



CRÉDIT AGRICOLE S.A.

Calibration of the amount of TLAC required

1. Is a common Pillar 1 Minimum TLAC requirement that is set within the range of 1a6 – 20% of risk-weighted assets (RWAs), and at a minimum twice the Basel III leverage requirement, adequate in the light of experiences from past failures to support the recapitalisation and resolution objectives set out in this proposal? What other factors should be taken into account in calibrating the Pillar 1 Minimum TLAC requirement?

We regret that regulators consider that TLAC should be a pillar 1 requirement. The pitfall of a pillar 1 minimum ratio is that it will restrict coupon payments on Tier 1 instruments. Regulators should indeed be aware that **investors look at the distance to the threshold of coupon reduction and expect a certain amount of buffer (typically in a range of 2-4%) above the required minimum threshold before investing.** This means that if banks have a ratio that is lower than that expected by investors, investors may consider that they would not receive AT1 coupons for a considerable time, which may **close the Additional Tier 1 market** at least for some banks. This problem could be addressed by setting the entire TLAC as a pillar 2 requirement¹. Pillar 2 is an obligation which banks have to comply with, so a pillar 2 requirement would allow fulfilling the objectives of the TLAC regulation and allow supervisors to reduce coupon payment where relevant. By contrast, a pillar 1 constraint would prohibit the strengthening of own funds with Additional Tier 1 capital in many cases.

We urge the FSB to take that point into consideration in its QIS and further reflexion, and **calculate the shortfall of TLAC eligible liabilities of the industry taking into account these “management” buffers for AT1 issuance purposes.**

Moreover, it should be noted that with a pillar 1 requirement, once the resolution occurs, the restructured entity will not be able to reach the TLAC requirement rapidly, not even within the 12-24 months of the proposed conformance period. The amount of subordinated debt to be issued in order to avoid any restriction of distribution is indeed quite high and will require much more time.

Having said that, we urge the FSB to pay close attention to the following elements in the calibration of the TLAC requirement.

The experiences of past failures need to be analysed in light of the new prudential and resolution frameworks for G-SIBs that have been implemented since the crisis. In the same vein, measures have been taken to address sources of losses during the crisis with margin requirements and the ISDA protocol. Overall, these new requirements provide a completely different picture which needs to be taken into account when calibrating the TLAC requirement. Finally, the results of the European stress test and Asset quality review exercise should also be taken into account.

¹ We ask that a breach of the TLAC requirement be treated with the measures applicable to a pillar 2 requirement and not with measures applicable to a pillar 1 requirement (e.g. including restrictions on AT1 distributions)..

The TLAC requirement would need to reflect the fact that resolution does not mean resurrection of the whole failing bank but ensuring the continuity of its critical functions, as provided in its resolution plan. The TLAC requirement should be focused on facilitating the group resolution plan. It is our view that it is very important to ensure that the objectives of TLAC regulations focus on the aforementioned outcome as a full resurrection of the whole failing bank, rather than continuation of its critical systemic functions (e.g. payments administration), would result in the distortion of competition for healthy, prudently managed banks and this is an outcome which would not be commensurate with the outcome of a “classic” insolvency and liquidation proceedings

Against this background, we consider that **the proposed 16-20% of RWAs or double leverage ratio is much too high than necessary**. Moreover, it is key that the TLAC requirement does not follow any possible increases in the leverage ratio or changes to the RWA requirements. It should be subject to its own, separate analysis to make sure it remains calibrated to actual resolution requirements based on the resolution plan, and not to prudential concerns. We consider that:

- **The leverage ratio should remain a backstop measure and should not be used for the determination of TLAC.** A fortiori, if nevertheless maintained, it should not be based on a multiplier of the leverage ratio which has neither been calibrated nor harmonised across jurisdictions yet. At the very maximum, it should be set at 6% of total assets and follow a long transition period.

Moreover, when TLAC is based on the leverage ratio, it would be helpful to confirm a) that the capital buffers can count as TLAC, contrary to what is envisaged for TLAC based on RWAs where the buffers come on top of the TLAC; and b) that the 2.5% RWA of senior unsecured liabilities can also count as TLAC (TS 13).

- Regarding the RWA basis of the ratio, we believe that **a common fixed amount of 16% applicable across G-SIBs would be sufficient**. 16% RWA amounts to twice the minimum own funds requirements and it can be backed up by the capital buffers and pillar 2 requirements. Furthermore, a common fixed amount would ensure a level playing field across banks and jurisdictions, contrary to a range.

Should a 16-20% range be maintained, the classification as a G-SIB in the matrix established by the FSB should be considered when setting the TLAC requirement in respect of the proposed range of 16-20%-of-RWA TLAC requirement. A G-SIB classified in the 1.0% or 1.5% category of the G-SIB matrix should naturally be subject to a lower TLAC requirement (i.e. closer to the 16%-of-RWA) than one classified in the 2.5-3.5% ranges of the G-SIB matrix.

Finally, we believe that the calibration of the TLAC requirement should be closely linked to the results of the QIS and the market survey analysis scheduled by the FSB in 2015. Indeed, **it is important to make sure that the final TLAC minimum requirement retained by the FSB is practicable** (i.e. it takes into account the depth of markets for eligible TLAC instruments) **and sustainable for banks so that they could maintain their crucial role in financing the real economy**, particularly in the current context where regulatory requirements and prudential frameworks have already been significantly strengthened since the crisis. Moreover, we consider that the TLAC calibration should take into account the stress tests scenario as a critical determining factor and be consistent with it.

2. Does the initial exclusion of G-SIBs headquartered in emerging market economies (EMEs) from meeting the Common Pillar 1 Minimum TLAC requirement appropriately reflect the different market conditions affecting those G-SIBs? Under what circumstances should the

exclusion end?

We don't understand the rationale for excluding emerging market economies. EMEs are equal competitors on the international market and as such they should follow the same rules. **Having different rules for banks that can compete on the same market raises a serious competitive issue.** Furthermore the notion of EMEs is not well defined and is rapidly evolving. For example in Europe some countries are part of the single European market and are EMEs, and on the other hand in Asia some emerging economies are reaching a higher level of development. Every bank should compete on the market based on the same rules.

Moreover, the initial exclusion should end for G-SIBs headquartered in emerging markets when these institutions become internationally active. For the already established international activities of EME G-SIBs such a phase-out may not be required and any exclusion may worsen the distortion of the level playing field of competition. We would recommend considering in the forthcoming FSB QIS the extent to which EME G-SIBs already are active globally.

Finally, if the exemption is justified in certain jurisdictions according to the FSB, it should be clarified that the MPE subsidiaries of EME headquartered G-SIBs, which are competing in jurisdictions subject to the TLAC, are also subject to TLAC, to ensure a level playing field.

Should the initial exclusion of G-SIBs headquartered in EMEs be maintained, we believe that transparency on the schedule of its phase-out, when it materialises, is necessary in order to minimize the level playing field issue that it generates.

3. What factors or considerations should be taken into account in calibrating any additional Pillar 2 requirements?

Firstly, we note that the TLAC requirement should be a pillar 2 requirement as a whole (cf. answer to Question 1 for our reasoning in this context).

With the TLAC ratio, a G-SIB would have to meet: own funds and TLAC requirements + G-SIB surcharge + countercyclical buffer + any possible increase in own funds requirements pursuant to pillar 2. It should be clarified **what weaknesses an additional TLAC pillar 2 surcharge would seek to cover that is not already addressed.** Moreover a pillar 2 TLAC surcharge requirement would decrease transparency and predictability of TLAC requirements for investors and could lead to unjustified goldplating by national regulators and thus to an unlevel playing field.

In addition, in certain jurisdictions the pillar 2 requirements under Basel II/III shall not be disclosed, which would prohibit any use of Pillar 2 for the TLAC ratio as the disclosure of the TLAC would reveal the pillar 2 level of the entity.

Furthermore, we think that there should be no requirement for a TLAC pillar 2 surcharge in excess of the TLAC requirements set in respect of RWA's and leverage ratio measures. Considering that the resolution objectives are to preserve the bank's critical functions, and not to bring back to life a full-fledged institution, post resolution the structure of the remaining group will be very different, and therefore diversification effects will lead to significantly different results where a full pillar 2 is not necessary anymore. The resolution authority has the power to separate banking activities between a good bank and a bad bank, which would likely lead to a downsizing of the remaining good bank and a reduction of its pillar 2 risks.

For all these reasons, we would invite the FSB to **remove the additional pillar 2 surcharge requirement.**

Ensuring the availability of TLAC for loss absorption and recapitalization in the resolution of cross-border groups

4. Should TLAC generally be distributed from the resolution entity to material subsidiaries in proportion to the size and risk of their exposures? Is this an appropriate means of supporting resolution under different resolution strategies? Which subsidiaries should be regarded as material for this purpose?

5. To what extent would pre-positioning of internal TLAC in material subsidiaries support the confidence of both home and host authorities that a G-SIB can be resolved in an orderly manner and diminish incentives to ring-fence assets? Is a requirement to pre-position internal TLAC in the range of 75 - 90% of the TLAC requirement that would be applicable on a stand-alone basis, as set out in the term sheet (Section 22), appropriate to satisfy the goals of the proposal and ensure that TLAC is readily and reliably available to recapitalize subsidiaries as necessary to support resolution? Can this pre-positioning be achieved through other means such as collateralized guarantees?

To questions 4 and 5:

We accept the need for host authorities to be confident that LAC would be available to allow orderly resolution. But care should also be taken that the allocation of TLAC within a group does not create fragmentation and lead to trapped pools of resources, especially in resolution. We believe that the Crisis Management Groups (CMG) created by the FSB are the right fora to develop trust amongst resolution authorities. TLAC distribution within a group should depend on the group's resolution strategy and resolution plan as agreed in the bank's CMG. **There should be no automatic allocation of TLAC** upon meeting the criteria set out in TS 21 but rather, and where relevant, an allocation to subsidiaries based on a decision by the CMG in line with the group's resolution strategy.

Should an internal TLAC be maintained, it should as much as possible be limited to material subsidiaries in jurisdictions where the health of the subsidiary on a stand-alone basis has a substantial impact on the stability of the host country. The inclusion of internal TLAC should also limit the responsibility of the holding company with regard to the recapitalisation of the subsidiary: as such, **internal TLAC should act as a stop-loss for the holding company and be linked to the ability to have a resolution at the subsidiary level alone**, in line with the group resolution plan.

Moreover, we believe that the determination of internal TLAC should be discussed between home and host authorities, based on a top-down approach of the external TLAC allocation, and as such **reflecting the allocation of the group TLAC capital to the subsidiary**. Otherwise, the sum of the internal TLAC determined at the solo level for the material subsidiaries could become super-equivalent to the external TLAC, which, in our understanding, is not the objective of the FSB term sheet.

Furthermore, **more flexibility is needed on the constitution of internal TLAC**. The proposed option to make use of guarantees would provide appropriate flexibility (TS 23) but it should be possible to take into consideration other forms of support such as unconditional but unfunded guarantees of the parent with supervisory approval; intra-group financial support agreements (as provided in the BRRD) or internal cross-guarantee schemes of cooperative banks.

As a general rule, groups should be able to decide the mix of debt and equity that is appropriate to distribute internal TLAC. In this regard, it should be confirmed that the 33%

debt requirement would not apply to internal TLAC but only to the consolidated level (TS 7). Indeed, flexibility is necessary to consider the specificities of subsidiaries in certain jurisdictions which may create obstacles to debt issuance. Moreover, the requirement of internal TLAC in form of debt may generate tax issues that could be lowered with equity.

Determination of instruments eligible for inclusion in external TLAC

6. *Are the eligibility criteria for TLAC as set out in the term sheet (Sections 8-17) appropriate?*

Exclusions (TS12):

The definitions of the exclusions from the TLAC would need to be clarified. Indeed, in TS12 (excluded liabilities), there is a mix between exclusions for reasons of ranking, and exclusions for reasons of practicality of resolution, which may generate confusion on the order in which creditors bear loss in resolution. More specifically:

- **Structured notes (TS12):** these instruments are excluded from the TLAC due to concerns over the operational complexity of bailing-in this kind of debt and not from economical or legal reasons as far as we understand it. **We disagree with such a priori blanket exclusion of structured notes.** They are economically long-term liabilities that should be able to absorb losses the same way as other senior debts in bail-in. In fact, most structured notes often have relatively simple market risk features and are quite industrial instruments, with a large degree of standardization, including back-office, listing and valuation processes.. Even if structured notes are excluded from the TLAC calculation for practical reasons, they should not be excluded from the waterfall of the bail-in and should remain *pari passu* with other senior debt eligible to the TLAC. The latter principle should also be borne in mind for the instruments that are not TLAC-eligible only because they do not meet the residual maturity criterion.

In order to address the operational concern mentioned above for structured notes, **a principle-based approach would probably allow the FSB to guide the possible exclusions** that would be in the hands of the resolution authorities when assessing the feasibility and credibility of the resolution plans. We would advise the FSB to work with banks to define such a grid of principles related to structured notes.

- “Callable on demand without supervisory approval” (TS12): clarifications are required about the rationale underlying the exclusion of “any liability that is callable on demand without supervisory approval”. In any case, any liability that is callable only at the issuer’s discretion should be eligible, considering that issuers would only call those instruments as long as they comply with TLAC minimum requirement

Redemption restrictions (TS15):

We would urge the FSB to reconsider this provision and **to require a supervisory approval only when redeeming eligible TLAC would lead to a breach** of the TLAC requirement. Otherwise, as drafted, this provision which applies to all eligible TLAC instruments would generate rigidity in the day-to-day business management of the G-SIBs.

7. *What considerations bear on the desirability of an expectation that a certain proportion of the common minimum Pillar 1 TLAC requirement consists of (i) tier 1 and tier 2 capital instruments in the form of debt plus (ii) other eligible TLAC that is not regulatory capital?*

The rationale behind this proposal remains unclear as in any case it is better to have a loss

absorbing capacity that is exclusively composed of CET1 rather than the same capacity composed of convertible instruments which are of lower quality. Such constraint would add rigidity to the framework while supervisors traditionally prefer CET1 capital. Moreover, it would penalise cooperative banking groups, which capitalize most of their profits and have therefore much CET1 and little convertible or hybrid debt. **More flexibility is therefore necessary to accommodate specific business models and capital structures, as well as the CET1 expectations of the relevant supervisors and the affordability of the hybrid debt market.** There should be no unnecessary restrictions on firms' flexibility in deciding on the appropriate funding mix for a given situation.

8. Are the conditions specified in the term sheet (Section 8) under which pre-funded commitments from industry-financed resolution funds to provide resolution funding contribute to TLAC appropriate?

The conditions stated in this section will exclude any pre-funded commitments from the European resolution funds (notably, the condition requiring that there is no limit specified in law in respect of the amount which may be contributed) from the TLAC instruments, which may **create level playing field issues vis-à-vis other jurisdictions.**

9. Is the manner in which subordination of TLAC-eligible instruments to excluded liabilities is defined in the term sheet (Section 13) sufficient to provide certainty regarding the order in which creditors bear loss in resolution, and to avoid potentially successful legal challenges or compensation claims? Where there is scope for liabilities which are not subordinated to excluded liabilities to qualify for TLAC, are the transparency and disclosure requirements set out in section 13 and 24 sufficient to ensure that holders of these instruments would be aware of the risk that they will absorb losses prior to other equally ranking but excluded liabilities? If not, what additional requirements should be adopted?

We understand the rationale underlying the subordination criterion and we believe that the three modes of subordination proposed (contractual, statutory and structural) should be kept. However, we would like to highlight that in practice these three modes will not be readily applicable and will generate adaptation costs. This is especially true for **European banks which are structured under an operating mother company, and whose structure does not allow the subordination of TLAC-eligible senior debt to TLAC-excluded senior debt.** As a consequence, we believe that the condition on subordination should not be too prescriptive and rather be tailored by resolution authorities according to the applicable resolution law. **In the EU, TLAC should take into account the statutory bail-in regime** which enables the bail-in of a broad scope of senior debts and leave the resolution authority flexibility to exclude some debts in resolution (for practical or systemic reasons, on a case by case basis).

Regarding the scope left for non-subordinated liabilities, as said before (see also response to question 6), we believe that the way the exclusions are defined needs to be clarified, as it mixes exclusions due to insolvency ranking and other exclusions (for practical reasons).

Finally, regarding the proposed inclusion of senior debt into the TLAC, we understand that this is **an option at the discretion of banks**, and not a requirement. We support such optional approach. Moreover, it would be helpful for the FSB to clarify the rationale behind the proposed amount of 2.5% RWAs.

Clarifications are also needed regarding the way this amount would be increased in cases where the final calibration of the TLAC would exceed 16% of the RWAs. We suggest increasing this option proportionally to the increase of the TLAC requirement beyond 16% RWAs in relation to the current minimum capital ratio (for instance: a TLAC requirement set at 18% RWAs corresponds to an increase of 25% of the current minimum capital ratio, therefore the allowed amount of senior debt in TLAC should be proportionally increased by 25%, resulting in a 3,125% RWAs amount).

Interaction with regulatory capital requirements and consequence of breaches of TLAC

10. Do you agree that the TLAC requirement for G-SIBs should be integrated with Basel III such that the minimum TLAC requirement should be met first, and only after TLAC is met should any surplus common equity tier 1 (CET1) be available to meet the Basel III buffers?

Yes, we support the idea that any erosion of CET1 would be allocated to buffers first.

Transparency

11. What disclosures (in particular in terms of the amount, nature and maturity of liabilities within each rank of the insolvency creditor hierarchy) should be required by resolution entities and material subsidiaries to ensure that the order and quantum of loss absorption in insolvency and resolution is clear to investors and other market participants?

Considering that a lot of different disclosure configurations are possible, we would suggest that either full discretion is left to the bank for its declaration **or alternatively a disclosure following a scenario-approach** based on a loss hypothesis at the point of non-viability.

In terms of granularity of the information disclosed, we encourage the FSB to base its requirement on what already exists under the current prudential framework, in order to avoid multiplying disclosure requirements unnecessarily. Moreover, we believe that the disclosure should be required **only at the resolution entity level**.

Limitation of contagion

12. What restrictions on the holdings of TLAC are appropriate to avoid the risk of contagion should those liabilities be exposed to loss in resolution?

If G-SIBs may not count their holdings of other G-SIBs' liabilities towards their TLAC ratio, this raises the question of the **existence of a market for such TLAC instruments**. Especially in Europe where debt markets are relatively small, added to the fact that all GSIBs would need to raise large amounts of subordinated debt at the same time, the consequence of such restriction would be to increase costs of TLAC debt and to make it uneconomical for dealers to underwrite or make a market in TLAC instruments. While we can understand the contagion risk concerns, **more flexibility is required to enable the development of a market for TLAC instruments**.

The FSB should establish a threshold below which the holding of G-SIBs TLAC instruments by other G-SIBs would be allowed. We invite the FSB to consider in its QIS the calibration of such a threshold specific for TLAC purposes.

Conformance period

13. Should G-SIBs be required to conform with these requirements from 1 January 2019? Why or why not? What, within the range of 12 to 36 months following the identification as a G-SIB, should be the conformance period for banks identified as G-SIBs at a future date?

Taking into account the structural impacts of implementing a TLAC requirement and the limited market depth to absorb the required volume of TLAC debt, we would urge the FSB to allow a **longer transition period**.

Should the 2019 deadline be maintained, a phasing-in would be necessary to comply with some of the additional requirements if they were to apply, namely the minimum of debt in

the TLAC ratio and internal TLAC for foreign subsidiaries.

We would ask regulators' support to make sure credit rating agencies could not preempt the new rules and downgrade ratings before even knowing the concrete impacts of the new rules.

Market impact and other aspects

14. How far is the TLAC proposal, if implemented as proposed, likely to achieve the objective of providing sufficient loss-absorbing and recapitalization capacity to promote the orderly resolution of G-SIBs?

Subject to our responses to many important aspects of the proposal, if appropriately amended and implemented, we believe the TLAC should achieve its objectives and end the too-big-to-fail issue. It should also solve the question of the structural organisation of universal banks' trading activities once and for all.

15. What will be the impact on G-SIB's overall funding costs of the adoption of a Pillar 1 Minimum TLAC requirement?

Subordinated debt is by nature more risky and thus more expensive than senior debt (e.g. ca. +130bp for Credit Agricole S.A. in the current context of low interest rates and ample liquidity - Jan. 2015), so will further increase when interest rates pick up and liquidity decreases). Therefore we expect that **the Pillar 1 minimum TLAC requirement, which implies a significant recourse to subordinated debt, will materially increase the funding costs of G-SIBs.**

Furthermore, G-SIBs will have to deal with the costs of adapting their financing structure and their functioning to the TLAC requirement (i.e. costs relating to the creation of holding companies and contractual subordination).

In order to limit the impact on funding cost of G-SIBs, it is of the highest importance to phase-in the introduction of the measure, especially in the eventuality of the reduction of State support. **TLAC is expected to limit, if not exclude State support; this will have direct consequences on banks' ratings and funding costs.** It is thus of the highest importance to have a smooth phase-out of State support in parallel with a phase-in of the TLAC requirements in order to give time for banks to issue TLAC-eligible debt and limit the impact on ratings.

16. What will be the impact on the financial system and its ability to provide financing to the real economy?

If the TLAC proposal is not appropriately calibrated and consistently applied, and if the impact of the new rule is sudden and not progressive, **banks will likely be massively downgraded.** This will increase their funding cost and may lead to the disappearance of some activities like ABCP refinancing (used to refinance consumer loans) that are directly linked to bank ratings. In addition, it needs to be borne in mind that with TLAC, by construction, **the more banks will lend, the more TLAC they will need and the more they will have to finance the costs of raising subordinated debt.**