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CROATIAN NATIONAL BANK'S APPROACH TO SETTING THE MINIMUM REQUIREMENT FOR OWN FUNDS AND ELIGIBLE LIABILITIES

1 Initial provisions

- 1.1 The minimum requirement for own funds and eligible liabilities (hereinafter: minimum requirement, MREL) is the minimum amount of own funds and eligible liabilities that ensures that a credit institution is capable of absorbing an adequate amount of losses and, depending on the resolution strategy, being recapitalised by an amount sufficient to implement the preferred resolution strategy and achieve resolution objectives.
- 1.2 The Council of the Croatian National bank sets the minimum requirement for a credit institution that is not part of a group or for an EU group of credit institutions that is not a cross-border group and for which the Croatian National Bank is the group-level resolution authority.
- 1.3 The Croatian National Bank participates in the procedure of adopting a joint decision on the minimum requirement on a consolidated basis. The Croatian National Bank draws up a proposal for the minimum requirement on an individual basis for a subsidiary having its head office in the Republic of Croatia (RC) that is part of an EU group. The Croatian National Bank may also draw up a proposal for the minimum requirement on a sub-consolidated basis for an RC group that is part of an EU group. In conformity with the adopted joint decision, the Croatian National Bank may request that the minimum requirement be maintained on an individual or sub-consolidated basis.
- 1.4 If so requested, the credit institution is obliged to continuously meet MREL both on an individual basis and a sub-consolidated/consolidated basis.
- 1.5 MREL is set in accordance with the provisions of *Commission Delegated Regulation (EU) 2016/1450 of 23 May 2016 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodology for setting the minimum requirement for own funds and eligible liabilities (Text with EEA relevance)* (SL L 237, 3. 9. 2016.; hereinafter: *Delegated Regulation on MREL*).

2 Minimum requirement for own funds and eligible liabilities

- 2.1 When setting total minimum requirement the amount required to ensure the absorption of losses (hereinafter: loss absorption amount) is determined separately from the amount required, where necessary, to continue to comply with the conditions related to authorisation or to ensure the continuity of critical functions, in accordance with the

preferred resolution strategy (hereinafter: recapitalisation amount). The loss absorption amount is set on the basis of the credit institutions' current capital requirements, with a possibility to determine an amount that is higher or lower than the regular capital requirements based on an assessment of the resolution authority. The recapitalisation amount equals the amount required to meet the applicable capital requirements necessary to comply with the conditions related to authorisation after the implementation of the preferred resolution strategy and to sustain market confidence.

- 2.2 The MREL level is directly linked to the selected resolution strategy and the selected resolution tool planned to be applied in the resolution of a credit institution.
- 2.3 The credit institution being resolved by applying open bank bail-in tool must, in addition to an adequate amount to absorb the expected losses in resolution, continuously maintain an adequate amount to restore its Common Equity Tier 1 ratio to a level sufficient to maintain the capital requirements for authorisation and sustain sufficient market confidence after the resolution.
- 2.4 The recapitalisation amount for credit institutions for which the selected resolution strategy is that of ensuring the continuity of critical functions by transferring these functions to another credit institution or a bridge institution must be sufficient only to absorb the increase in the capital requirements of the recipient of a part of assets and liabilities of the institution under resolution deriving from the risk-weighted assumed part of assets, which may not be lower than 5% of the amount of liabilities transferred.
- 2.5 MREL for credit institutions for which it is established in the course of the resolvability assessment that their bankruptcy proceedings are feasible and credible consists only of the loss absorption amount that does not exceed the credit institution's total capital requirements.

3 Determining the loss absorption amount

- 3.1 The Croatian National Bank determines the loss absorption amount based on the default amount according to Article 1 of *Delegated Regulation on MREL*. The binding leverage ratio requirement will not be taken in the account in the calculation until it comes into force. The Basel I floor according to Article 500 of Regulation (EU) No 575/2013¹ (hereinafter: *Regulation (EU) 575/2013*) has not been in force since 31 December 2017 and is therefore also not taken into account in the calculation.
- 3.2 The Croatian National Bank does not make any additional adjustments to the default loss absorption amount.
- 3.3 The loss absorption amount is determined applying the credit institution's total risk exposure on an individual basis.

¹ REGULATION (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND THE COUNCIL of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Text with EEA relevance) (SL L 176, 27. 6. 2013.)

4 Determining the recapitalisation amount

- 4.1 The Croatian National Bank determines the recapitalisation amount based on the default amount according to Article 2 of *Delegated Regulation on MREL*. The binding leverage ratio requirement will not be taken in the account in the calculation until it comes into force. The Basel I floor according to Article 500 of *Regulation (EU) No 575/2013* has not been in force since 31 December 2017 and is therefore also not taken into account in the calculation.
- 4.2 The recapitalisation amount also includes any additional amount necessary to sustain market confidence after the resolution. The default additional amount equals the combined buffer requirement.
- 4.3 In the case of application of the bail-in tool, the recapitalisation amount is determined applying the credit institution's total risk exposure on an individual basis.
- 4.4 In the case of application of the instrument of partial transfer of assets or liabilities to a purchasing credit institution or a bridge institution, the recapitalisation amount is determined applying the assessed risk exposure of the part of assets subject to the transfer.
- 4.5 The recapitalisation amount for the credit institution whose bankruptcy proceedings are feasible and credible equals zero. The Croatian National Bank determines the recapitalisation amount for credit institutions the resolution of which is necessary in public interest.

5 Adjustments to the recapitalisation amount

- 5.1 The Croatian National Bank adjusts the required recapitalisation amount in the part relating to the adjustment to additional capital requirements under Pillar II, the adjustment to the additional amount necessary to sustain sufficient market confidence and the adjustment to the expected total risk exposure after the resolution.
- 5.2 The adjustment to additional capital requirements under Pillar II in accordance with the expected general risk profile of the credit institution after its resolution involves a 50% reduction in current additional capital requirements under Pillar II.
- 5.3 The adjustment to the additional amount necessary to sustain sufficient market confidence whose default amount equals the combined buffer requirement involves retaining only the capital conservation buffer.
- 5.4 The adjustment to the expected total risk exposure after the resolution involves reducing the total risk exposure by the total loss absorption amount.

6 MREL for a group of credit institutions

- 6.1 An EU parent institution having its head office in the Republic of Croatia is also required to maintain MREL on a consolidated basis for its group.
- 6.2 The Croatian National Bank may also set MREL on a sub-consolidated basis for an RC group of credit institutions that is a part of an EU group. The Croatian National Bank sets MREL on a sub-consolidated basis for a group of credit institutions having an RC subsidiary designated as the point of entry to the resolution of an RC group of credit institutions.
- 6.3 MREL on a sub-consolidated/consolidated basis is set as specified in items 3, 4 and 5 herein. By way of exception from item 3.3, the loss absorption amount is determined applying the total risk exposure of the credit institution on a sub-consolidated/consolidated basis. By way of exception from item 4.3, the recapitalisation amount is determined applying the total risk exposure of the credit institution on a sub-consolidated basis that includes only the group members having head offices in the European Union for which bankruptcy proceedings are neither feasible nor credible.

7 Additional adjustments to total MREL

- 7.1 The Croatian National Bank may increase total MREL if it establishes in the resolution planning process that some MREL eligible liabilities will be excluded from the write down or conversion for a reason justified by at least one of resolution objectives (e.g. ensuring the continuity of critical functions or avoiding a major adverse effect on the financial system by preventing contagion).
- 7.2 The Croatian National Bank may increase total MREL for other systemically important institutions to ensure that write down and conversion amounts are sufficient to meet the conditions for access to the resolution fund.
- 7.3 The Croatian National Bank may decrease total MREL in accordance with the expected amount of deposit guarantee scheme contributions for the financing of the selected resolution strategy.

8 Overall MREL assessment

- 8.1 Total MREL consists of the sum of the loss absorption amount and the recapitalisation amount plus potential additional adjustments to MREL.
- 8.2 MREL for credit institutions is expressed as a percentage of total liabilities and own funds (TLOF), with derivative liabilities included on the basis that full recognition is given to counterparty netting rights and that derivative liabilities are determined in their net amount. MREL on an individual basis is expressed in relation to individual total

liabilities and own funds. MREL on a sub-consolidated/consolidated basis is expressed in relation to sub-consolidated/consolidated total liabilities and own funds of an RC group.

- 8.3 The Croatian National Bank may determine that MREL be binding or indicative.

9 Subordination of MREL instruments

- 9.1 The Croatian National Bank may require that MREL on a consolidated, sub-consolidated or individual basis be partly met by subordinated claims. Subordinated claims are claims subject to an agreement between the creditor and the credit institution providing that the creditor in bankruptcy proceedings will be compensated after all other higher and lower priority level creditors.
- 9.2 The Croatian National Bank may require from the credit institution to partly meet MREL by subordinated claims if it assesses that there is a risk that the need for the absorption of losses and recapitalisation by liabilities that qualify for inclusion in MREL and are not excluded from the absorption of losses and recapitalisation could lead to a breach of the no creditor worse off principle (NCWO).
- 9.3 The Croatian National Bank may also require from a credit institution to partly meet MREL by subordinated claims if it assesses that there are major impediments to the resolution that threaten the feasibility of the resolution strategy and could be removed by means of subordinated MREL claims.

10 MREL eligible instruments

- 10.1 MREL is met by the instruments of own funds and eligible liabilities that meet the criteria specified in Article 24 of the Act on the Resolution of Credit Institutions and Investment Firms (OG 19/2015).
- 10.2 The credit institution's MREL on an individual basis is met by the credit institution's own funds and eligible liabilities on an individual basis.
- 10.3 MREL for a group is met by the consolidated/sub-consolidated own funds of the group of credit institutions and the eligible liabilities of the parent company of an EU group of credit institutions having its head office in the Republic of Croatia or the eligible liabilities of an RC subsidiary having its head office in the Republic of Croatia designated as the point of entry to the resolution of an RC group of credit institutions.

11 Deadline for meeting MREL

- 11.1 The decision on MREL is made in parallel with the drawing up and revision of the resolution plan and constitutes its integral part.
- 11.2 The Croatian National Bank may also determine an appropriate transitional period to reach the final MREL. In addition to determining the transitional period, which must be as short as possible, the Croatian National Bank also communicates to the credit institution a planned MREL for each 12 month period during the transitional period.
- 11.3 A constituent part of the decision on MREL referred to in item 11.1 is deadline by which a credit institution must meet MREL and the planned level of the requirement for each 12 month period.
- 11.4 The decision on MREL is revised regularly and updated if necessary, at least within the regular resolution planning process.

12 Final provisions

- 12.1 In accordance with amendments to the legislative framework for resolution planning, the setting of MREL and the eligibility of liabilities for inclusion in MREL, the Croatian National Bank will alter the approach to setting MREL to the extent necessary.