

ARTICLE 55 OF THE BRRD AND POST-BREXIT TRANSITION PERIOD EU AND UK UNDERWRITER LIABILITIES IN NEW BOND ISSUES AND ECP DEALER LIABILITIES

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Introduction

1. This note seeks to explain the background to the requirements for the contractual recognition of bail-in under Article 55 of the Bank Recovery and Resolution Directive (“BRRD”) and the requirements that will continue to apply in the UK after the end of the Brexit transition period in the context of underwriters’ liabilities under typical bond issues¹. It also refers to ECP dealers’ liabilities. This note does not deal with actual debt liabilities themselves, which are liabilities of bond and ECP issuers.

Key points

- Currently, underwriters based in the EU27 and UK are subject to the requirements of Article 55 of the BRRD, which requires a “contractual recognition of bail-in” clause to be included in various contracts related to new bond issues and ECP where those contracts are governed by a non-EEA law or non-English law² (e.g. New York law). This has been in force since 1 January 2016.
- The Brexit transition period is due to end at 11pm UK time on 31 December 2020. After the end of the Brexit transition period, EU27 banks will continue to be subject to this requirement. However, English law will no longer be treated as an EEA law. This means that underwriters that are EU27 financial institutions will need to start including a “contractual recognition of EU bail-in” clause in various contracts related to new bond issues and ECP where those contracts are governed by English law (as well as continuing to include such a clause in relevant contracts governed by other non-EEA laws such as New York law).
- In addition, after the end of the Brexit transition period, the UK will amend its rules to reflect the onshoring of Article 55 of the BRRD, meaning that underwriters that are UK financial institutions will need to start including a “contractual recognition of UK bail-in” clause in various contracts related to new bond issues and ECP where those contracts are governed by an EEA law (e.g. German law, French law), subject to applicable transitional provisions. They will need to continue including a contractual recognition of bail-in clause in various new or materially amended

¹ Amendments to the BRRD (known as BRRD II) entered into force on 27 June 2019 and are expected to apply in most cases by 28 December 2020. However, these changes (including their implementation into UK law) are not expected to impact upon the subject matter of this note.

² This note refers to English law because English law is the most commonly used UK law for the purposes of bond and ECP issues. However, the references in this note to English law apply equally to other UK laws (e.g. Scottish law).

contracts governed by a non-EEA law (e.g. New York law), but the form of clause will need to refer to the UK bail-in regime, rather than the EU bail-in regime.

- The introduction of a “contractual recognition of bail-in” clause in relevant bond issue and ECP contracts as a result of the end of the Brexit transition period merely acknowledges the powers that resolution authorities have as a matter of law before the end of the Brexit transition period. **Therefore, in practical terms, it should not change the position of the parties as they stand under EEA and English law in effect before the end of the Brexit transition period.**

What is ‘Article 55’?

2. BRRD was adopted in spring 2014 to provide authorities with comprehensive powers to deal with failing banks and cooperation arrangements to tackle cross-border banking failures within the EU. It aims to ensure an orderly resolution of failing banks with minimal costs for taxpayers.
3. One of the tools available to resolution authorities under BRRD is the “bail-in” tool, which is intended to allow resolution authorities in the EU to write-down or convert to equity a failing bank’s liabilities.
4. Article 55 of the BRRD supports the bail-in tool by requiring banks to include clauses in contracts governed by third country law (i.e. non-EEA law such as New York law) to ensure that liabilities under these contracts can be effectively written down or converted by the resolution authority of a failing bank. This is known as “contractual recognition of EU bail-in”.

What liabilities are caught under Article 55?

5. Article 55 of the BRRD is very broad in scope. As well as applying to actual debt liabilities (e.g. unsecured bonds), it also applies to other liabilities.
6. In practice, this means that a “contractual recognition of EU bail-in” clause is required in a very broad scope of agreements governed by a non-EEA law, even if the risk of the liability crystallising in practice may be very remote and/or within the control of the relevant party.
7. In respect of underwriters’ liabilities in new bond issues, the scope of agreements is understood to include subscription agreements and dealer agreements.
8. Parties to other bond issue contracts to which the underwriters are not a party, such as agency agreements and trust deeds, may wish to consider whether a contractual recognition of EU bail-in clause is required in those contracts.

9. In respect of ECP dealers' liabilities under ECP programmes, the scope is understood to include the ECP dealer agreement.

What does Article 55 mean for underwriters' counterparties?

10. Broadly speaking, underwriters' counterparties (e.g. issuers) need to acknowledge in third country law-governed contracts with underwriters that the underwriters' liabilities under the contract may be written down or converted by the relevant resolution authority. This is intended to ensure that the underwriters' resolution authorities have the same powers that they would have as a matter of law, if the contract was governed by an EEA law.
11. A contractual recognition of EU bail-in clause has been required in relevant third country law governed contracts (e.g. New York law contracts) since 1 January 2016.

Why will the end of the Brexit transition period change things?

12. The Brexit transition period is due to end at 11pm UK time on 31 December 2020. After the end of the Brexit transition period, English law will no longer be treated as an EEA law. Because the requirements of Article 55 of the BRRD relate to liabilities governed by a non-EEA law, this means that underwriters subject to Article 55 of the BRRD will need to start including a "contractual recognition of EU bail-in" clause in relevant contracts governed by English law (as well as continuing to include such a clause in relevant contracts governed by other non-EEA laws, e.g. New York law).
13. In addition, after the end of the Brexit transition period, the UK will amend its rules that implement Article 55 of the BRRD, creating a parallel but distinct bail-in regime for the UK. This means that underwriters that are UK financial institutions will need to start including a "contractual recognition of UK bail-in" clause in relevant contracts where those contracts are governed by an EEA law (e.g. German law, French law), subject to any applicable transitional provisions (see paragraph 17a below).
14. Underwriters that are UK financial institutions will also need to continue including a contractual recognition of bail-in clause in relevant new or materially amended contracts governed by a non-EEA law (e.g. New York law)³, but the form of clause will need to refer to the UK bail-in regime, rather than the EU bail-in regime.
15. Although a contractual recognition of bail-in clause will be required in a larger number of contracts after the end of the Brexit transition period, it is important to note that the inclusion of this language merely acknowledges the powers that resolution authorities have as a matter of law before the end of the Brexit transition period. **Therefore, in practical**

³ As noted in paragraph 13, after the end of the Brexit transition period, this will include contracts governed by non-English laws.

terms, it should not change the position of the parties as they stand under EEA and English law in effect before the end of the Brexit transition period.

When do underwriters need to start reflecting the necessary changes in relevant contracts?

16. Underwriters that are EU27 financial institutions

Subject to the views of national resolution authorities or relevant EU official bodies, underwriters subject to Article 55 of the EU BRRD need to start including a “contractual recognition of EU bail-in” clause in any relevant new or materially amended English law-governed contract after the end of the Brexit transition period (i.e. from 1 January 2021).

17. Underwriters that are UK financial institutions

a. Contracts governed by an EEA law (e.g. German law, French law):

UK authorities are currently consulting upon provisions that would grant transitional relief under the UK requirements in respect of certain types of liabilities governed by an EEA law. This may mean that underwriters that are UK financial institutions only need to start including a “contractual recognition of UK bail-in” clause in any relevant new or materially amended contracts governed by an EEA law from 31 March 2022. This point will need to be analysed once the relevant UK requirements are finalised.

b. Contracts governed by a non-EEA, non-English law (e.g. New York law, Hong Kong law):

Underwriters that are UK financial institutions need to start including a new form of “contractual recognition of UK bail-in” clause in any such relevant new or materially amended contracts after the end of the Brexit transition period (i.e. from 1 January 2021) (rather than continuing to include a “contractual recognition of EU bail-in clause” that reflects the EU regime).

Are there standard forms of language available?

18. In 2015, a standard form of “other liabilities” language was developed by AFME, ICMA and leading law firms. This standard form was used by underwriters to address the requirements of Article 55 of the BRRD in non-EEA law governed bond issue and ECP contracts from the time that BRRD was introduced in 2016 until the start of the Brexit transition period on 1 January 2020. During the Brexit transition period, the definition of “Bail-in Legislation” needed to be adjusted to reflect the fact that the UK was no longer a Member State of the EU, but that EU law still applied in the UK. After the end of the Brexit transition period, it is anticipated that parties will reverse the change made to the definition of “Bail-in Legislation” that was needed during the Brexit transition period, and use the original standard form clause. That original standard form “Recognition of EU bail-in clause” is set out in Annex 1.

19. A new version of the clause has been developed by ICMA, AFME and leading law firms for use by UK financial institutions in relevant non-English law governed bond issue and ECP contracts. This “Recognition of UK bail-in clause” is set out in Annex 2.
20. Whether one or both of these clauses is needed in relevant bond issue and ECP contracts will depend on the identity of the parties and the governing law of the contract, as summarised in the table below.

	In-scope entities	Governing law of in-scope contract	Type of clause needed
1.	EU27 and UK	Non-EEA and Non-English law e.g. New York law	Recognition of EU bail-in (Annex 1) and UK bail-in (Annex 2)
2.	EU27 and UK	English law	Recognition of EU bail-in only (Annex 1)
3.	EU27 and UK	EEA law	Recognition of UK bail-in only (Annex 2)
4.	EU27 only	Non-EEA law (including English law)	Recognition of EU bail-in only (Annex 1)
5.	UK only	Non-English law	Recognition of UK bail-in only (Annex 2)

21. In scenario 1 above, where both a “Recognition of EU bail-in clause” and a “Recognition of UK bail-in clause” are required, parties can choose to: (a) include the two separate clauses set out in Annex 1 and Annex 2 to this paper; or (b) draft one combined clause that caters for both the EU and UK bail-in regimes based on those separate clauses.

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ANNEX 1

RECOGNITION OF EU BAIL-IN CLAUSE FOR OTHER LIABILITIES

Set out below is a model clause for contractual recognition of bail-in powers for liabilities other than debt instruments or liabilities governed by industry standard master agreements (collectively, “other liabilities”) governed by a non-EEA law reflecting the requirements of Article 55 of the EU Bank Recovery and Resolution Directive (BRRD). This clause was originally developed by a group of leading law firms for AFME and ICMA. Its intended uses include contracts related to new issues of bonds, bond issuance programmes and ECP issuance programmes. For debt liabilities, one of the model clauses set out in [AFME’s model clauses for the contractual recognition of bail-in under Article 55 BRRD](#) may be relevant.

Provision ⁴	Other Liabilities governed by a non-EEA law ⁵
Contractual acknowledgement	Notwithstanding and to the exclusion of any other term of this [<i>Agreement</i>] or any other agreements, arrangements, or understanding between [[<i>BRRD Party</i>] and [<i>Creditor or Counterparty of BRRD Party</i>]]^{6,7} [<i>Creditor or Counterparty of BRRD Party</i>]⁸ acknowledges and accepts that a BRRD Liability arising under this [<i>Agreement</i>] may be subject to the exercise of Bail-in Powers by the Relevant Resolution Authority⁹, and acknowledges, accepts, and agrees to be bound by: a. the effect of the exercise of Bail-in Powers by the Relevant Resolution Authority in relation to any BRRD Liability of [[<i>BRRD Party</i>] to [<i>Creditor or Counterparty of BRRD Party</i>]]¹⁰ under this agreement, that (without limitation) may include and result in any of the following, or some combination thereof: i. the reduction of all, or a portion, of the BRRD Liability or outstanding amounts due thereon;¹¹

⁴ **Note to counsel preparing the transaction documentation:** Consider other relevant provisions for amendment / inclusion in the main agreement. For example, under English law, the benefit of a contract but not the burden can be assigned. Accordingly, in order to avoid the assignment of a contract to a person who has not consented to bail-in, if there is a consent to assignment clause, consider having a termination right where assignment takes place without consent. Where there is not a consent to assignment clause in the main agreement, we advise that this is added, and consent to assignment should only be given where the assignee consents contractually to bail-in.

⁵ **Note to counsel preparing the transaction documentation:** Consideration should be given to obtaining advice in relation to the effectiveness of this clause in relation to the law of the non-EEA state governing the contract. Consideration may also be given to having the consent to bail-in governed by the law of an EEA state to avoid the need for a contractual recognition clause.

⁶ Include “[*BRRD Party*] and [*BRRD Party*] (each a “**BRRD Party**”)” where the liabilities of both parties under the Agreement may be subject to bail-in under the BRRD.

⁷ Reflecting Article 44(4) of Commission Delegated Regulation (EU) 2016/1075 (the “**Delegated Regulation**”)

⁸ Include “each BRRD Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the BRRD.

⁹ Reflecting Article 44(1) of the Delegated Regulation.

¹⁰ Include “a BRRD Party (“**Relevant BRRD Party**”) to the other BRRD Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the BRRD.

¹¹ Reflecting Article 63(1)(e) of the BRRD, as per the requirements in Articles 44(2) and 44(3)(a)(i) of the Delegated Regulation.

Provision ⁴	Other Liabilities governed by a non-EEA law ⁵
	ii. the conversion of all, or a portion, of the BRRD Liability into shares, other securities or other obligations of [BRRD Party]¹² or another person, and the issue to or conferral on [Creditor or Counterparty of BRRD Party]¹³ of such shares, securities or obligations;¹⁴ iii. the cancellation of the BRRD Liability;¹⁵ iv. the amendment or alteration of any interest, if applicable, thereon, the maturity or the dates on which any payments are due, including by suspending payment for a temporary period;¹⁶ b. the variation of the terms of this [Agreement], as deemed necessary by the Relevant Resolution Authority, to give effect to the exercise of Bail-in Powers by the Relevant Resolution Authority.¹⁷
Definitions	“Bail-in Legislation” means in relation to a member state of the European Economic Area which has implemented, or which at any time implements, the BRRD, the relevant implementing law, regulation, rule or requirement as described in the EU Bail-in Legislation Schedule from time to time. “Bail-in Powers” means any Write-down and Conversion Powers as defined in the EU Bail-in Legislation Schedule, in relation to the relevant Bail-in Legislation. “BRRD” means Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms. “EU Bail-in Legislation Schedule” means the document described as such, then in effect, and published by the Loan Market Association (or any successor person) from time to time at http://www.lma.eu.com/pages.aspx?p=499. “BRRD Liability” means a liability in respect of which the relevant Write Down and Conversion Powers in the applicable Bail-in Legislation may be exercised. “Relevant Resolution Authority” means the resolution authority with the ability to exercise any Bail-in Powers in relation to [BRRD Party]¹⁸.

¹² Include “the Relevant BRRD Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the BRRD.

¹³ Include “the other BRRD Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the BRRD.

¹⁴ Reflecting Article 63(1)(f) of the BRRD as per the requirements in Articles 44(2), 44(3)(a)(ii) and 44(3)(c) of the Delegated Regulation.

¹⁵ Reflecting Article 63(1)(g) of the BRRD as per the requirements in Article 44(2) of the Delegated Regulation.

¹⁶ Reflecting Article 63(1)(j) of the BRRD, and the requirements in Articles 44(2) and 44(3)(a)(i) of the Delegated Regulation.

¹⁷ Reflecting Article 44(3)(b) of the Delegated Regulation.

¹⁸ Include “the Relevant BRRD Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the BRRD.

ANNEX 2

RECOGNITION OF UK BAIL-IN CLAUSE FOR OTHER LIABILITIES

Set out below is a model clause for contractual recognition of bail-in powers for liabilities other than debt instruments or liabilities governed by industry standard master agreements (collectively, “other liabilities”) governed by a non-English law reflecting the requirements of the UK bail-in regime. This clause was originally developed by a group of leading law firms for AFME and ICMA. Its intended uses include contracts related to new issues of bonds, bond issuance programmes and ECP issuance programmes. For debt liabilities, one of the model clauses set out in [AFME’s model clauses for the contractual recognition of bail-in under Article 55 BRRD](#) may be relevant.

Provision	Other Liabilities governed by a non-English law ¹⁹
Contractual acknowledgement	Notwithstanding and to the exclusion of any other term of this [Agreement] or any other agreements, arrangements, or understanding between [[UK bail-in party] and [creditor or counterparty of UK bail-in party]]²⁰, [creditor or counterparty of UK bail-in party]²¹ acknowledges and accepts that a UK Bail-in Liability arising under this [Agreement] may be subject to the exercise of UK Bail-in Powers by the relevant UK resolution authority²², and acknowledges, accepts, and agrees to be bound by: a. the effect of the exercise of UK Bail-in Powers by the relevant UK resolution authority in relation to any UK Bail-in Liability of [[UK bail-in party] to [creditor or counterparty of UK bail-in party]]²³ under this agreement, that (without limitation) may include and result in any of the following, or some combination thereof: i. the reduction of all, or a portion, of the UK Bail-in Liability or outstanding amounts due thereon; ii. the conversion of all, or a portion, of the UK Bail-in Liability into shares, other securities or other obligations of [UK bail-in party]²⁴ or another person, and the issue to or conferral on [creditor or counterparty of UK Bail-in Party]²⁵ of such shares, securities or obligations; iii. the cancellation of the UK Bail-in Liability;

¹⁹ **Note to counsel preparing the transaction documentation:** Consideration should be given to obtaining advice in relation to the effectiveness of this clause in relation to the (non-English) law governing the contract.

²⁰ Include “[UK bail-in party] and [UK bail-in party] (each a “UK Bail-in Party”)” where the liabilities of both parties under the Agreement may be subject to bail-in under the UK Bail-in Legislation.

²¹ Include “each UK Bail-in Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the UK Bail-in Legislation.

²² This is the terminology used in the AFME model clause for *debt* liabilities of entities organised in the UK, available in the [AFME model clauses and user guide document](#).

²³ Include “a UK Bail-in Party (“**Relevant UK Bail-in Party**”) to the other UK Bail-in Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the UK Bail-in Legislation.

²⁴ Include “the Relevant UK Bail-in Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the UK Bail-in Legislation.

²⁵ Include “the other UK Bail-in Party” where the liabilities of both parties under the Agreement may be subject to bail-in under the UK Bail-in Legislation.

Provision	Other Liabilities governed by a non-English law ¹⁹
	iv. the amendment or alteration of any interest, if applicable, thereon, the maturity or the dates on which any payments are due, including by suspending payment for a temporary period; b. the variation of the terms of this [Agreement], as deemed necessary by the relevant UK resolution authority, to give effect to the exercise of UK Bail-in Powers by the relevant UK resolution authority.
Definitions	“UK Bail-in Legislation” means Part I of the UK Banking Act 2009 and any other law or regulation applicable in the UK relating to the resolution of unsound or failing banks, investment firms or other financial institutions or their affiliates (otherwise than through liquidation, administration or other insolvency proceedings). “UK Bail-in Liability” means a liability in respect of which the UK Bail-in Powers may be exercised. “UK Bail-in Powers” means the powers under the UK Bail-In Legislation to cancel, transfer or dilute shares issued by a person that is a bank or investment firm or affiliate of a bank or investment firm, to cancel, reduce, modify or change the form of a liability of such a person or any contract or instrument under which that liability arises, to convert all or part of that liability into shares, securities or obligations of that person or any other person, to provide that any such contract or instrument is to have effect as if a right had been exercised under it or to suspend any obligation in respect of that liability.