Total operational cost' reported for each provider of critical services under PRA operational continuity policy: column 150 of Part 1 of PRA reporting template 109, or as updated from time to time, available at [www.bankofengland.co.uk/pradocuments/crdiv/prat109template.pdf](http://www.bankofengland.co.uk/pradocuments/crdiv/prat109template.pdf).

to absorb costs and losses and ensure continuity in critical service provision through any resolution restructuring.

9.3 Where a critical service provider is itself an institution subject to external or internal MREL, the Bank expects to increase the quantum of external or internal MREL that it requires the institution to maintain at all times in order to provide for loss-absorbing capacity for operational continuity. Where a critical service provider in a UK group is not itself an institution (ie it is an unregulated provider of services) the Bank expects its parent to downstream the relevant amounts to the critical service provider (in the form specified below) unless it can demonstrate that the critical service provider already has the resources in the required form. Where institutions are part of non-UK groups and rely on critical services providers in the group that are outside the United Kingdom, the Bank will seek assurance in discussion with other authorities that appropriate arrangements are in place for loss-absorbing capacity for operational continuity.

9.4 The Bank proposes that the form of the operational continuity loss-absorbing capacity will depend on the type of entity that is providing the critical services. Where the entity is a material subsidiary that is already subject to internal MREL above capital requirements, the loss-absorbing capacity would need to meet the same eligibility criteria as would be needed to meet internal MREL. Where the entity is not subject to internal MREL above capital requirements, the loss-absorbing capacity requirement can be satisfied by capital or by debt instruments meeting the same eligibility criteria as internal MREL eligible liabilities. If the critical services provider is an unregulated service company that is part of a sub-group of other unregulated service companies the Bank may permit the loss-absorbing capacity to be maintained at the parent entity within the service-providing group.

## 10 Transitional arrangements

### General transitional arrangements

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

10.2 To allow institutions flexibility over timing of changes to their liability structures in order to meet MREL, generally the Bank does not expect to direct institutions to maintain MREL greater than its regulatory capital requirements prior to the dates set out in paragraph 10.4 below. The Bank has however provided UK resolution entities (on a bilateral basis) with an indication of the external MREL that is likely to apply at the consolidated level at the end of the relevant transitional period (in the first instance the interim MRELS). The Bank also proposes to provide institutions with an indication of the internal MREL that is likely to apply at the end of the relevant

transitional. 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.

10.3 The Bank currently expects to direct institutions to comply with an end-state external MREL (calculated in accordance with the methodology described in Section 3 and 4 above) and internal MREL (calculated in accordance with the methodology described in Section 7 above) from 1 January 2022.

10.4 Notwithstanding 10.3 above, to ensure that institutions make progress towards meeting their end-state requirements the Bank expects to direct institutions to meet the following interim MRELS and internal MRELS:

- (a) From 1 January 2019 UK resolution entities that are G-SIBs will be required to meet the minimum requirements set out in the 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. At the same time, material subsidiaries of G-SIBs that are incorporated in the United Kingdom will need to meet these minimum requirements multiplied by an institution-specific scalar that is determined by the Bank.<sup>(1)</sup> In addition, the Bank expects institutions in G-SIB groups to comply with any additional requirement in respect of loss-absorbing capacity for operational continuity (as described in Section 9 above) from this date.
- (b) From 1 January 2020:
  - a. UK resolution entities that are G-SIBs or D-SIBs will be required to maintain MREL equal to the higher of:
    - i. two times their Pillar 1 capital requirements and one times their Pillar 2A add-ons, ie  $(2 \times \text{Pillar 1}) + (1 \times \text{Pillar 2A})$ ;<sup>(2)</sup> or
    - ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6.5% if the leverage ratio requirement is 3.25%). G-SIBs in any case must meet at least 6% of leverage exposures.

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

(1) 'Scalar' refers to the 75%–90% scaling adjustment that the Bank expects to apply to the MREL calibration that would otherwise apply. This scalar may be 100% for groups with a simple structure.

(2) Or, if higher and to the extent it applies after 31 December 2017, the Basel I floor.

expects institutions in D-SIB groups to comply with any additional requirement in respect of loss-absorbing capacity for operational continuity (as described in Section 9 above) from this date.

- b. UK resolution entities which are not G-SIBs or D-SIBs will be required to maintain MREL equal to 18% of risk-weighted assets. At the same time, material subsidiaries of these institutions that are incorporated in the United Kingdom will need to meet this minimum requirement multiplied by an institution-specific scalar that is determined by the Bank. In addition, the Bank expects the institutions to comply with any additional requirement in respect of loss-absorbing capacity for operational continuity (as described in Section 9 above) from this date.

10.5 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.

10.6 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 apply with respect to both interim and end-state MRELS. Please consult chapter 4 of the PRA supervisory statement for further details.

### **Institution-specific transitional arrangements**

10.7 The Bank may on an institution-specific basis set an earlier compliance date during the transition period for interim

(external and internal) MRELS and/or end-state MRELS greater than regulatory capital requirements, for example where the Bank has concerns about the resolvability of a group or institution, or to implement international standards.

10.8 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 external and/or internal MREL applicable to an institution which has been resolved as necessary, such that the institution would not be in breach of MREL immediately following resolution.

10.9 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 for external MREL where the change in MREL is material. The Bank would expect to determine similar transitional arrangements for a group's internal MREL as for its external MREL. However, where groups are already subject to external MREL in excess of capital requirements, the Bank will determine the appropriate transitional period to meet internal MREL on an institution-specific basis for any subsidiaries that are newly designated as material.

## Appendix 2: Proposed changes to the Statement of Policy on the Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL)<sup>(1)</sup>

### 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<sup>(2)</sup> authorised for the purpose of the Financial Services and Markets Act 2000 (FSMA) by the Prudential Regulation Authority (PRA) or Financial Conduct Authority (FCA);<sup>(3)</sup>
- (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<sup>(4)</sup> 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 730k 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. References in this Statement of Policy to a 'group' means any group comprising one or more entities referred to in 1.2 above, whether established and authorised in the United Kingdom or elsewhere.

1.4 MREL must be set in line with the provisions of the No. 2 Order, the Bank Recovery and Resolution Directive (BRRD) and the 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 the Capital Requirements Directive 2013/36/EU (CRD4) or the Markets in Financial Instruments Directive 2014/65/EU (MiFID2) and to sustain sufficient market confidence in the institution or entity;
- (c) the need to ensure that, if the resolution plan anticipates that certain classes of eligible liabilities might be excluded from bail-in under 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 common equity Tier 1 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; CRD4 or MiFID2;
- (d) the size, the business model, the funding model and the risk profile of the institution;

(1) Changes in red show proposed additions (underlined) or deletions (struck through) relative to the Statement of Policy that was published in November 2016.

(2) 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'.

(3) 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.

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

- (e) the extent to which the Deposit Guarantee Scheme could contribute to the financing of resolution in accordance with article 109 of the BRRD;
- (f) the extent to which the failure of the institution would have adverse effects on financial stability, including due to its interconnectedness with other institutions or with the rest of the financial system, through contagion to other institutions.

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

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

## **2 Statutory interaction of MREL and the capital framework**

**2.1** 1.8 The PRA has published a **concurrent** supervisory statement on the interaction of MREL and the capital framework.<sup>(1)</sup> 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** 1.9 Please consult the PRA's supervisory statement for further details.

## **2 Definitions and interpretation**

2.1 'Own funds' have the same meaning as in article 4(1)(118) of Regulation 575/2013/EU (CRR).

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

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

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

2.5 External MREL instruments are issued from a 'resolution entity' in a group, that is to say, the entity that would be subject to the use of resolution powers under the preferred resolution strategy.

2.6 Internal MREL instruments are issued from legal entities in a group that are not themselves resolution entities. They are issued directly or indirectly to the resolution entity in their group. References to resources that are 'equivalent' to internal MREL mean subordinated instruments in other jurisdictions that can absorb losses and recapitalise a subsidiary, such as through being written down and/or converted to equity, without the use of resolution tools at the subsidiary level.

2.7 In developing the preferred resolution strategies, the Bank will identify the institution within the group (if any) to which the Bank would expect to apply its resolution powers and which would therefore be the UK resolution entity<sup>(2)</sup> for which 'external MREL' is set.

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

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

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

(1) Capital Requirements Directive (2013/36/EU) (CRD) and Capital Requirements Regulation (575/2013) (CRR) — jointly 'CRD-IV'; PRA (2016), 'The minimum requirement for own funds and eligible liabilities (MREL) — buffers and Threshold Conditions', PRA Supervisory Statement 16/16, available at [www.bankofengland.co.uk/pr/Pages/publications/ss/2016/ss1616.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ss/2016/ss1616.aspx). The PRA has consulted on updating Supervisory Statement 16/16 to clarify that the expectations set out in SS16/16 are not intended to create a different buffer requirement from that which is usable in the going-concern regime, available at [www.bankofengland.co.uk/pr/Documents/publications/cp/2017/cp1517.pdf](http://www.bankofengland.co.uk/pr/Documents/publications/cp/2017/cp1517.pdf).

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

### 3 Framework for setting MREL

3.1 This section sets out the framework the Bank uses to inform the calibration of an institution's MREL. Section 4 describes additional adjustments which may be made on the basis of the preferred resolution strategy for an institution, Section 5 describes additional criteria which liabilities must meet in order to qualify as **external** MREL resources, Section 6 sets out the Bank's principles for setting MREs within groups and, Section 7 [describes internal MREL scope and calibration](#), [Section 8 sets out internal MREL instrument eligibility](#), [Section 9 covers loss-absorbing capacity for operational continuity](#), and [Section 10](#) sets out the Bank's approach to the transition to final (end-state) MREs, including interim requirements.

[3.2 The Bank will communicate to institutions or their parent companies annually their resolution strategies, the critical functions<sup>\(1\)</sup> \(if any\) that they or their group provide, and their external and internal MREL \(if any\).](#)<sup>(2)</sup>

[3.3](#) 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/CRD4**<sup>(3)</sup> capital requirements (Pillar 1, Pillar 2A and capital buffer requirements), any applicable leverage ratio, and, [should it continue to apply after 31 December 2017](#), the Basel I floor, as reference points.

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

#### Loss absorption amount

[3.5](#) The Bank will set the loss absorption amount to cover the losses that would need to be absorbed up to and in resolution. The starting point in the MREL RTS is that the loss absorption amount will equal an institution's **regulatory capital requirements**<sup>(4)</sup> (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).<sup>(5)</sup>

[3.6](#) 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.

[3.7](#) In light of the PRA policy on the interaction of MREL and capital buffers, in particular that CET1 cannot be used simultaneously to meet both MREL and capital buffers, the

Bank expects to exclude buffers from the loss absorption amount for institutions subject to that policy. This includes those institutions with a modified insolvency resolution strategy, including those for which the FCA is the sole competent authority. Therefore the Bank expects generally to set the loss absorption amount equal to an institution's regulatory capital requirements.<sup>(6)</sup>

### 4 Resolution strategies and **external** MREL

4.1 MREL will be set to ensure that institutions can be resolved in line with the resolution objectives, [in Section 4 of the Banking Act](#). In particular MREL will be set to enable the preferred resolution strategy for an institution to be effected. This section outlines key factors the Bank will consider when determining the preferred resolution strategy, and how this determination may affect **the any external** 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 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)).<sup>(7)</sup> 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 **external** MREL to zero. This would mean that an institution's **external** MREL would be set at a level equal to

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- (1) [See section 3\(1\) of the Banking Act and Prudential Regulation Authority \(2013\), 'Resolution planning', PRA Supervisory Statement SS19/13; www.bankofengland.co.uk/pr/Documents/publications/policy/2013/resolutionplanning1913.pdf.](#)
- (2) [For institutions which form part of a group for which the Bank is not the EU group-level resolution authority, the institution will receive the communication via the relevant EU group-level resolution authority.](#)
- (3) [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/Documents/publications/ss/2016/ss1616.aspx; Capital Requirements Directive \(2013/36/EU\) \(CRD\) and Capital Requirements Regulation \(575/2013\) \(CRR\) — jointly 'CRD 4'.](#)
- (4) 'Capital requirements' means the higher of (1) the amount and quality of own funds the appropriate regulator (PRA or FCA) thinks the firm should hold at all times under the overall financial adequacy rule (for PRA-authorised persons Internal Capital Adequacy Assessment 2.1 PRA Rulebook and for FCA-authorised persons IFPRU 2.2.1R of the FCA Handbook) as it applies on a solo or a consolidated level; (2) (if applicable) minimum leverage ratio in Leverage Ratio 3.1 of the PRA Rulebook; and (3) (if applicable) the Basel I floor.
- (5) Please see the PRA Policy Statement on Pillar 2 for further details: [www.bankofengland.co.uk/pr/Documents/publications/ps/2015/ps1715.aspx.](#)
- (6) As set out in the MREL RTS, the loss absorption amount may be adjusted in certain circumstances.
- (7) 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.

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;
- (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 9 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 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 **external** MREL might be reduced to reflect the fact that less than the entire balance sheet of the institution will need to be recapitalised at the point of resolution. For example, to the extent that an institution's critical liabilities<sup>(1)</sup> represented only a proportion of its total liabilities, the recapitalisation component of **external** MREL may be reduced to reflect this. The Bank will also consider whether any components of Pillar 2A will cease to be relevant as a result of the transfer.
- (b) **Subordination**: where a transfer resolution strategy assumes that only liabilities benefitting from preference in insolvency<sup>(2)</sup> will be transferred, the Bank may not require MREL resources to be subordinated to senior operating liabilities. This is because the transfer can allow all non-transferred liabilities to receive *pari passu* treatment in a bank administration procedure. This reduces the risk of breaches of the 'no creditor worse off than insolvency' (NCWO) safeguard which might occur if the bail-in stabilisation power had been applied but exclusions were made for certain senior liabilities.

### Bail-in

4.9 The stabilisation power that is most likely to be appropriate for large complex institutions **and groups** is bail-in. The Bank is likely to make use of a bail-in strategy for institutions **and groups** 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 **institutionsUK resolution entities** subject to a bail-in strategy to ensure that their MREL resources are subordinated to operating liabilities, using structural subordination except in the case of building

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

(2) 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.

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. [Further detail is provided in Section 6.](#)

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

- a. G-SIBs [with a resolution entity in the United Kingdom](#)<sup>(1)</sup> will be required to meet an MREL equivalent to the higher of:
  - i. two times the sum of Pillar 1 and Pillar 2A, ie 2x(Pillar 1 plus Pillar 2A);<sup>(2)</sup> 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).<sup>(3)</sup>
- b. D-SIBs<sup>(4)</sup> and any other [UK bail-in institutions resolution entities](#) will be required to meet an MREL equivalent to the higher of:
  - i. two times the sum of Pillar 1 and Pillar 2A, ie 2x(Pillar 1 plus Pillar 2A);<sup>(5)</sup> or
  - ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6.5% if the leverage ratio is 3.25%).

## 5 [External MREL liability instrument 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 eligible liabilities](#).<sup>(6)</sup> 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 institutions](#) to consider the overall maturity profile of their externally issued MREL [resources eligible liabilities](#), 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' institutions' MREL resources eligible liabilities](#) may decrease in periods of market stress, and the Bank does not intend to apply a

minimum maturity requirement [to MREL eligible liabilities](#) beyond that applicable under the No. 2 Order. The Bank may use its powers of direction to further specify [MREL eligibility criteria for MREL eligible liabilities](#) for individual [relevant persons institutions](#).

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

- 5.7 [5.6](#) The Bank does not consider liabilities the value of which is dependent on derivatives to be appropriate to qualify as MREL [resources eligible liabilities](#). The Bank

(1) [Global systemically important banks \(G-SIBs\) as identified by the Financial Stability Board in consultation with the Board Committee on banking supervision and national authorities.](#)

(2) [Or, if higher and to the extent it applies after 31 December 2017, the Basel I floor.](#)

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

(4) [Domestic systemically important banks \(D-SIBs\) are those institutions that are subject to the PRA leverage ratio requirement \(ie with retail deposits over £50 billion\) and/or any institutions that are designated as an O-SII \(other systemically important institution\) by the PRA pursuant to article 131\(3\) of the Capital Requirements Directive \(2013/36/EU\), and which have a resolution entity in the United Kingdom.](#)

(5) [Or, if higher and to the extent it applies after 31 December 2017, the Basel I floor.](#)

(6) See in particular Section 123(4).

does not consider liabilities which only include put or call options to be dependent on derivatives for this purpose.

- 5.8 ~~5.7~~ Liabilities subject to contractual set-off or netting arrangements are not appropriate MREL ~~resources~~eligible liabilities.
- 5.9 ~~5.8~~ Where a liability is governed by non-EEA law, ~~the Bank institutions~~ will need to ~~be satisfied~~ensure that the liability could absorb losses and contribute to recapitalisation costs in resolution, having regard to the terms of the contract and legal opinions, in line with the BRRD and the contractual recognition of bail-in rules in the PRA HandbookRulebook and FCA Handbook.<sup>(1)</sup>
- 5.9 ~~The Bank's view is that the failure to meet the eligibility criteria, as described above, in both non-CET1 own funds instruments and MREL eligible liabilities is likely to constitute an impediment to successful resolution, as the resolution authority must have certainty as to the quantum of loss-absorbing capacity that will be available should the institution find itself in stress. The Bank therefore expects relevant persons to ensure that non-CET1 own funds instruments and MREL eligible liabilities comply with the eligibility criteria set out above~~
- 5.10 ~~The Bank's view is that external issuance of MREL from subsidiaries in both own funds instruments and eligible liabilities is likely to constitute an impediment to successful resolution. In line with this, externally issued regulatory capital in subsidiaries of a resolution entity may be used to meet that resolution entity's MREL to the extent that such capital qualifies as regulatory capital at the group consolidated level until the current end-state MREL date of 1 January 2022. After that point, only externally issued CET1 issued by such subsidiaries should be used to meet a resolution entity's external MREL and only then if the external issuance of CET1 is required by local regulations.~~
- 5.10 ~~5.11~~ The responsibility for ensuring that liabilities, ~~including own funds instruments,~~ are MREL eligible rests with ~~relevant persons~~institutions. ~~Relevant persons~~Institutions should obtain independent legal advice on a liability's eligibility, and provide this to the Bank where required.
- 5.11 ~~5.12~~ In line with the continuous resolvability assessment process, ~~relevant persons~~institutions 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 intra-group distribution of MREL.~~
- 6.1 The Bank will set an external MREL at the group consolidated level. ~~In addition, the~~
- 6.2 ~~The Bank will set individual MRELS for all require groups or institutions within the group. The Bank may also set individual MRELS for other entities or relevant persons<sup>(2)</sup> 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:-~~
- (c) ~~internal MREL resources must be subordinated to the operating liabilities in respect of the group entities issuing them;~~
- (d) ~~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~~
- (e) ~~internal MREL resources must be appropriately distributed within groups.~~
- 6.4 ~~6.2~~ The Bank will require institutions subject to a in respect of which bail-in is the preferred resolution strategy to structure their liabilities to achieve structural subordination of external MREL resources issued by resolution entities. 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 ~~6.3~~ For groups or 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

(1) See [www.prarulebook.co.uk/rulebook/Content/Part/211722/26-10-2016-wwww.prarulebook.co.uk/rulebook/Content/Part/211722/26-10-2016](http://www.prarulebook.co.uk/rulebook/Content/Part/211722/26-10-2016-wwww.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](http://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.

paragraph 5.2 above) should not exceed 5% of the resolution entity's overall external MREL resources.

### Availability of surplus MREL in groups

6.4 Resolution entities will be required to issue external MREL resources at least equal to all the internal MREL qualifying liabilities resources or, in other jurisdictions, equivalent subordinated instruments that can absorb losses and recapitalise a subsidiary, such as through being written down and/or converted to equity, without the use of stabilisation or resolution powers at the subsidiary level ('internal loss-absorbing resources') that are 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. For groups with UK resolution entities, the Bank expects that any 'surplus MREL' — the difference in requirements between external MREL and the sum of what must be issued to the resolution entity as internal loss-absorbing resources — should be readily available to recapitalise any direct or indirect subsidiary as necessary to support the execution of the resolution strategy and there should be no legal or operational barriers to this. For example, the surplus MREL could be used to invest in high-quality liquid assets which would be maintained at the UK resolution entity.<sup>(1)</sup> This would constitute a 'central reserve' of MREL which could be made available to material subsidiaries as needed, on the agreement of home and host authorities.

### External MREL for MPE resolution entities

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

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

6.7 A UK resolution entity should not double count MREL resources. Accordingly, the external MREL for a UK MPE resolution entity will be increased by the amount of any MREL investments its resolution group has made in other resolution groups in the same group.

### Group consolidated MREL for MPE groups

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

6.6 6.9 Accordingly, where the Bank is the home authority for the ultimate parent of a G-SIB, the Bank proposes that the group consolidated MREL that would apply to the relevant institution between 2019 and 2022 should reflect the TLAC standard and therefore constitute the highest of: (i) 16% of RWAs; (ii) 6% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups. From 1 January 2022 it should reflect the higher of: (i) 18% of RWAs; (ii) 6.75% of leverage exposures on a consolidated basis; and (iii) the sum of requirements relating to each of its resolution groups.

6.7 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.

(1) High-quality liquid assets as defined in Part Six (Liquidity) of CRR and the European Commission Delegated Act with regards to the liquidity coverage requirement (LCR) for credit institutions.

## 7 Internal MREL

### Scope

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

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

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

- a. has more than 5% of the consolidated risk-weighted assets of the group; or
- b. generates more than 5% of the total operating income of the group; or
- c. has a total leverage exposure measure larger than 5% of the group's consolidated leverage exposure measure; or
- d. exceptionally, is otherwise 'material', either directly or through its subsidiaries, to the delivery of a group's critical functions. The Bank will continue to review groups' structures and critical functions to judge if this criterion applies to any entities.

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

7.5 Where no prudential sub-consolidation currently exists for a material subsidiary, the Bank reserves the right to require the institution to draw up a sub-consolidated balance sheet to enable the Bank to calculate internal

MREL for that material subsidiary on a consolidated or sub-consolidated basis. Such circumstances might arise if the material subsidiary owned a group of subsidiaries that did not meet the conditions for internal MREL themselves but together constituted a significant proportion of the group's risk-weighted assets. This is independent from any decision by the PRA whether to set prudential requirements for the material subsidiary on a consolidated or sub-consolidated basis.

### Calibration

6.9 7.6 The intra-group 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 intra-group distribution must ensure that losses can be absorbed and passed up to the resolution entity or entities from material subsidiaries.

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

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

7.8 These factors allow the Bank to set internal MREL based on discussion with other authorities in crisis management groups – as envisaged in the TLAC standard, and resolution colleges – as required by BRRD.

7.9 The largest banking groups in the United Kingdom are subject to legislation<sup>(3)</sup> which will require them to carry out their core UK financial services and activities within a ring-fenced body (RFB) and separate these from certain

(1) For example, paragraph 4.4 provides an indicative threshold that institutions with below 40,000-80,000 transactional accounts would have a modified insolvency resolution strategy.

(2) See section 3(1) of the Banking Act and PRA (2013), 'Resolution planning', *Supervisory Statement SS19/13*; [www.bankofengland.co.uk/pradocuments/publications/policy/2013/resolutionplanning1913.pdf](http://www.bankofengland.co.uk/pradocuments/publications/policy/2013/resolutionplanning1913.pdf).

(3) The Financial Services and Markets Act 2000, as amended by the Financial Services (Banking Reform) Act 2013.

other activities of the wider group. Where an RFB is part of a material sub-group (see paragraph 7.4), the Bank expects to scale the internal MREL for the top entity of the material sub-group at 90%, as a starting point, unless the Bank is satisfied that the wider group has sufficient readily-deployable resources to justify moving to a lower calibration in the 75% to 90% range.<sup>(1)</sup> This approach is intended to ensure that the setting of internal MREL for RFBs is in line with the range set out in the FSB's international standard while minimising the RFB's dependence on the rest of the group, consistent with the PRA's ring-fencing objectives. The Bank is committed to working with overseas resolution authorities to build confidence in each other's resolution regimes. This should help contribute towards the ability to make reductions over time in the internal MREL in material sub-groups that contain a RFB.

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

7.11 For UK groups with a simple structure – for example, a single material subsidiary that sits below a UK resolution entity with few, if any other, subsidiaries – the Bank would not expect to adjust downwards the internal MREL for that UK material subsidiary. This means the internal MREL would be set at 100% of the external MREL that would have applied to the material subsidiary if it were a resolution entity. The Bank would also apply this approach also for the top entity of material sub-groups containing an RFB or for an RFB which is not part of a material sub-group if the RFB's group has a simple structure. The Bank's approach to not applying scaling would be judgement-based, and decided on a case-by-case basis, giving due consideration to the relationship between the risk profile of a material subsidiary and its wider group.

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

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

7.14 A subsidiary or sub-group should only count the internal MREL resources that it issues towards meeting its own internal MREL. Where an institution has subsidiaries that

also have internal MREL or equivalent resources, it should ensure that it has sufficient internal MREL to match both its own individual MREL as well as the internal MREL or equivalent resources of its subsidiaries. In order to achieve this, the Bank proposes that internal MREL for an institution will be increased by the amount of any internal MREL or equivalent (or loss-absorbing capacity for operational continuity) investments it has made in other entities in the same group.

## 8 Internal MREL instrument eligibility

8.1 All the eligibility criteria set out in paragraphs 5.2–5.8 that apply to external MREL resources apply equally to internal MREL eligible liabilities.

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

- (1) subordination;
- (2) the holder of the instrument;
- (3) contractual triggers; and
- (4) mismatching of internal and external MREL.

### Subordination

8.3 As in the case of eligibility for external MREL liabilities, internal MREL resources must be subordinated to the operating liabilities of the group entities issuing them. This is necessary to ensure that, in converting internal MREL, the Bank is not required to bail-in other liabilities that might rank *pari passu* and which may either be difficult to bail-in or would result in a change of ownership of the entity if converted into equity. Internal MREL eligible liabilities will need to be contractually or statutorily subordinated. However, if the entity is a holding company, it may be permitted to issue internal MREL instruments as senior liabilities provided that the sum of its liabilities that do not meet the other internal MREL eligibility criteria (excluding liabilities that previously met the internal MREL eligibility criteria but no longer meet the minimum maturity requirement referred to in paragraph 5.2 above) do not exceed 5% of the entity's overall internal MREL resources (see Section 6).

### The holder of the instrument

8.4 Institutions and groups should ensure that the issuance of internal MREL by a material subsidiary or sub-group credibly supports the resolution strategy and the passing of losses and recapitalisation needs to the resolution entity. Internal MREL eligible liabilities must be issued either directly or indirectly via

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

other entities in the same resolution group to the parent resolution entity. The Bank generally expects to accept issuance indirectly to the resolution entity along the chain of ownership, as long as there are no technical obstacles to the resolution entity becoming exposed to losses through this chain. Direct issuance could also be acceptable unless there are circumstances in which converting internal MREL to equity could result in a change of control that could be an impediment to resolution — for example if there were significant governance or tax issues as a result.

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

8.6 The Bank's view is that external issuance of MREL from non-resolution entity subsidiaries in both own funds instruments and eligible liabilities is also likely to constitute an impediment to resolution. In line with this, externally issued regulatory capital in subsidiaries of a resolution entity may be used to meet internal MREL to the extent that such capital qualifies as regulatory capital until the current end-state MREL date of 1 January 2022. After that point, only externally issued CET1 issued by such subsidiaries should be used to meet a subsidiary's internal MREL and only then if the externally issued CET1 is required by local regulations.

### **Contractual triggers**

8.7 Internal MREL resources must be capable of being written down or converted to equity without or ahead of any use of resolution powers in relation to the entity which issues them.

8.8 As a general matter, the trigger for an internal MREL instrument will need to provide the resolution authority of the material subsidiary with the right to exercise a write-down or conversion where:

- the resolution authority determines that the institution is failing or likely to fail and will, disregarding any write-down and/or conversion of the instruments, continue to be so; and for internal MREL for subsidiaries of non-UK groups, the home resolution authority consents or does not object to the write-down or conversion following 24 hours' notice; or
- a resolution entity in the group, which is a direct or indirect parent of the institution, is subject to resolution proceedings in the United Kingdom or elsewhere.<sup>(1)</sup>

8.9 The Bank's view is that the absence of contractual triggers in both non-CET1 own funds instruments and MREL eligible

liabilities is likely to constitute an impediment to resolution on the grounds that (1) the joint home-host trigger envisaged by the contractual trigger provides the mechanism for the home and host authorities to agree whether additional resources are required by the relevant subsidiary in addition to the capital provided by the conversion of the internal MREL and (2) the ability to trigger all internal MREL simultaneously provides assurance that all relevant subsidiaries are well-capitalised and ensures that the surplus resources are available to the subsidiaries (if any) that require additional resources. The Bank therefore expects institutions to include those terms in any internal MREL resources (including non-CET1 own funds).

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

### **Mismatching of internal and external MREL**

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

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

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

## 9 Loss-absorbing capacity for operational continuity

9.1 The Bank will require institutions within the group to ensure that each provider of critical services within the group maintains sufficient loss-absorbing resources to continue providing critical services during resolution, and after resolution.

9.2 With respect to calibration of loss-absorbing capacity for operational continuity, the Bank proposes that critical service providers supporting the delivery of the group's critical functions must maintain resources equivalent to at least 25% of the annual operating costs of providing services.<sup>(1)</sup> The Bank may determine, based on an analysis of individual circumstances, that a larger amount of resources is warranted to absorb costs and losses and ensure continuity in critical service provision through any resolution restructuring.

9.3 Where a critical service provider is itself an institution subject to external or internal MREL, the Bank expects to increase the quantum of external or internal MREL that it requires the institution to maintain at all times in order to provide for loss-absorbing capacity for operational continuity. Where a critical service provider in a UK group is not itself an institution (ie it is an unregulated provider of services) the Bank expects its parent to downstream the relevant amounts to the critical service provider (in the form specified below) unless it can demonstrate that the critical service provider already has the resources in the required form. Where institutions are part of non-UK groups and rely on critical services providers in the group that are outside the United Kingdom, the Bank will seek assurance in discussion with other authorities that appropriate arrangements are in place for loss-absorbing capacity for operational continuity.

9.4 The Bank proposes that the form of the operational continuity loss-absorbing capacity will depend on the type of entity that is providing the critical services. Where the entity is a material subsidiary that is already subject to internal MREL above capital requirements, the loss-absorbing capacity would need to meet the same eligibility criteria as would be needed to meet internal MREL. Where the entity is not subject to internal MREL above capital requirements, the loss-absorbing capacity requirement can be satisfied by capital or by debt instruments meeting the same eligibility criteria as internal MREL eligible liabilities. If the critical services provider is an unregulated service company that is part of a sub-group of other unregulated service companies the Bank may permit the loss-absorbing capacity to be maintained at the parent entity within the service-providing group.

## 710 Transitional arrangements

### General transitional arrangements

7.1 10.1 The MREL RTS allows the Bank to determine an appropriate transitional period for an institution to reach its end-state MREL. The transition period must be as short as possible.

7.2 10.2 To allow institutions flexibility over timing of changes to their liability structures in order to meet MREL, generally the Bank does not expect to direct ~~relevant persons/institutions~~ to ~~hold/maintain~~ MREL greater than ~~institutions'~~its regulatory capital requirements prior to the dates set out at 7.4 below in paragraph 10.4. The Bank ~~nevertheless proposes to provide~~has however provided UK resolution entities (on a bilateral basis) with an indication of the external MREL that is likely to apply at the consolidated level at the end of the relevant transitional period (in the first instance the interim MRELS). ~~The Bank also proposes to provide institutions with an indication of the internal MREL that is likely to apply at the end of the relevant transitional.~~ 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 10.3 The Bank currently expects to direct institutions to comply with an end-state external MREL (calculated in accordance with the methodology described in Section 3 and 4 above) and internal MREL (calculated in accordance with the methodology described in Section 7 above) from 1 January 2022.

7.4 10.4 Notwithstanding 7.3 above paragraph 10.3, to ensure that institutions make progress towards meeting their end-state requirements the Bank expects to direct ~~relevant~~ institutions to meet the following interim external MRELS and internal MRELS:

- (a) From 1 January 2019 UK resolution entities that are 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.<sup>(2)</sup> At the same time, material subsidiaries and sub-groups of G-SIBs that are incorporated in the United Kingdom will need to meet these minimum requirements multiplied by an

(1) For 'annual operating costs of providing services', the Bank will use 'Total operational cost' reported for each provider of critical services under PRA operational continuity policy: column 150 of Part 1 of PRA reporting template 109, or as updated from time to time, available at [www.bankofengland.co.uk/pradocuments/crdiv/prat109template.pdf](http://www.bankofengland.co.uk/pradocuments/crdiv/prat109template.pdf).

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

institution-specific scalar that is determined by the Bank.<sup>(1)</sup> In addition, the Bank expects institutions in G-SIB groups to comply with any additional requirement in respect of loss absorbing capacity for operational continuity (as described in Section 9 above) from this date.

- (b) From 1 January 2020:
- a. G-SIBs with UK resolution entities incorporated in the United Kingdom and that are G-SIBs or D-SIBs will be required to maintain MREL equal to the higher of:
    - i. two times their Pillar 1 capital requirements and one times their Pillar 2A add-ons, ie (2 x Pillar 1) plus (1 x Pillar 2A);<sup>(2)</sup> or
    - ii. if subject to a leverage ratio requirement, two times the applicable requirement (ie 6.5% if the leverage ratio requirement is 3.25%). G-SIBs in any case must meet at least 6% of leverage exposures.

At the same time, material subsidiaries of G-SIBs or D-SIBs that are incorporated in the United Kingdom will need to meet these minimum requirements multiplied by a institution-specific scalar that is determined by the Bank. In addition, the Bank expects firms in D-SIB groups to comply with any additional requirement in respect of loss absorbing capacity for operational continuity (as described in Section 9 above) from this date.

- b. Groups for which the preferred resolution strategy is use of stabilisation powers, but UK resolution entities which are not G-SIBs or D-SIBs; will be required to maintain MREL equal to 18% of risk-weighted assets. At the same time, material subsidiaries of these institutions that are incorporated in the United Kingdom will need to meet this minimum requirement multiplied by an institution-specific scalar that is determined by the Bank. In addition, the Bank expects the institutions to comply with any additional requirement in respect of loss-absorbing capacity for operational continuity (as described in Section 9 above) from this date.

**7-5 10.5** 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 10.6** 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 apply with respect to both interim

and end-state MRELS. Please consult chapter 4 of the PRA supervisory statement for further details.

### **Institution-specific transitional arrangements**

**7-7 10.7** The Bank may on an institution-specific basis set an earlier compliance date during the transitional period withfor interim (external and internal) MRELS and/or end-state MRELS greater than regulatory capital requirements, for example where the Bank has concerns about the resolvability of ana group or institution, or to implement international standards.

**7-8 10.8** 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 external and/or internal MREL applicable to an institution which has been resolved as necessary, such that the institution would not be in breach of MREL immediately following resolution.

**7-9 10.9** 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 for external MREL where the change in MREL is material. The Bank will determine the appropriate transitional period on an institution-specific basis, and expects to allow at least 36 months for transition for external MREL where the change in MREL is material. The Bank would expect to determine similar transitional arrangements for a group's internal MREL as for its external MREL. However, where groups are already subject to external MREL in excess of capital requirements, the Bank will determine the appropriate transitional period to meet internal MREL on an institution-specific basis for any subsidiaries that are newly designated as material.

(1) 'Scalar' refers to the 75%–90% scaling adjustment that the Bank expects to apply to the MREL calibration that would otherwise apply. This scalar may be 100% for groups with a simple structure.

(2) Or, if higher and to the extent it applies after 31 December 2017, the Basel I floor.