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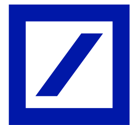

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Dear Mr. Farkas,

DB response to the Draft Regulatory Technical Standards (RTS) on criteria for determining the minimum requirement for own funds and eligible liabilities under Directive 2014/59/EU

Deutsche Bank (DB) welcomes the opportunity to comment on the European Banking Authority's (EBA) draft RTS on criteria for determining the minimum requirement for own funds and eligible liabilities (MREL) under the Bank Resolution and Recovery Directive (BRRD).

We support the EBA's effort to ensure a harmonised implementation of the BRRD across the European Union, and provide common criteria for the determination of MREL. In some areas, however, we think the draft RTS are not tailored enough to individual bank's circumstances and resolution strategy. Therefore, we suggest some refinements, notably:

- We are concerned that by considering separately the loss absorption and recapitalisation amounts the EBA risks doubling up requirements, thereby imposing a significantly higher level of MREL than is necessary. We recommend recognising the interplay between the two criteria as well as the interaction with the resolution strategy, and to view them as part of a continuum of overall loss-absorbing capacity.
- The EBA, by focusing on capital requirements, is going in the right direction; however this does not imply that MREL should automatically be set at double the capital requirements of the group as a whole, nor should the combined buffer requirements, leverage and Basel 1 floor be considered as automatic criteria when determining MREL.
- When considering loss-absorbing capacity, it is important to bear in mind that at the point of resolution, a bank will likely no longer be a Global Systemically Important Bank and would still have significant amounts of capital and Common Equity Tier 1 remaining. In addition, it would have significantly more bail-in

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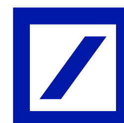


capacity than only MREL. Therefore, the resolution authority needs to take into account what the bank would look like at the point of resolution when determining MREL.

- Finally, we support the RTS' intention to take into account the impact of exclusions from bail-in to ensure that the "no creditor worse off" principle is respected; and to consider the likelihood of needing the resolution fund in bail-in. However, neither should result in a mechanistic adjustment to MREL, and the use of resolution funds should not be specific to G-SIBs.

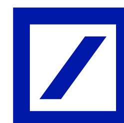
Additionally, we appreciate the EBA's intention to align the draft RTS on MREL with the Financial Stability Board (FSB) proposals on total loss-absorbing capacity (TLAC). We agree the draft RTS should provide flexibility within the MREL framework for resolution authorities who wish to enforce TLAC minima early to do so. However, given the very significant issues faced by European banks under the current FSB proposals, we believe that legislative changes to the BRRD will be needed during the review of the Directive - including to MREL eligibility and minimum percentages. It is important to implement TLAC in a way that maintains a level playing field between banks globally and even within the EU.

Our detailed responses to the questions are below. Please let us know if you would like to discuss this further.

Yours sincerely,

Daniel Trinder

Global Head of Regulatory Policy



Draft Regulatory Technical Standards on criteria for determining MREL

Q1. The draft text above *(Article 2)* describes comprehensively capital requirements under the CRR/CRD IV framework, which includes minimum CET1, AT1 and total capital requirements, capital buffers required by CRD IV, Pillar 2 capital requirements set on a case-by-case basis, and backstop capital measures (Basel 1 floor and leverage ratio). The EBA is seeking comments on whether all elements of these capital requirements should be considered for the assessment of the loss absorption amount. Do you consider that any of these components of the overall capital requirement (other than the minimum CET1 requirement) are not appropriate indicators of loss in resolution, and if so why?

With regards to how resolution authorities should assess whether institutions have sufficient eligible liabilities to absorb losses, we agree that the criteria should be closely linked to the capital requirements. As calibrated under the Basel framework, capital requirements already seek to capture unexpected losses that might need to be absorbed.

However, we are concerned that the current drafting requires entirely separate evaluation of loss absorption and recapitalisation amounts, simply summing them rather that recognising the interplay between the two. This risks doubling up requirements and potentially requiring significantly higher percentages of MREL than is even required for G-SIFIs under the FSB's TLAC requirement.

It also ignores that, at the point of resolution, firms are likely to have significant amounts of capital and Common Equity Tier 1 (CET 1) remaining. In addition, significantly more bail-in capacity (e.g. instruments with maturity less than one year) is likely to exist than only that met through MREL-eligible instruments. A bank like Deutsche Bank for instance can expect to have an amount of bail-in available about twice the MREL amount - on top MREL eligible liabilities - at the point of resolution. To ensure proportionality and avoid imposing excessive MREL on banks which would potentially constrain their ongoing business, we strongly recommend viewing the two criteria as part of a continuum of overall loss-absorbing capacity.

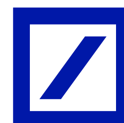
To determine the loss absorption amount for the purpose of MREL some elements are more relevant than others:

a) We agree that core capital requirements are a key indicator of loss in resolution.

b) We agree that the pillar 2 process is also relevant given that it helps identify any specific risks individual banks might be facing. However, this should not necessarily be an automatic doubling of Total Supervisory Review and Evaluation Process (SREP) requirements.

c) We do not believe that the combined buffer requirements are an appropriate determinant here. These buffers are designed to be used in a period of stress, without the bank being deemed to be in breach of minimum capital requirements. If the combined buffer requirements were automatically included in the loss absorption amount, the buffers would become a de facto minimum requirement, contrary to their original purpose.

d) Although leverage is an important backstop that may be relevant to consider when setting the loss absorption amount, it should not become the primary constraint as it is not risk sensitive. The purpose of leverage is not to replace risk based capital requirements, and therefore the EBA should not require it as an automatic indicator to determine the loss absorption amount.



e) Finally, we consider that it would not be appropriate to use the Basel 1 floor - a transitional measure in the Capital Requirement Regulation (CRR) - in MREL which is a permanent requirement.

As a general rule, these backstop measures (such as the transitional Basel 1 floor and the leverage ratio which is not yet binding) may be taken into account when setting the loss absorption amount but should not be automatic. We would recommend putting point d) and e) in a separate paragraph, making clear that they are a backstop rather than a primary determinant for MREL.

Q2. Should paragraph 5 refer only to the resolution authority *increasing* the loss absorption amount, rather than *adjusting* it? Are there specific circumstances under which resolution authorities should allow a smaller need to be able to absorb losses before entry into resolution and in the resolution process than indicated by the capital requirements (for example due to the use of national discretions in setting capital requirements)?

First, we agree that "adjusting" is the right approach as the requirement under Article 45 of the BRRD refers to MREL being determined by the resolution authority based on EBA criteria, whereas restricting to "increasing" would amount to the EBA setting a minimum. Resolution authorities should have the discretion to either reduce or increase MREL. One specific scenario where the level 1 BRRD text seems to suggest that loss absorption amount could be lowered is if there is clearly a wider availability of eligible liabilities that can feasibly and credibly be bailed in, beyond MREL.

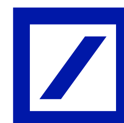
We suggest including the following paragraph: "The resolution authority shall assess whether eligible liabilities other than those qualifying for MREL will feasibly and credibly be available at the point of resolution, and adjust the loss absorption amount accordingly."

Second, we are concerned with the current wording of paragraphs 4 and 5 of the draft RTS, which seems to imply that the resolution authority can essentially revise the competent authority's assessment of a firm's capital requirements without their consent. This is at odds with the statement in the background that the resolution authority should not act "as a shadow supervisor".

The RTS should be clear that the resolution authority is not judging the adequacy of capital requirements - that is the supervisor's role - but rather reviewing them to consider whether adjustments to the loss absorption amount under MREL are necessary. This would clarify the division of tasks and highlight that supervisors remain best placed to assess capital requirements which have been calibrated to take into account potential losses.

We therefore suggest deleting paragraph 4 (or replacing with the additional paragraph outlined above) and reformulating paragraph 5 to say: "If the resolution authority considers, as part of the resolvability assessment, that the capital requirements and eligible liabilities assessed as feasible and credible to absorb losses are not sufficient to ensure the effectiveness of the resolution strategy, then the resolution authority should consult the competent authority and adjust the loss absorption amount, if they consider it is necessary and proportionate to do so."

For the same reason, paragraph 6 should also specify "in accordance with the EBA RTS on resolvability assessments and guidelines on measures to remove impediments" to



ensure the process involving the supervisor and conditions to apply measures only where necessary and proportionate as set out in those detailed rules are respected and followed.

Q3. Should any additional benchmarks be used to assess the necessary degree of loss absorbency? If yes, how should these be defined and how should they be used in combination with the capital requirements benchmark? Should such benchmarks also allow for a decrease of the loss absorption amount compared to the institution's capital requirements?

As outlined above, we believe that firms are likely to have significant amounts of capital and CET1 remaining when the decision is taken to resolve the bank and much more bail-in capacity than only that from MREL. As such, the use of stress test scenarios could be useful to inform the calibration of MREL as they will help to estimate losses and what is realistically likely to be available for bail-in under severe stress. However, we caution against using stress test scenarios as an automatic determinant for MREL.

Q4. Do you consider that any of these components of the overall capital requirement are not appropriate indicators of the capital required after resolution, and if so why?

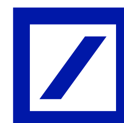
We support that the resolution authority should consider the amount that needs to be recapitalised when determining MREL, but that does not automatically mean the recapitalisation should be at least equal to the capital requirements necessary for the entire group's authorisation. Instead, the resolution authority should consider an appropriate recapitalisation level for on-going authorisation post-resolution and upon implementation of the specific resolution plan, taking into account the overall circumstances of the institution at the point of resolution.

For example, at the point of failure, it is very unlikely that all capital would have been exhausted. Past experiences show (and new recovery rules require) that problems in banks will have to be dealt with long before losses grow to a size large enough to consume all equity in a bank. With enhanced capital levels, in order to reach the point of failure G-SIBs will have to be severely weakened by an on-going crisis and will have already executed recovery measures such as deleveraging or disposals. In addition, it is likely that authorities will already be exercising early intervention powers. As a result, the bank's balance sheet will be smaller and risk weighted assets lower at the point of resolution, therefore requiring a smaller recapitalisation level.

The resolution authority needs to bear this in mind when determining MREL. The draft RTS already go some way towards recognising this in paragraph 3, but this should be more closely linked to the recovery and resolution plan and the likely future shape of the institution. Paragraph 3 should therefore be amended as follows:

- a) "**the recovery plan or** the resolution plan identifies, explains, and quantifies a change in the denominator"; and
- Point c: "for **institutions not expected to remain G-SIBs at the point of resolution**"

Likewise, there is no reason that this approach for the denominator should not be replicated for the numerator. As such, we recommend amending paragraph 5: "The



recapitalisation amount shall be at least equal to the capital requirements necessary to comply with the conditions for authorisation after the implementation of the preferred resolution strategy, **unless all of the following circumstances are met:**

- **a) the recovery plan or the resolution plan identifies, explains and quantifies a change in the numerator; and**
- **b) the above change is considered in the resolvability assessment to be both feasible and credible to provide additional eligible liabilities able to contribute to recapitalisation; and**
- **c) for institutions not expected to remain G-SIBs at the point of resolution."**

Furthermore, in paragraph 6, in terms of capital requirements after resolution, we do not believe buffers should be included as they are not likely to be relevant once a firm enters resolution (as outlined in our response to Q1). Similarly, backstop measures such as the Basel 1 floor and the leverage ratio could be taken into account but should not be binding for determining the recapitalisation amount.

Finally, while we understand the desire for a "buffer" above minimum authorisation requirements to restore market confidence, we do not think it will always be necessary given the broader availability of remaining CET1 and other bail-in eligible liabilities beyond MREL. Where it is considered necessary, rather than basing it on the higher of the combined buffer requirements or automatically set through a peer group comparison, we believe it should be based on a flat buffer for all banks, which would be informed by a peer group analysis, as outlined below.

Q5. Is it appropriate to have a single peer group of G-SIIs, or should this be subdivided by the level of the G-SII capital buffer?

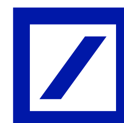
Should the peer group approach be extended to Other Systematically Important Institutions (O-SIIs), at the option of resolution authorities? If yes, would the appropriate peer group be the group of O-SIIs established in the same jurisdiction?

Should the peer group approach be further extended to other types of institution?

Although we understand the need to ensure market confidence, we do not support the idea of an automatic peer group approach, which is a circular reference with an ever increasing effect. For instance, if a bank has its MREL increased as a result of the peer group comparison, it may meet that by increasing its CET 1. This means each increase will lead to a new assessment which will lead to an automatic increase. This is not necessarily desirable from a market point of view. Indeed, it would be a race to the top not justified on objective grounds but merely as a side effect of the design of MREL. We therefore think that a flat buffer (e.g. 1.5% per article 27 of the BRRD) would be more appropriate. This could be reviewed annually, informed by a peer group comparison.

Such a peer group approach - if designed appropriately as outlined above - should apply to all institutions rather than only to G-SIBs. However, such a peer group comparison should be done between banks with similar business models. Different banks fund themselves differently so it is important to be cautious when identifying a group of peer banks. We would recommend that the EBA clarifies this in the draft RTS.

As noted above in our answer to Q4, we do not believe the combined buffer requirement is relevant for resolution given that buffers are designed to be used in periods of stress, it



is unlikely that at the point of resolution a failed bank would still be a G-SIB, or that an institution in resolution will be seeking to make distributions.

Q6. The approach outlined in Articles 2 and 3 will reflect differences between consolidated and subsidiary capital requirements. Are there additional ways in which specific features of subsidiaries within a banking group should be reflected?

It is not clear how exactly Article 2 and 3 reflect the specific features of subsidiaries within a banking group. In particular, we do not think the draft RTS sufficiently take into account the interaction with the preferred resolution strategy (Single Point of Entry (SPE) or Multiple Points of Entry (MPE)). For banks with a SPE strategy, where the parent company is the resolution entity, MREL will usually be set primarily on a group consolidated basis; while for MPE, MREL will be required primarily on a solo basis in the relevant subsidiaries.

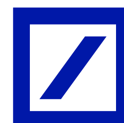
Resolution authorities should therefore also take into account cross border agreements between home and host authorities when defining MREL. The host authority might want to waive the local MREL requirement because it is confident that the consolidated MREL will cover subsidiaries. On the other hand, the home authority might waive the consolidated requirement on the basis that subsidiaries would be covered already. We would recommend adding a paragraph in both Articles 2 and 3 stating that "the resolution authority shall take into account the preferred resolution strategy and potential cross border agreements between home and host authorities when defining MREL". It might also be worth clarifying that it is the local resolution authority that decides on local MREL requirements.

Finally, if combined buffers requirements are used to determine either the loss absorption amount or recapitalisation amount in the final RTS, this should be clarified to only apply at the group level. In other words, the MREL for subsidiaries should be set on a standalone basis, and buffers should only be required if relevant to the subsidiary (e.g. whether if it is considered as Other Systemically Important Institution domestically or not).

Q7. Do you agree that there should be a de minimis derogation from this provision for excluded liabilities which account for less than 10% of a given insolvency class?

We strongly support the EBA's effort to ensure that the "no creditor worse off" principle is respected and we believe that Article 5 goes in the right direction. The resolution authority should have this principle in mind during the whole process of determining MREL.

We agree that the authority should be able to adjust the amount of MREL to take into account the potential exclusions, as per Article 45 paragraph 6 point c) of the BRRD. However, we disagree with the suggestion in Box 2 of the background and rationale that the authority could require MREL to be met using subordinated instruments. This is at odds with the clear focus of the BRRD bail-in regime on senior unsecured liabilities and would have a significant impact on European banks if required for MREL, as outlined in the EBA's own impact assessment. While resolution authorities have powers under the BRRD to require contractual bail-in instruments, no such explicit power exists to require subordination. The final RTS should avoid suggesting this.



Regarding the de minimis derogation for excluded liabilities which account for less than 10% of a given insolvency class, examining the overall impact of exclusions will indeed be necessary for the RTS to be aligned with the EBA's guidelines on differential conversion rates. However, we do not believe there is a clear justification for establishing the threshold automatically at 10%. The amount of liabilities likely to be excluded will vary significantly between banks and business models, as will the potential impact on whether the "no creditor worse off" principle is at risk of being breached.

Instead of an arbitrary threshold, paragraph 3 should require the resolution authority to quantify this risk as far as possible and point b) should specify: "the amount of liabilities identified totals a material amount of any one class of liabilities such that it gives rise to potential risks to the no creditor worse off principle". Paragraph 4 should then be amended to read: "The resolution authority shall assess whether the MREL **and other eligible liabilities are** sufficient to ensure that the amount identified pursuant to paragraph 3 can be **credibly and feasibly** absorbed by instruments which are (i) **eligible for bail-in** and (ii) are not excluded **in accordance with paragraph 1**, without breaching…etc".

Q8. Do you agree that resolution authorities should seek to ensure that systemic institutions have sufficient MREL to make it possible to access resolution funds for the full range of financing purposes specified in the BRRD?

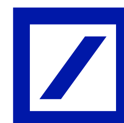
While we agree that resolution authorities should seek to quantify how the overall resolution strategy may require use of resolution funds in bail-in, we believe that the EBA should be cautious when drafting the RTS.

The aim of resolution planning is to ensure losses can be absorbed by the bank' shareholders and creditors, avoiding reliance on the resolution fund for bail-in. Resolution funds are not primarily meant to provide capital and should be used for bail-in only under very specific and extreme circumstances. It is very unlikely that G-SIBs in particular would ever use the resolution fund given that they would have a very large amount of liabilities available for bail-in, particularly once TLAC requirements are in place. If anything, other banks – such as those without large wholesale debt in issuance – would be more likely to use the resolution fund.

In addition, as outlined under Q4, G-SIBs will have changed tremendously at the point of failure. They will have a smaller balance sheet and reduced risk weighted assets, especially if several recovery options have been executed prior to resolution. The bank therefore is unlikely to be a G-SIB anymore after resolution due to large losses before bail-in is applied and important recovery measures taken.

Therefore, we would recommend the following changes to Article 7 of the draft RTS:

- Paragraph 1 should specify that this article applies to any institution subject to MREL if they are likely to use the resolution fund: "**For any institution subject to MREL**, the resolution authority shall assess whether the **resolution plan may result in the use of the resolution fund in bail-in and if so whether** MREL **and other eligible liabilities are** sufficient to permit the requirements set out in Article 44 of Directive 2014/59/EU governing a contribution to loss absorption by the resolution financing arrangement to be met".



- Paragraph 2 should also be amended to be less automatic and more flexible, so that it is proportionate to the likelihood of using the fund for bail-in and the specificities of the individual banks:
    - a) should read "there are no **material** impediments to a feasible and credible resolution without a contribution to **bail-in** from the resolution financing arrangement"
    - b) we believe that the term 'plausible' is too vague and subjective. We would suggest instead: "There are no **likely** circumstances in which a contribution from the resolution financing arrangement would be necessary to avoid a breach of the safeguards provided in Title IV Chapter VII of Directive 2014/59/EU"
    - c) 'only' should be replaced by 'mainly': "the preferred resolution strategy assumes that losses are absorbed **mainly** by liabilities […]"
    - A paragraph d) should be added stating "**there are sufficient eligible liabilities that are feasible and credible to bail-in to support the conclusions under a) and b)**".

Q9 and 10. Is this limit on the transition period appropriate? Should the resolution authority also set a transitional period for the MREL of banks which are undergoing or have undergone a resolution process?

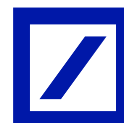
As for all capital frameworks (such as the Capital Requirement Directive and Regulation – CRD IV/CRR; or the TLAC), a phase-in period is very important to mitigate the potential impact on the bank's on-going business. As MREL is tailored to the individual bank's specific profile, the transition period should also be suitably calibrated, to take into account the specific situation of each bank.

Moreover, we believe it is appropriate to allow a transitional period during or after the resolution process, depending on the resolution outcome. According to Article 41 of the BRRD, the bridge institution can be waived from complying with the requirements of certain directives (CRD IV and MIFID II) for a short period of time. The same logic should be applied as regards to the restoration of MREL after a bank fails. An additional paragraph 4 could be therefore added to Article 9: "the resolution authority may decide to allow a longer transitional period for the restoration of MREL of banks which are undergoing or have undergone resolution."

Q11. Overall, do you consider that the draft RTS strikes the appropriate balance between the need to adapt the MREL to the circumstances of individual institutions and promoting consistency in the setting of adequate levels of MREL across resolution authorities?

With these RTS, the EBA determines criteria that are appropriate and relevant to the setting of MREL. To ensure that the specificities of each institution are really taken into account:

- First, loss absorption and recapitalisation should be viewed jointly, as part of a continuum of overall loss-absorbing capacity. This would guarantee proportionality while providing a harmonised framework for resolution authorities at EU level.



- We also recommend clarifying that competent authorities are best placed to determine whether capital requirements are adequate for loss absorption and allowing adjustments to the recapitalisation amount as required based on the resolution plan
- Another crucial element would be to look at exclusions from bail-in on a bank-by-bank basis, and to take into account preferred resolution strategies when determining MREL and how it applies to groups and to subsidiaries.
- Additionally, we think it would be helpful if the EBA could clarify how “total liabilities” should be calculated in order to determine MREL. The phrase “total liabilities” is used in several places in the BRRD with different meanings. The European Commission, in its delegated acts on resolution funding, has clarified its understanding of ‘total liabilities’ with respect to contributions to resolution funds. The EBA could do the same here to ensure a harmonised approach across the EU. Given the variation in accounting regimes and differences between national regimes and IFRS, this clarification would be useful. This is particularly the case with regards to derivatives, given the variation in their accounting treatment. There is also an asymmetry between the denominator and the numerator when calculating MREL which should be addressed, and between the calculation of MREL and the requirement to bail-in 8% of ‘total liabilities’ before the resolution fund can contribute in bail-in. As solution would be to calculate derivatives under total liabilities in all circumstances relating to MREL in line with the leverage exposure method, as under the resolution financing calculation method.