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Finance for Europe

Association for Financial Markets in Europe

EBA Draft RTS on own funds and eligible liabilities

AFME consultation response

28 August 2020

Introduction

The Association for Financial Markets in Europe (AFME)[1] welcomes the opportunity to comment on the European Banking Authority's (EBA's) draft regulatory technical standards (RTS) pursuant to the mandates provided to it under Articles 72b(7) and 78a(3) of the CRR2. We hope that the EBA will find our response of assistance when finalising their proposed RTS.

AFME has been very supportive of the development of an effective recovery and resolution framework in Europe and we continue to support the overarching aims of ensuring resolvability. Clarity on specific aspects of the eligibility criteria for MREL, including what constitutes an incentive to redeem, and indirect funding, as well as a clear understanding of the process and procedure for the calling, redemption, repayment or repurchase ('redemption') of eligible liabilities instruments are vital for institutions to continue on the path to achieving resolvability, in part through the issuance and management of MREL.

We recognise the instruction of the level one text under Article 72b(7) to fully align the RTS related to the applicable forms and nature of indirect funding of eligible liabilities instruments, and the form and nature of incentives to redeem, with those that already exist for own funds instruments. We also recognise that the level one text instructs alignment in relation to Article 78a(3)(d), on the meaning of 'sustainable for the income capacity of the institution', in relation to the RTS for the redemption of own funds instruments.

In our view these instructions are appropriate, but they should not be taken to mean alignment in areas beyond this, particularly where nuanced approaches are necessary to accommodate differences between own funds and eligible liabilities instruments. It is with this in mind that we have approached the EBA's consultation, to which we set out our views below.

Executive Summary

We welcome the publication of the EBA's draft RTS and after having reviewed the proposals it is clear to us that there are a number of key areas where we would welcome further consideration:

1. **Deductions and 'sufficient certainty':** We welcome the clarity provided by the EBA in their draft RTS stating clearly that, in line with the existing RTS on own funds, deductions for ad hoc prior permissions should occur once the redemption is expected to take place with 'sufficient certainty'; specifically following

[1] The Association for Financial Markets in Europe (AFME) represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society. AFME is listed on the EU Transparency Register, registration number 65110063986-76.

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both the public announcement of the redemption by the relevant entity, and when the prior permission itself has been obtained. Unfortunately, some competent authorities have required deduction following only the granting of the prior permission, even for liability management exercises, seemingly due to a particular EBA Q&A answer. We therefore encourage the EBA to provide clarity in this area to ensure that the rules in the existing RTS on own funds and the proposed future RTS are not overridden by Q&A answers and are appropriately and consistently applied across the EU.

With regards to the proposed approach to deductions for the general prior permissions, we note that the concept of 'sufficient certainty' has, rather disappointingly, been disregarded. The EBA's approach appears to be to restrict the possible use of the general prior permission to only market making activities by applying the same deductions procedure here. This runs against the intention of the general prior permission and the level one text that provides for their use across a variety of activities, covering both market making and liability management exercises. We strongly believe that the EBA should revisit its approach such that the general prior permission can be utilised for liabilities management exercises in a way that sits on par with the approach for ad hoc prior permissions, i.e. that the concept of 'sufficient certainty' continue to apply when considering the time at which a deduction should take place. The intent behind the use of any general prior permission should be fully considered and reflected in the EBA's final RTS.

The final RTS should also take into consideration in-scope liabilities that are no longer deemed eligible, by virtue of having less than 12-months maturity remining. The CRR is clear on their inclusion, however the RTS does not set out clearly that permissions pursuant to these liabilities should not incur a deduction. In our view the procedure for redeeming such liabilities should also be streamlined given their continued cost to firms despite their diminished value for meeting MREL requirements.

2. **The 3% limitation to the eligible liabilities' general prior permission:** We believe that there are fundamental issues with the imposition of a limit to the general prior permission for eligible liabilities. In part deriving from the much larger volume of eligible liabilities in issue with relatively shorter maturities compared to own funds instruments. Notwithstanding our concerns on the proposed approach to deductions, the proposed 3% cap is likely to be insufficient for institution to be able to rely on a general prior permission to redeem and refinance instruments. This would likely require multiple ad hoc permissions to be necessary, with the extra cost this would entail.

   More significantly however, we note that the 3% cap proposed by the EBA is not required by the mandate to the EBA in the level 1 text, nor are the limitations required to meet prudential objectives. The level 1 text also does not require alignment with the redemption rules that apply to own funds in this area. The question therefore arises as to why the EBA feels that it is appropriate to suggest this limitation given Article 78a bestows the power to the relevant resolution authority to set the limit of the eligible liabilities general prior permission.

3. **Extension of the notification period and general prior permission renewals:** The EBA's proposal to extend the notification period from three months to four months for individual permissions, and apply the same period for general prior permissions, is very disappointing. The additional month introduces complexities that may not have been fully considered, including through interactions with reporting and disclosure dates. Whilst we recognise the need for both competent and resolution authorities to liaise when determining whether to permit a redemption, an additional month for this to take place appears somewhat excessive and disproportionate. As the approval process can be highly standardised, three-months should be more than sufficient for the competent authority to process the application and liaise with the resolution authority.

Where any redemptions require a sufficient replacement of own funds or eligible liabilities, we strongly believe that the process should be further streamlined, recognising that the act of redeeming an instrument after or at the same time as issuing a replacement represents little or no risk to the institution compromising the level at which it operates above its requirements. Authorities should therefore not require a full three-month consideration period, and we propose that the EBA should set the period for such scenarios at two-months.

For the case of renewing an existing general prior permission, similar reductions in notice periods should be observed.

4. **Scope:** We would welcome clarity from the EBA as to the scope of instruments covered by the proposed RTS, specifically whether or not this extends to instruments eligible by virtue of BRRD2 derogations to the CRR2 eligibility criteria (e.g. structured notes). The question also arises as to whether the regime applies to any legacy instruments that may, by virtue of grandfathering provisions, capture instruments as eligible for MREL, even where the institution does not count such liabilities towards their MREL requirement, or when such legacy instrument are due to be phased out. Clarity on these issues would be most welcomed by the EBA in their final RTS.

Below we visit each question in turn providing additional comments where appropriate. Should there be any questions on our response, please do let us know.

<u>Responses to questions provided</u>

4. **It is recalled that, as per the mandate to the EBA, the RTS on eligible liabilities for the purpose of indirect funding has to be fully aligned with the one on own funds. Are the interactions and consequences of the rules on direct and indirect funding appropriately described and captured for eligible liabilities and resolution groups?**

We welcome the EBA's draft RTS with regards to Article 72b, clarifying the applicable rules on direct and indirect funding, as well as on incentives to redeem. We recognise that alignment is mandated by the level 1 text and believe that the EBA have reflected this in their proposals.

However, further clarity would be welcomed on direct/indirect funding for MREL, particularly in the case of internal MREL/TLAC transactions (as per paragraph 15), given that it is normal business practice for subsidiaries to deposit and receive funds from its parent entity.

It would be helpful to clarify that an institution is not directly or indirectly funding its internal MREL/TLAC requirements through the payment of a lawful dividend or an early repayment of an MREL instrument occurring at a point in time when the institution is also receiving new MREL/TLAC from its parent, which may arise in refinancing or restructuring of an institution's internal MREL/TLAC for capital efficiency or as part of a double leverage transaction. Where double leverage transactions occur, i.e. where a bank holding company conducts a debt offering to an external third party to acquire equity in one of its own subsidiaries (as may be pursued to meet internal TLAC/MREL requirements), it would be important for such activity to not be captured by the EBA's definition. Whilst we do not see such a set of circumstances being deemed as direct or indirect funding given the source of the internal funding remains an external issuance, a statement from the EBA to this effect would provide a clear understanding on this point.

Whilst the EBA consultation paper does not seek views on its proposed RTS regarding incentives to redeem, we would welcome further clarity from the EBA. Specifically, that zero coupon callables, or make-whole call options, will not be seen as being an incentive to redeem. It is important that the final RTS does not exclude instruments with these features by designating them as incorporating an incentive to redeem, as such call options can only be exercised following a successful application for redemption. It is also necessary that these call options remain open to institutions to include in issuances to ensure flexibility in issuance structure. This would enable institutions to access investors with appetite for instruments with such call options.

6. **Do you consider that the general prior permission as per the 2nd subparagraph of Article 78(1) CRR, with the limits included therein, would be sufficient to cater for permissions to repurchase own funds instruments then to be passed on to employees as part of their remuneration (former Article 29(4) of the RTS), in addition to market making and other repurchase activities? Would you consider any derogations to be needed (in particular in terms of limits and one-year timeframe)?**

Regarding staff remuneration with own funds instruments, we understand from the explanatory text on Article 28 that the EBA did not intend to change the content of the current RTS (Article 29(4)). Indeed, the EBA states "(…) <u>*have only been moved here*</u> *from the former Article 29(4) in order to bundle provisions related to deductions in Article 28*". That is confirmed as the proposed new RTS still states "*deduct these instruments from own funds on a corresponding deduction approach <u>for the time they are held</u>*" (Article 28(4)).

However, since the proposed new Article 28(4) combines the remuneration topic with "*When applying for a general prior permission* (…)" (beginning of the first sentence of the proposed new Article 28 (4)), the outcome in relation to staff remuneration is not consistent with the intention.

For a general prior permission, the proposed Article 28(3) unhelpfully specifies that the approved amount has to be deducted once the permission has been obtained. For the remuneration case the proposed new Article 28(4) leads to the impression that the instruments held have to be deducted in addition to those from the general deduction of the predetermined amount for the general prior permission, and that the remuneration buybacks also have to be included in and monitored against the limit of the predetermined amount of the general prior permission.

We support the EBA's intention to maintain the same treatment for cases of staff remuneration with own funds instruments. We therefore believe that permission for repurchases of own funds instruments for remuneration purposes (current Article 29(4)) should not be solely possible under a general prior permission, but that they should still be possible to obtain under the ad hoc approach too. The institution should be able to apply separately for employee remuneration as under the current Article 29(4) (for which under the current practice no Euro amount is granted but a permission allowing the buyback etc. of e.g. a certain number of shares) under which only the instruments actually held need to be deducted. Should an institution wish to apply for this under a general prior permission that also should be possible. Such remuneration cases do not have to be included in and monitored against the limit of the predetermined amount of the general prior permission. For this purpose we recommend to use the wording of the current Article 29(4), whilst still having the option, but not the obligation, to seek a permission for remuneration purposes under the general prior permission approach.

Finally, we note that it is typical for employees to be awarded a number of shares, and not a EUR-amount as share-equivalent. As a consequence, the bank has a delivery obligation of a certain number of shares, and hence a purchase requirement in this number of shares. Therefore, it is preferable that permissions for share buybacks with respect to remuneration could continue to cover the approval of a maximum number of shares instead of a EUR-amount. This would avoid seeking approval of an uncertain projection relying on a future share price assumption.

8. Is the information required appropriate? Please specify any change you would make and why. Please consider consistency with the prior permission regime for eligible liabilities instruments.

15. Do you think the information required in Article 32d is appropriate? Please precise any change you would suggest and why. Please consider consistency with the prior permission regime for own funds.

The content of the application to be submitted in accordance with the draft RTS Article 30(1)(d), and Article 32d to reduce own funds and eligible liabilities significantly overlaps with information already obtained by the supervisory and resolution authorities through other channels (e.g. supervisory reporting). Furthermore, these elements are set either by (i) regulations; or, (ii) the supervisory and resolution authorities. Therefore, this information is already available to the supervisory and resolution authorities.

Further to this, the additional information requested under the proposed new Article 30a diverges from the practices in place at the ECB. The proposed requirement under the RTS to specify in the application of a general prior permission the specific amount of each relevant Tier 2 issue subject to the request, and the total carrying amount of the relevant outstanding instruments, conflicts with the ECB's approach to grant permissions for all Tier 2 instruments without such information being required.

We therefore do not believe that the information required is appropriate, and we urge the EBA to limit the information request to solely those elements that are (i) necessary to assess the institution's request; (ii) is not already publicly available or obtained by the supervisory and resolution authorities through other channels; and (iii) is aligned with the approach already undertaken at the ECB (for example with regard to Tier 2).

9. Do you consider the four months deadline appropriate? Would you consider making a difference between the individual permissions pursuant to Article 78(1) points (a) or (b) CRR and the general prior permission pursuant to the 2nd subparagraph of Article 78(1) CRR? In case the four months deadline was kept for first time applications for general prior permission, would you see merit in:

(a) shortening the deadline for applications for the renewal of the permission?

(b) adjusting the content of the application to be submitted to the competent authority?

Please provide some rationale. Also, please consider consistency with the prior permission regime for eligible liabilities instruments.

16. Do you consider the four months deadline in Article 32f appropriate? Would you consider making a difference between the individual prior permission pursuant to Article 78a(1) points (a), (b) or (c) CRR and the general prior permission pursuant to the 2nd subparagraph of Article 78a(1) CRR? In case the four months deadline was kept for first time applications for general prior permission, would you see merit in:

(a) shortening the deadline for applications for the renewal of the permission?

(b) adjusting the content of the application to be submitted to the competent authority?

Please provide some rationale. Also, please consider consistency with the prior permission regime for eligible liabilities instruments.

The EBA's proposal to extend the notification period from three months to four months for individual permissions, and apply the same period for general prior permissions, is very disappointing. This is especially in light of recent calls from industry at relevant EBA roundtables to reduce the notification period applicable to ensure institutions can react swiftly and more dynamically to market conditions, and can more effectively and efficiently manage their liabilities whilst still maintaining appropriate levels of own funds, and MREL more broadly.

The additional month introduces complexities that may not have been fully considered. We believe that a four-month period, representing more than a quarter, may have implications for disclosures to the market ahead of any formal announcements on potential redemptions, as this may cut across end-quarter reporting and disclosure dates. Previously such conflicts could be avoided within a three-month period. By extending the period to four-months cases may arise where institutions have to disclose this intention, before a formal announcement is made to the market, whilst they wait for approval. This could impact the pricing of the instrument and undermine the commercial drivers for making the redemption in the first place.

Beyond this there are also concerns around increased costs to institutions. If an institution is required to refinance an instrument prior to submitting a notification to the competent authority, an additional month added to the notification period will further reduce potential market windows for redemption, whilst also increasing the cost of carrying the instrument.

Whilst we recognise the need for both competent and resolution authorities to liaise when determining whether to permit a redemption, an additional month for this to take place appears somewhat excessive and disproportionate. Especially given that both authorities should be engaged from an early stage, and not only after an initial three-month consideration by the leading authority. As the approval process can be highly standardised, three-months should be more than sufficient for the competent authority to process the application and liaise with the resolution authority, or vice-versa. To help support an efficient and timely assessment of prior permissions, the EBA should strongly encourage competent and resolution authorities to closely coordinate and develop streamlined processes for information sharing and decision-making to facilitate reduced timeframes for approval.

Where any redemptions require a sufficient replacement of own funds or eligible liabilities, we strongly believe that the process should be further streamlined. The process must recognise that the act of redeeming an instrument after or at the same time as issuing a replacement represents little or no risk to the institution compromising the level at which it operates above its requirements. Authorities should therefore not require a full three-month consideration period, and we propose that the EBA should set the period for such scenarios at two-months. Such a reduced period should also apply for immaterial redemption amounts, especially where institutions are operating at a sufficient level above their requirements. If the final RTS are to take a proportionate approach, such different scenarios should follow an adjusted process to reflect the potential (lack of) impacts on an institutions level of loss-absorbing capacity. A reduced notification period should form part of that differentiation, as should the information requirements.

Regarding the renewal of general prior permissions, similar reductions in notice period and information requirements should also be applied. Especially where any general prior permission is utilised to obtain permission for activities related to pre-existing thresholds, e.g. market making. Alternatively, while CRR Articles 78(1) and 78a(1) limit the general permission regime to a time period not exceeding one year, we suggest to allow in the RTS a procedure that the general permission is applicable for a period not exceeding one year, but is automatically renewed unless the institution is notified otherwise by the competent authority. This would ensure compliance with the Level 1 text, while also providing an efficient process for both the institution and the competent authority. It would also bring the final RTS more closely into alignment with existing such permissions in some Member States, where such permissions are in place for several years.

11. Do you consider the deduction rules appropriate for eligible liabilities? If not, what would be the rationale for departing from the rules applicable for own funds?

We welcome the clarity provided by the EBA in their draft RTS stating clearly that deductions for ad hoc prior permissions should occur once the redemption is expected to take place with 'sufficient certainty'; specifically that this is deemed to have been achieved following *both* the public announcement of the redemption by the relevant entity, *and* when the prior permission itself has been obtained. Whilst this appropriately replicates the existing approach within the RTS for own funds, unfortunately some competent authorities have required deduction following only the granting of the prior permission – not when sufficient certainty has been obtained as per the existing RTS – even for liability management (non-market making) activities. We therefore welcome the EBA's proposal, but encourage the EBA to address this issue of divergent treatment. We understand the current approach taken by these competent authorities stems from a particular Q&A[2], which we would strongly encourage the EBA to provide clarity on at this opportunity. The Q&A should not override the RTS, and a deduction at point of authorisation should not become the automatic treatment for all instances of own funds instrument redemption, repayment and repurchase activities.

We are concerned that the approach to deductions for the proposed general prior permission dismisses the notion of 'sufficient certainty' and severely limits the use of it to smaller market making activities, which are already subject to such an approach to deductions as per the EBA's guidance following a number of related Q&As[3]. This would make sense if the general prior permission were strictly limited to such activities, however it is not. The general prior permission could, and should, be open to entities to utilise for liability management exercises. The CRR itself does not restrict the general prior permission to one specific activity, and clearly envisages the use of the general prior permission for calls, redemptions, repayments, and repurchases; all of which can occur in liability management exercises.

It is important that the final EBA RTS do not prejudice or act to restrict the possible use of the general prior permission in any way, but should instead accommodate the different forms in which it may be applied. Therefore, we suggest that the timing of the applicable deduction following the granting of a general prior permission should be tailored to the way in which it has been used. As there are currently two different approaches to deductions for ad hoc prior permissions, depending on whether the redemption is related to market making activity or not, we strongly recommend that such consideration be made for deductions under a general prior permission too. This would require entities to state when applying for a general prior permission whether it is to cover market making activities or not. This would allow a level playing field between entities utilising either an ad hoc or general prior permission for liability management exercises, specifically avoiding the proposed capital penalty that would apply through immediate deduction under the proposed approach in the draft RTS for general prior permissions.

We wish to stress that it is important to differentiate the approach to such deductions according to the intent of the institution to ensure that the general prior permission is not inadvertently restricted to market making activities. Article 32b(3) as proposed would make it too punitive to apply the general permission regime for anything other than very small market making limits (and even then posing problems for this activity too). In restricting the use of the general prior permission in this way, it in turn increases the burden to process the otherwise necessary ad hoc applications for liability management exercises, for both institutions and the competent authorities. Such an approach would circumvent the intended benefits of the general prior permission.

[2] EBA Q&A: 2017_3277: https://eba.europa.eu/single-rule-book-qa/-/qna/view/publicId/2017_3277
[3] EBA Q&As: 2014_1352: https://eba.europa.eu/single-rule-book-qa/-/qna/view/publicId/2014_1352 & 2017_3174; https://eba.europa.eu/single-rule-book-qa/-/qna/view/publicId/2017_3174

Given the larger volume of eligible liabilities in issue and their relatively shorter maturity, it is likely that these issues may arise more frequently than for own funds. It would generally be impractical for both the institution and the competent authority to apply an instrument-by-instrument approval process that can be completed in a timely manner. The general permission regime would in these cases be more practical; indeed it was in part for this reason this it was envisaged as a useful way of institutions obtaining the permission required. This problem will also only be exacerbated by the application of Articles 77(2) and 78a to all eligible liability instruments, including eligible liability instruments for internal TLAC and MREL purposes.

In addition to this, there are subsequent implications to having a deduction the moment approval is obtained for liability management exercises and calls/redemptions within the general prior permission process, due to requirements under the Market Abuse Regulation, specifically to disclose inside information. If a bank is required to deduct large amounts of debt instruments from the moment the permission is granted, and this is published in a Pillar 3 report, there may be grounds for inadvertently disclosing information to the market that a bank is potentially looking to tender certain notes. This may be price sensitive information and could require a bank to make an announcement to the market clarifying its position on those bonds (despite the fact that the bank may not actually know at that point whether it wants to carry out a tender offer or not). This should be avoided by continuing to apply the principle of 'sufficient certainty' with regards to the deductions for liability management exercises under the general prior permission.

We therefore encourage the EBA to amend the proposed RTS to ensure that 'sufficient certainty' continues to act as the trigger for appropriate deductions under a general prior permission, just as it does under the ad hoc prior permission regime. This would enable not just a level playing field between the two routes to prior permission, but would just as importantly not impose punitive restrictions on the use of the general prior permission thereby limiting the benefits it can bring to effective liability management. This could be achieved through the creation of two separate types of general prior permission, each with the appropriate approach to deductions applying (e.g. one for market making in eligible liabilities instruments (as we suggest below); and another for liability management exercises including call options, tender exchanges and any kind of similar exercises for eligible liabilities instruments).

Redemption of former eligible liabilities instruments: The CRR is clear that formerly eligible liabilities (i.e. those with less than 12 months remaining until maturity) are within scope of the prior permission regime. However, the EBA RTS does not make account for these in their draft RTS, specifically with regard to the process that should be followed, including on deductions.

We do not believe there is any reason for a deduction to apply for the redemption of such an instrument as it will no longer be eligible to count towards a firm's MREL requirement. As such the RTS should specify that where a permission concerns such an instrument, no deduction is to be taken forward, be this under an ad hoc prior permission or as part of a general prior permission.

Formerly eligible liabilities with less than 12 months remaining until maturity should also, in our view, not be subject to the same procedure as for eligible liabilities given their regulatory treatment and their diminished value to the institution as a result. It is our strong view that authorities should automatically provide for the permission of such instruments being redeemed upon receipt of a request from an institution. It should not be in the interest of either authorities or institutions to have the costs of carrying ineligible instruments incurred for longer than is necessary. Streamlining the process for redeeming such instruments should therefore be given consideration by the EBA as part of their work to finalise the RTS.

Approach to deductions for market making: The EBA's current approach to market making, i.e. to deduct the full amount of the permission at the point where permission is granted, is overly punitive in our view. In light of our concerns as set out above in regard to the approach for general prior permissions, we encourage the EBA to revisit its approach to deductions for market making activities in eligible liabilities under both the ad hoc prior permission and the general prior permission. We suggest that the approach be reconsidered particularly given the prerequisite that permissions can only be granted where institutions meet their requirements and provide safeguards to authorities that they are able to operate sufficiently above them too.

One solution that we wish to suggest would see institutions apply for permissions as at present for market making envelopes in eligible liabilities, but upon authorisation no deduction would be immediately taken. Instead, the current approach put in place by the Single Resolution Board (SRB) should apply[4]. Specifically, that inventory held for market making purposes would be deducted in real time, and any redemptions, recalls or repurchases for market making purposes would lead to a deduction at the point such activity takes place, provided that it falls within the agreed limit of the prior permission.

This approach has already been proven to work, and would still introduce requirements for prior permission and the need for firms (as per the level 1 text) to provide safeguards to authorities that they are able to operate sufficiently above their requirements, but whilst also minimising the cost to firms of offering and undertaking market making activity. In light of this approach having already been endorsed by the SRB by virtue of taking it forward ahead of the EBA's RTS on this matter, we strongly believe that it should continue. There have been no detrimental effects and, absent any, we see no reason for a loss in efficiency in undertaking market making activities in eligible liabilities.

We also believe that in considering this the EBA should be mindful of the benefits that come from a firm market making in its own issuances. When issuing instruments to fulfil requirements, investors are given greater confidence in the future tradability of the instrument if the issuer is able to market make in that issuance sufficiently, and without undue delay in providing pricing to that investor. Being able to offer liquidity in own MREL issuances through market making further strengthens the marketability, and desirability, of holding and investing in such an instrument, which in turn promotes and assists the development of a deep and liquid market in MREL. Market making in own instruments, provided it is undertaken without detriment to that firm meeting its own requirements, is a positive and complementary activity. Whilst we agree that prudent measures around this activity is understandably necessary, we strongly believe the approach undertaken by the SRB to be just that, and that it has proven to be effective whilst also minimising cost to firms and in turn investors.

Deduction reversals and partial permission use: In addition to this we believe that it is worth taking this opportunity to raise the issue of reversing a permission and the relevant deduction. Specifically, if a deduction has been taken in anticipation of a proposed redemption after having reached a point of 'sufficient certainty', a bank should be able to reverse the deduction immediately at the point when it decides not to proceed with a proposed redemption. Currently this is not foreseen in the draft RTS for either own funds or eligible liabilities and we believe this should be provided for so as to not unfairly penalise any institution that has opted to not redeem own funds or eligible liabilities instruments. We would welcome the EBA's thoughts on this, as it would be a sensible improvement to the regime.

The current RTS also do not consider instances where a permission is not fully utilised, for example following a tender exercise with less than 100% take-up. Whilst a permission may be pursued for the full potential amount that could be redeemed, sufficient certainty on the redemption itself is not obtained until the tender exercise is completed. We would therefore welcome the EBA clarifying in their final RTS that the intended

[4] SRB, 'CRR addendum to the 2018 SRB MREL Policy' – Annex 1 (page 6): https://srb.europa.eu/sites/srbsite/files/crr_addendum_to_the_2018_srb_mrel_policy.pdf

redemptions following a tender exercise should be the amount that attracts a deduction, not the amount in full should such a tender not be fully subscribed.

12. **Do you agree that general prior permissions should not be confined only to market making? Why would liability management operations not be sufficiently covered, as for own funds, via ad-hoc permissions? Please substantiate based on concrete experience.**
13. **Is the maximum limit of 3% of the total amount of outstanding eligible liabilities instruments sufficient? If not, please explain which percentage value of outstanding eligible liabilities instruments you would suggest and justify based on your experience.**

We believe that there are fundamental issues with the imposition of a limit to the general prior permission for eligible liabilities, and we strongly oppose the EBA's proposed 3% limit in relation to the general prior permission to redeem, call and/or purchase eligible liability instruments.

Market making volumes and impact on investors: Market making in eligible liabilities, in particular senior vanilla or structured bonds sold to private investors, features greater volumes that are not comparable with market making in own funds instruments. As such, the adoption of the same quantitative threshold for own funds in the case of eligible liabilities would be incompatible and inappropriate, given the market volumes of eligible liability instruments. Contrarily to own funds and TLAC instruments, senior plain vanilla and structured bonds tend to be distributed by banks to investors in significant amounts. The proposed limit would therefore risk reducing liquidity in many of these outstanding instruments.

Impact on funding costs and operational burdens: As an example, if we consider a range of banks of different sizes with €2-€4bn and €50-€90bn in outstanding eligible liabilities instruments, these in turn could avail of a general prior permission that is limited to €60-€120m and €1.5-€2.4bn respectively in any given year regardless of the excess eligible liabilities instruments that they hold above the combined requirements.

Such institutions would very likely have a stock of callable eligible liabilities instruments with a residual maturity of one year or less in an amount of €120-€311m and €3bn-€7bn every other year, and such institutions would, therefore, not be able to benefit from this general prior permission and would need to request numerous ad-hoc permissions to reduce entire series of eligible liabilities instruments (4 months in advance as per the currently proposed RTS). This is the case regardless of whether the same banks replaced the redemptions with other eligible liabilities or where they had a residual stock of eligible liabilities instruments that exceeded the combined requirements.

This would have the effect of creating unwarranted operational issues for the institutions given the compounded effect created by both (i) the proposed 4 months' period to obtain permission and (ii) the number of instruments callable each year.

An institution may be required to pursue multiple prior permissions to refinance instruments, or face having to refinance instruments without the ability to call them, with the extra cost this would entail. Assuming a large bank with an average of €5bn callable MREL in any given year, this would result in an additional cost of €50m a year, however for many banks the annual callable amount could be multiples of this. This is a particularly prevalent issue for eligible liabilities instruments (as opposed to own funds) because eligible liabilities instruments lose their regulatory value in the final year to maturity and, therefore, banks require the additional flexibility afforded by the general prior permission to manage their MREL resources efficiently and effectively.

Implications for competitiveness: The above factors represent a meaningful negative impact on the way in which European banks can manage their eligible liabilities in a way that is replicated nowhere else, undermining the competitiveness of European banks. At best this approach would require multiple further permissions creating unnecessary inefficiencies and costs for both banks and authorities, but at worst it could limit the ability of firms to manage liabilities and significantly increase carry costs.

It is important to also consider the impact such a cap may have, particularly where it would limit the amount of market making that could be undertaken under a given general prior permission. Such a limit being put in place on European banks would hinder their ability to market make or at the very least increase the operational costs of undertaking such activities were multiple permission processes needed to be pursued. The proposed cap may also give other banks not subject to these restrictions a competitive advantage in terms of funding costs, as they would have greater flexibility in increasing and decreasing their own liabilities as needed. These factors should be considered by the EBA.

Mandate of the EBA: More significantly we note that the 3% cap proposed by the EBA is not required by the mandate to the EBA in the level 1 text, nor are the limitations required to meet prudential objectives. The level 1 text also does not require alignment with the redemption rules that apply to own funds in this area. The question therefore arises as to why the EBA feels that it is appropriate to suggest this limitation given Article 78a bestows the power to the relevant resolution authority to set the limit of the eligible liabilities general prior permission. Continuing with a 3% limit, whilst on its own not the biggest barrier to the use of the general prior permission (given our concerns on the deductions approach proposed), it does constitute the EBA prejudicing the decisions of resolution authorities, and would represent an overriding of the level 1 text. This would set an unwelcome precedent.

It is noticeable that the EBA have not taken forward a proposed quantitative threshold for the margin by which the relevant authorities consider it necessary for an institution to exceed for permission to be granted on a proposed redemption. Whilst we would not expect this, it would be deemed similar to the setting of the 3% cap and we would welcome clarity from the EBA as to why it seeks to propose a threshold in one area but not the other. We would in any case recommend that the 3% limit not be retained in the final RTS for the reasons set out above.

Additional comments:

Scope: We would welcome clarity from the EBA as to the scope of instruments covered by the proposed RTS. Whilst the EBA have been clear that the permission regime applies for external and internal TLAC and MREL, what is not clear is whether or not this extends to instruments eligible by virtue of BRRD2 derogations to the CRR2 eligibility criteria (e.g. structured notes).

The question also arises as to whether the regime applies to any legacy instruments that may, by virtue of grandfathering provisions, capture instruments as eligible for MREL, even where the institution does not count such liabilities towards their MREL requirement, or when such legacy instruments are due to be phased out. Clarity on these issues would be most welcomed by the EBA in their final RTS.

Transparency: We understand that in the UK the Prudential Regulation Authority (PRA), via the Financial Conduct Authority (FCA) Register, formally publish the basis of redemption decisions for own funds instruments, where the date of publication is controlled by the issuer themselves. Has the EBA considered whether it would seek to do the same for own funds and eligible liabilities instruments going forwards as a means of improving general transparency?

We welcome any questions or views you may have on this response and we are very happy to discuss these issues further.

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