

Finansinspektionen (Swedish Financial Supervisory Authority) and Riksgälden's (Swedish National Debt Office) response to the FSB consultative document on TLAC

Finansinspektionen and Riksgälden strongly support the overriding objectives of the TLAC proposal. As regards the further development we would like to state a couple of priorities we believe need to be considered in order to ensure that the framework will **achieve its intended objectives** and **minimise unintended consequences**.

It is a key priority for us to ensure that the framework will not be **excessively rigid** in a crisis, while ensuring **strong incentives for banks** and **effective powers for the relevant authorities**. This will serve to avoid unintended consequences and the exacerbation of systemic liquidity issues, as well as to ensure that the framework can be applied also in situations characterised by severe and extended market dislocation. We believe this will be crucial in order to deliver a framework which is credible and sustainable.

In this regard we consider it imperative that the TLAC framework **does not accelerate the point of resolution**. While we understand that this is not the intention, we note that **principle 10** and section 7 of the term sheet require that a breach of the TLAC minimum (at which point the combined capital buffer will be zero given the TLAC framework, irrespectively of the bank's capital position) should be treated **as severely as a breach or likely breach of minimum capital requirements**. This may be seen to **significantly accelerate the implementation of resolution action** (especially in jurisdictions, such as the EU, where "failing or likely to fail" is more strongly linked to breaches of minimum capital requirements¹).

For this reason, we believe that **the reference to breaches of minimum capital requirements in principle 10 should be removed**². A more flexible approach is required in order to allow the authorities to differentiate their actions depending on the

¹ See Consultation Paper on Draft Guidelines on failing or likely to fail, EBA/CP/2014/22, 22 September 2014.

² Note that this would also be in line with the FSB Key Attributes on entry into resolution, see paragraph 3.1 Entry into Resolution, Key Attributes of Effective Resolution Regimes for Financial Institutions, FSB, 15 October 2014.

cause of the breach. For example, while it may be reasonable to treat a breach of the TLAC minimum caused by credit losses as severely as a breach of minimum capital requirements, it may not be reasonable to treat a breach caused by re-financing problems in a corresponding manner – particularly if the causes of such problems are non-idiosyncratic in nature.

It may be argued that a more flexible approach increases the risk that the banks' loss absorption capacity will be depleted at the point of resolution. We would however argue that this risk is mitigated by the requirement that TLAC-eligible instruments must have a remaining maturity of at least one year. Even if a bank is unable to refinance its maturing TLAC instruments – and therefore breaches TLAC – it will still maintain its loss absorbing capacity for one year (all else being equal).

An **alternative and more flexible approach** would be for principle 10 to define a breach of the TLAC minimum as a **serious obstacle to resolvability** and require appropriate and effective powers to ensure its removal. In the case where the relevant authorities deem that an institution meets the conditions for resolution after the TLAC requirement is breached, nothing should of course prevent them from initiating resolution as appropriate. As indicated above, resolution action would not, however, be an appropriate response where breaches result from systemic funding issues in the market which are not idiosyncratic to a particular institution. Rather than enhancing financial stability we believe that principle 10 as it is currently stated may impact financial stability negatively.

In addition, regardless of whether a breach of TLAC is treated as an obstacle to resolvability (which we prefer) or as a breach of minimum capital requirements (which we do not favour), we believe that in order to ensure that the gone-concern perspective is properly taken into account, the TLAC framework should explicitly require that resolution authorities (if different from the supervisor) should be closely involved in the decision on what measures breaches should result in.³

As a final remark, we also note that while the proposal that **the TLAC minimum must be met before any CET1 capital is available to meet the combined buffer** is a constructive and powerful incentive for banks to avoid breaches, it may also make breaches of the buffers more likely as a failure to refinance a TLAC instrument would trigger the redistribution of CET1 from the buffer to the TLAC requirement. Notably, the proposal could make it more difficult to raise the highest-quality forms of capital, for which distributions are discretionary and consequently subject to the issuer meeting the

³ This provision is of importance in jurisdictions where the resolution authority does not have the powers associated with the resolvability assessment.

combined buffer. An inability to raise high-quality capital may in turn make it more difficult to raise other forms of TLAC-eligible debt and thereby trigger a vicious circle. Consequently we would suggest that the relevant authority should be able to **temporarily suspend this requirement**, under **certain conditions**. Such conditions should notably include situations where the capital requirements, including the buffer, are met, where the institution is deemed to be fully cooperating with authorities in remedying the breach, and when access to liquidity is systemically distorted.

Principle 10 – Alternative drafting suggestion:

10. A breach or likely breach of Minimum TLAC should be considered as a serious obstacle to resolvability by the supervisory or resolution authority, notwithstanding the conclusions of any prior resolvability assessment, and authorities should act promptly to ensure a breach is remedied quickly to ensure sufficient LAC is available in resolution.

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