

11 August 2020

Resilience and Resolution Team
HM Treasury
1 Horse Guards Road
London SW1A 2HQ



Dear Sir or Madam

Consultation: Transposition of the Bank Recovery and Resolution Directive 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.

Directive (EU) 2019/879 as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms ("**BRRD II**") entered into force on 27 June 2019. BRRD II updates the E.U.'s resolution policy and framework for Minimum Requirements for Own Funds and Eligible Liabilities ("**MREL**"), provided by Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms ("the **BRRD**"). In the context of the U.K.'s withdrawal from the E.U., some parts of BRRD II—especially some aspects of Article 1(17)—will apply after the end of the transition period (31 December 2020). To that end, HM Treasury has stated that it will not transpose any of Article 1(17) which revises the framework for MREL requirements. HM Treasury has published a Consultation on the transposition of BRRD II, which, it has stated, concerns those parts of BRRD II that come into effect before the end of the Transition Period.¹ The FMLC would like to take this opportunity to highlight a few issues of legal uncertainty in connection with the transposition of BRRD II.

The transposition of BRRD II and the U.K.'s withdrawal from the E.U.

The FMLC would urge HM Treasury to align, at least in the short-term, the U.K.'s framework in this area, with that of the E.U. In the event an applicable agreement on the future relationship is not agreed between the U.K. and the E.U. by the end of the Transition Period, the "onshored" version of BRRD II will have the effect of unilaterally removing the U.K. from certain benefits which are the subject of mutual obligations (e.g. of recognition, notification and consultation) between E.U. Member States and, in particular, withdrawing from regional and international collaboration arrangements agreed in the aftermath of the financial crisis. Any substantial divergence from E.U. law at this early stage may also create difficulties in establishing similarity with the E.U.'s financial markets framework for the purposes of equivalence assessments for access to the E.U. markets. Market certainty would be better assured if any divergence from E.U. law were to follow careful consultation and signposting.

On a similar note, if there are aspects of BRRD II which HM Treasury is transposing but intends to discard after the end of the Transition Period, the FMLC considers that

¹ HM Treasury, *Consultation: Transposition of the Bank Recovery and Resolution Directive II* (June 2020), available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/89419/2/220620_HMT_BRRDII_consultation_document.pdf, p. 2

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clarity around this would greatly help ensure legal certainty and reduce the operational burden on market participants.

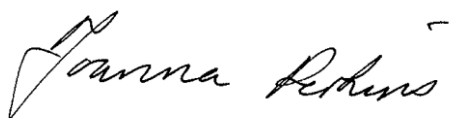
Contractual recognition of resolution stay powers

Under the new Article 71a, BRRD II introduces a requirement for in-scope entities to include a contractual term within financial contracts governed by Third Country law, recognising that the contract may be subject to the exercise of resolution powers by the resolution authority to suspend the firm's payment or delivery obligations, or to suspend a counterparty's termination or security enforcement rights. Chapter 8 of the Consultation asks for comments on these requirements.

Although the purpose of Article 71a is to introduce an E.U.-wide requirement for contractual recognition the stay powers described above, a number of jurisdictions have already put in place equivalent requirements. Market-based solutions covering the requirements, including template clauses and two ISDA protocols, have also been published. The European Banking Authority ("**EBA**") has published draft Regulatory Technical Standards ("**RTS**") for contractual recognition of stay powers which aim to support the effective application of temporary restrictions on early termination rights in relation to financial contracts governed by the law of a Third Country.² The new proposals diverge in form—although not in substance—from the stay recognition requirements that are already in place in a number of jurisdictions, including in the U.K., France and Germany. Stakeholders have mentioned to the FMLC that their implementation is likely to be unnecessarily burdensome and costly for the industry as they would necessitate a market-wide repapering exercise on a tight timeline to amend existing contracts that already meet the relevant requirements at the national level. The FMLC would recommend that HM Treasury ensure that implementation of the final RTS does not impact the solutions for the contractual recognition of resolution stays which are already in place.

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 Perkins³
FMLC Chief Executive

² EBA, *EBA consults on technical standards for contractual recognition of stay powers under the BRRD* (15 May 2020), available at: <https://eba.europa.eu/eba-consults-technical-standards-contractual-recognition-stay-powers-under-brrd>

³ The FMLC is grateful to Ferdisha Snagg (Cleary Gottlieb Steen & Hamilton LLP) and Andrew Bagley (Goldman Sachs) for their contributions to, and comments on, this letter.