

20 November 2019

Marie Donnay
Head of Unit Resolution and Crisis Management (DG FISMA)
European Commission
Rue de Spa 2
1000 Bruxelles
Belgium



Dear Ms Donnay

Article 59 of BRRD II

The role of the Financial Markets Law Committee (the “FMLC” or the “Committee”) is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.

The Bank Recovery and Resolution Directive (2014/59/EU) (the “BRRD”) was amended by Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 (“BRRD II”), which was published in the Official Journal on 7 June 2019 and entered into force on 27 June 2019. E.U. Member States are required to implement BRRD II by 28 December 2020.

The FMLC would like to take this opportunity to highlight in particular the following issues of legal uncertainty in respect of Article 59 of BRRD II:

- (1) BRRD II expands the Article 59 power to include “eligible liabilities”. While it appears that the independent exercise of the Article 59 power under Article 59(1)(a) may only be exercised in relation to internally-issued minimum requirements for own funds and eligible liabilities (“MREL”),¹ it is less clear whether the power may be used in relation to externally-issued MREL when used in combination with other resolution actions.²
- (2) Expanding the scope of Article 59 also calls into question the distinction between the mandatory conversion of capital instruments to utilise their loss absorbing capacity on the one hand and the discretionary use of the bail-in resolution tool on the other potentially in relation to a bank’s wider class of liabilities.³
- (3) Although certain of the safeguards that the BRRD imposes in relation to the exercise of the resolution powers are also imposed in relation to the use of the Article 59 write down and conversion powers, including:
 - (a) *ex ante* valuation to be carried out in accordance with Article 36; and⁴
 - (b) *ex post* valuation to be carried out in accordance with Article 74,⁵

there are some other safeguards that do not appear to apply, or do not apply fully, to eligible liabilities such as the “No Creditor Worse Off” principle in Article 34 which is *partially* applied to the eligible liabilities that are written down or converted.⁶

- (4) The resolution authority in exercising the Article 59 power is not required to have regard to the resolution objectives in Article 31. Although Article 60(1)(d) refers to the principal amount of eligible liabilities being written down or converted to equity to the extent required to achieve the resolution objectives in

+44 (0)20 7601 4286
chiefexecutive@fmlc.or

8 Lothbury
London
EC2R 7HH
www.fmlc.org

Registered Charity Number: 1164902.

“The FMLC” and “The Financial Markets Law Committee” are terms used to describe a committee appointed by Financial Markets Law Committee, a limited compar (“FMLC” or “the Company”). Registered office: 8 Lothbury, London, EC2R 7HH. Registered in England and Wales. Company Registration Number: 8733443.

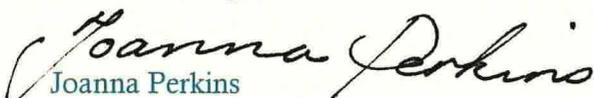
Article 31, this is not the same as a requirement for resolution authorities when exercising the write down and conversion power to “have regard” to the resolution objectives and in doing so choose the tools and powers that best achieve the objectives. Nor is the resolution authority expressly required to seek to minimise the adverse costs of resolution and the destruction of value or where the resolution objectives are of equal significance balance them as appropriate to the nature and circumstances of each case.

- (5) Further, the exercise of resolution powers are framed by some express safeguards that could be relied on in a public law challenge to a resolution authority but these are not applicable to the exercise of the Article 59 powers.

Given the uncertainty in scope and manner of application with respect to the newly expanded scope of Article 59, there is a risk that the Article 59 write down and conversion power which was previously positioned as a prior alternative to resolution based on the loss absorbing powers of a bank’s capital instruments will become a resolution-like power, although it can be used independently of resolution and thus with fewer checks and balances.

I and Members of the Committee would be delighted to meet you to discuss the issues raised in this letter. Please do not hesitate to contact me should you wish to arrange a meeting or if you have any questions.

Yours sincerely,


Joanna Perkins
FMLC Chief Executive⁷

¹ I.e. instruments issued by legal entities in a group that are not themselves resolution entities, directly or indirectly to the resolution entity in the group.

² Article 59(1a) refers to eligible liabilities with reference to Article 45f(2) but not Article 45b in the context of the Article 59 power being exercised independently of resolution action (Article 59(1)(a)). It therefore appears that the independent exercise of the Article 59 power under Article 59(1)(a) may only be exercised in relation to internal MREL.

Although Article 59(1a) appears to include the eligible liabilities limitation only in relation to the independent exercise of the power, reference is made throughout the rest of Article 59 to “eligible liabilities as referred to in paragraph 1a [of Article 59]” and could therefore suggest that the exercise of power under Article 59(1)(b)—which is the exercise of Article 59 power in combination with other resolution actions—relates also only to internal MREL.

³ Prior to BRRD II, under Article 59 of the BRRD, resolution authorities were provided with power to require the capital instruments of a bank to absorb losses as a potential alternative to the exercise of resolution tools (including bail-in). This is the *mandatory* write down and conversion to equity power in Section 6A (*Cases where mandatory write-down, conversion, etc applies*) of the U.K. Banking Act 2009 which implements the BRRD requirements for the write down or conversion of capital instruments.

⁴ Article 59(10).

⁵ Article 59(1).

⁶ Article 59(1a) provides that Member States shall ensure that the write-down or conversion is done in accordance with the principle referred to in point (g) of Article 34(1).

⁷ The FMLC is grateful to Ferdisha Snagg (Cleary Gottlieb Steen & Hamilton LLP) and Stuart Willey (White & Case LLP) for their contributions to, and comments on, this letter.