Adequacy of loss-absorbing capacity of global systemically important banks in resolution

Comments of the Polish Financial Supervision Authority

The Polish Financial Supervision Authority welcomes the FSB’s proposal on the adequacy of loss-absorbing capacity of global systemically important banks in resolution. For a country where many of the banks are subsidiaries of G-SIBs it is of crucial importance to have efficient tools applicable in the time of crisis. The European solution is provided by the Bank Recovery and Resolution Directive, but at it is limited in scope only to institutions established in the Union the FSB’s proposal is still important for achieving stability of global financial market.

The FSB’s proposal differs in some aspects from the European one, but the core of the proposal and main assumptions remain the same. Overall assumptions are therefore generally right, but the following issues need to be raised:

1. The proposal introduces a unique concept of external and internal TLAC. There is also a requirement to have a prepositioned internal TLAC in material subsidiaries introduced in order to increase confidence of host authorities. This requirement itself is a good one, but there seems to be misunderstanding of host authorities’ concerns which leads to wrong conclusions. For the local authority it is the stability of the local market and local economy that is a matter of concern. It is usually their statutory duty to take care of the local financial market. From this standpoint it is irrelevant whether some company is significant for the group or not. The only thing that matters is its significance for the local economy. Therefore unless the determination of the companies which are to be required to hold internal TLAC is based on the local authorities determination of domestic systemic importance, the confidence of host authorities cannot be achieved.

It should also be possible, in some cases, to require the internal TLAC to be at the level of 100% of the level that would be necessary if the entity were the separate resolution entity. It is then also very important to emphasize the statement made in the term sheet in part devoted to internal TLAC that the host authorities can increase this requirement if needed.
2. The proposed level for the TLAC requirement seems to be a good starting point. Although some common minimum threshold is a concept distinct from the one adopted in BRRD, it has some advantages. It needs to be noted though, that the RWA- based requirement has a deficiency stemming from the lack of comparability in RWA calculations. It seems to be possible now, that some bank due to increased capital levels would seek risky activity that would increase its profitability without formally increasing risk weights. In the end, it could happen that such a bank does not have the level of capital/eligible liabilities at the level allowing to offset the underlying risk.

3. The question of capital buffers and their treatment is definitely an important one. Putting the buffers on top of the TLAC requirement has the advantage of creating a coherent framework that supports building up a cushion that could not only protect the bank from breaching capital requirement but also from breaching the required MREL level. It is though very important to consider carefully the transitional period when the banks would be required to work towards fulfillment of both these requirements.