MFSA MALTA FINANCIAL SERVICES AUTHORITY

Circular

17th October 2019

Circular to Institutions on a new CRR Requirement

This Circular shall apply to all institutions that do not fall within the remit of the Single Resolution Board in terms of Article 7(2) of Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010.

The objective of this Circular is to inform all institutions subject to minimum requirement for own funds and eligible liabilities ("MREL") decision of a regulatory change introduced through "the Banking Package"[1]. Particularly, this Circular focuses on the new article 78a of the CRR2. This new amendment became immediately applicable as of 27th June, 2019.

Therefore, as from 27 June 2019, all institutions subject to an MREL decision, are obliged to seek the approval of the Resolution Committee. Such permission must be sought prior to calling, redeeming, repaying or repurchasing eligible liabilities instruments defined under article 72b CRR2, comprising those which have a residual maturity of less than one year, before they reach their contractual maturity.

The CRR2 has introduced two categories of permissions regimes to be issued by the Resolution Committee: (a) an instrument-by-instrument permissions regime; and (b) a general prior permissions regime. With respect to the general prior permissions, institutions can effect calls, redemptions, repayments or repurchases of eligible liabilities instruments for a predetermined amount set by the Resolution Committee and for a specified period not exceeding one year, subject to the fulfilment of certain conditions specified in CRR2. The general prior permissions granted by the Resolution Committee may be renewed accordingly.

[1] Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements, and Regulation (EU) No 648/2012 ("CRR2"); Directive (EU) 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures ("CRDV"); Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 amending Directive 2014/59/EU as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms and Directive 98/26/EC ("BRRD2"); and Regulation (EU) 2019/877 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 806/2014 as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms ("SRMR2").

The requirement to obtain prior approval of the Resolution Committee lies with institutions with MREL decisions higher than the loss absorption amount ("LAA"). With respect to institutions with an MREL shortfall, the Resolution Committee can grant its approval only in instances where the eligible liabilities instruments are replaced by other eligible liabilities instruments or own funds. Reduction of eligible liabilities instruments without replacing such instruments is not permitted unless institutions exceed their MREL requirement by a margin prior to the reduction.

The granting of permission is not automatic but requires the submission of an application by an institution to the Resolution Committee specifying the type of permission being sought. The aforementioned application must contain the details stipulated in Appendix 1. The details provided under Appendix 1 highlight the main aspects which contribute to the successful granting of permission and indicate which documentation is required in support of the application and the time-limits.

In terms of the new article 78a of the CRR, the Resolution Committee shall withdraw the general prior permission in instances where an institution violates any of the conditions or criteria provided for in relation to the permission.

In line with the approach taken by the Single Resolution Board, as a provisional measure, institutions are not required to seek prior permission to perform market activities in own eligible liabilities instruments until the 31st day of December 2019. Such transitional arrangement is only applicable provided that the conditions set out in Appendix 1 are satisfied. As from 1st January 2020 institutions are required to obtain an instrument-by-instrument approval or a general prior permission in order to continue performing market making or other secondary market activities in own eligible liabilities.

Lastly, the CRR2 has also mandated the European Banking Authority ("EBA") to develop draft regulatory technical standards to address a number of elements and to present them to the European Commission by 28th December, 2019. This Circular may therefore be subject to revision following the publication of the EBA Guidelines.

All enquires related to this matter should be submitted electronically via the email address: resolution.policy@mfsa.mt

APPENDIX 1

Application under Article 78a CRR2

Submission date

All effected institutions are to submit their completed application to the Resolution Committee, at least four months prior to the date of the intended performance of the action of calling, redeeming, repaying or repurchasing (individually and collectively referred to as "Actions").

Contents of the application

The submitted application must provide the following information:

(1) Specification of the legal basis for the application being submitted. Such specification must clearly indicate whether permission is being sought under Article 78a(1)(a) or (b) or (c) or second subparagraph of Article 78a of the CRR2);

(2) A thorough explanation of the rationale for performing the Action in question;

(3) Information on MREL planning which cover, as a minimum, the next three years particularly: (a) the level of eligible liabilities before and after the Actions; and (b) the impact of the Actions on the applicable MREL requirements;

(4) In relation to the replacement of eligible liabilities instruments (Article 78a(1)(a) CRR2): (a) information on the residual maturity of the replaced instrument and the maturity of the replacement instrument; (b) the ranking in the creditor hierarchy (under article 29A of the Banking Act) of the replaced and the replacement instrument; (c) the cost of the replacement instrument; and (d) the impact of replacing eligible liabilities on sustaining the profitability of the institution;

(5) In relation to an Action under Article 78a(1)(c) of the CRR2, the applicant institution must demonstrate that the eligible liabilities with own funds instruments are partially or fully replaced in order to ensure compliance with own funds requirements laid down in CRR and under Directive 2013/36/EU[2] for continuing authorisation; and

(6) Any other information which may be deemed relevant for the purposes of assessing the appropriateness of granting a permission in terms of Article 78a of the CRR2.

Representation

[2] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC

The application shall be signed by a person who is vested with legal representation of the institution and shall include a statement that the information given is valid and accurate. Moreover, the institution is responsible to update its application with information it has provided and/or commits to provide additional information that the Resolution Committee may demand in order to ensure that the application is comprehensive.

Market making and other secondary market activities

In an attempt to avoid interruption of these activities in an interim period until an institution can obtain approval for Actions performed in market making and other secondary market, prior permission is not a requirement in the case of market making and other secondary market activities, provided that:

i. There activities are carried out during an interim period from 27th June 2019 to 31st December 2019;
ii. The aggregate trading volume in these activities during this interim period does not exceed 1% of the total consolidated risk exposure amount ("TREA") on a consolidated basis at the level of the resolution group; and
iii. Any MREL shortfall or increase which results from such activities has been compensated with eligible liabilities instruments on a quarterly basis.

In order to continue carrying out such activities as of 1st January 2020 without obtaining instrument-by-instrument approval, institutions shall obtain a general prior permission from the Resolution Committee.

The Resolution Committee may consider granting prior permission to institutions for market making and other secondary market activities notwithstanding the existence of MREL shortfall provided that any temporary shortfall or increase thereof which may have been created as a result from these activities, is compensated on a quarterly basis. The Resolution Committee shall re-assess the restriction of 1% TREA for market making on the basis of the experience earned in the course of the abovementioned interim period.