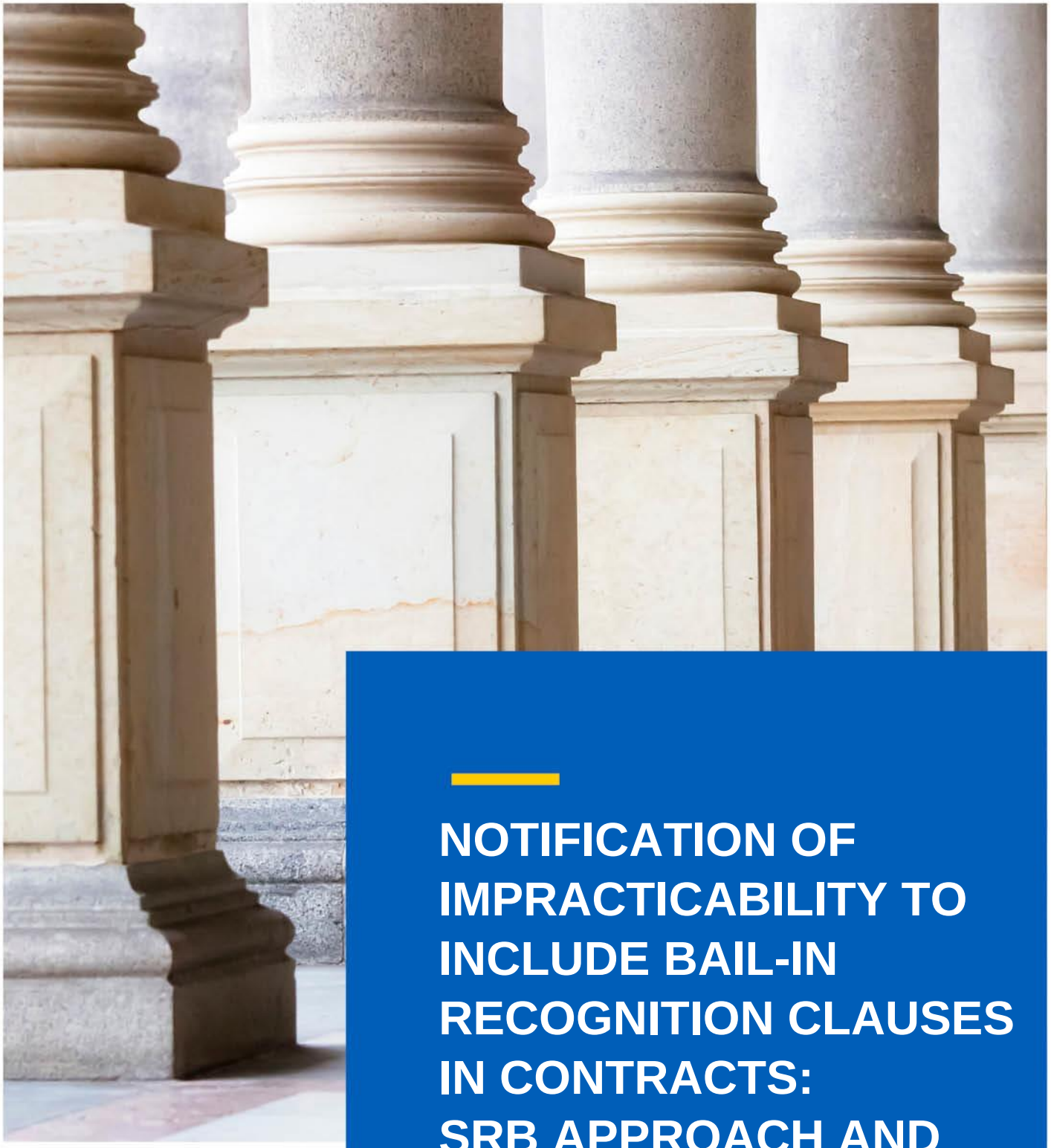

NOTIFICATION OF IMPRACTICABILITY TO INCLUDE BAIL-IN RECOGNITION CLAUSES IN CONTRACTS: SRB APPROACH AND EXPECTATIONS

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Single Resolution Board

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1. Background & overall approach

In line with Article 55 of the EU Bank Recovery and Resolution Directive 2014/59/EU (BRRD), banks are required to include specific terms (known as bail-in[1] recognition clauses) in relevant contracts governed by the law of a third country, to support effective write-down and conversion of the related liabilities by resolution authorities (RAs).

The SRB expects banks to prioritise the inclusion of bail-in recognition clauses in contracts where it matters most from a resolvability perspective, and to develop an implementation strategy supporting this prioritisation. Banks are expected to introduce such clauses first in the documentation supporting all Additional Tier 1 and Tier 2 instruments, as well as subordinated debt according to Article 48(1)(d) BRRD meeting the conditions of Article 55(1)(d) BRRD.[2] With regard to other liabilities, the main criteria for prioritising the introduction of bail-in recognition clauses are:

- The potential inclusion in the institution's minimum requirements for own funds and eligible liabilities (MREL);
- The relevance for the use of bail-in or write down and conversion powers;
- The sequence in which the capital instruments and eligible liabilities would be subjected to bail-in or to the write-down or conversion powers.

This shall neither limit authorities' powers under the BRRD and the SRMR to expose any liability to loss through bail-in or other resolution tools nor prevent RAs from requesting changes to the prioritisation proposed.

In line with Article 55(2) BRRD, banks may reach the determination that it is legally or otherwise impracticable to include bail-in recognition clauses in the contractual provisions governing a relevant liability, in which case they need to notify the RA. The impracticability process does not alter the existing obligation under the national transposition of Article 55(1) BRRD; it only provides a means of potentially removing a subset of liabilities from this obligation.

This paper outlines the SRB's procedural expectations with regard to such notifications, the conditions and categories for impracticability, as well as the process by which RAs may require banks to nevertheless include such clauses following the receipt of the notification. These are based on the applicable Delegated and Implementing Regulations.[3]

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[1] For the purpose of simplification, when this document refers to bail-in, it refers to both write-down and conversion powers under Article 21 SRMR and bail-in in the case of resolution. Similarly, when this document refers to bail-in-able instruments, it includes the instruments which may be subject to write-down and conversion.

[2] As noted below, these liabilities are not in scope of the impracticability process under Article 55(2) BRRD.

[3] Commission Delegated Regulation (EU) 2021/1527 of 31 May 2021 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards for the contractual recognition of write down and conversion powers; and Commission Implementing Regulation (EU) 2021/1751 of 1 October 2021 laying down implementing technical standards for the application of Directive 2014/59/EU of the European Parliament and of the Council with regard to uniform formats and templates for notifications of determination of the impracticability of including contractual recognition of write down and conversion powers.

2. Scope

2.1. Banks

All banks under the SRB's direct remit are subject to the provisions under the respective national laws that transpose Article 55 BRRD.

2.2. Instruments

Article 55(2) BRRD applies to a subset of bail-in-able liabilities governed by the law of a third country and otherwise meeting the conditions of Article 55(1) BRRD.

In this context, in accordance with the fourth subparagraph of Article 55(2) BRRD, AT1, T2 and unsecured debt instruments (i.e. bonds and other forms of transferable debt and instruments creating or acknowledging a debt) are not in scope of the impracticability notification and, when governed by the laws of a third country, have to contain bail-in recognition clauses.

In all cases, liabilities governed by third country law that are subject to the requirement to include a bail-in recognition clause in accordance with Article 55(1) BRRD, but which do not include the clause, even for reasons of impracticability, are not eligible for MREL.[4]

3. Notification and assessment process

Notifications under the process established under Article 55(2) BRRD depend on the bank itself first determining that it is impracticable to include a bail-in recognition clause in a particular contract, and are not otherwise required. A bank that includes a bail-in recognition clause in the third country law governed contracts to which it is party and which are within the scope of the obligation under Article 55(1) BRRD does not need to make any notification under this process.

The obligation to include the bail-in recognition clause is suspended from the date of notification.

[4] With the exception of certain instruments that were issued under UK law, please refer to https://srb.europa.eu/sites/default/files/uk_instruments_communication_march_2021.pdf.

3.1. Submission of notifications

Banks are expected to notify their national resolution authority (NRA)[5] in XBRL format, taking into account the taxonomy developed by the EBA in its Reporting Framework 3.0[6]. Banks are invited to liaise with their host NRA to prepare the introduction of XBRL reports.[7]

Where relevant, banks are encouraged to send notifications:

- per liability (based on template N.01.01), if any, on a quarterly basis, and
- per category (based on template N.01.02) on a semi-annual basis.

In both cases, banks are encouraged to send notifications within the last 10 working days of the first month of the period (i.e. January, April, July and October), except where indicated otherwise by the NRA.[8] If banks send ad hoc notifications, this may lead to longer processing times.

Banks are encouraged to make use of the categories of liabilities defined by the SRB in this document under section 4 below.[9] This section sets a preliminary list of categories, which will be reviewed as necessary. Banks are expected to report categories of liabilities under template N.01.02 on a forward-looking basis and include liabilities to be entered into within six months.

In all cases, the burden of proof of impracticability is on the bank making the notification.

3.2. Assessment of impracticability

The SRB, in cooperation with NRAs, will assess the notification, and may seek additional information from the bank in order to do so.

Following a complete notification, including additional information that may have been requested from the bank, the internal resolution team (IRT) will perform the assessment within the timeframe outlined under section 5 below.

When doing this, the SRB will take into account the nominal amount and remaining maturity of the contracts/liabilities, and pay particular attention to the following elements:

- in the case of notifications per liability in N.01.01: whether the condition (column 0140) and reason for meeting the condition (column 0160) are consistent with the elements listed under section 4 below;
- in the case of notifications per category in N.01.02: whether the reason for meeting the category (column 0030) is aligned with the basis for the category included in Annex I.

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[5] The NRA where the relevant entity is located. This approach is similar to the reporting of the Liability Data Report or other reports under Commission Implementing Regulation 2018/1624.

[6] https://www.eba.europa.eu/risk-analysis-and-data/reporting-frameworks/reporting-framework-3.0.

[7] If the bank considers it appropriate to send additional supporting documentation, such as a legal opinion or a copy of the contract, to support the notification, it will agree with the NRA how this should be sent.

[8] The NRA may specify any additional national-specific operational provisions regarding notifications.

[9] Banks are thereby encouraged to use template N01.02 where possible. Template N01.01 is to be used whenever banks determine impracticability for liabilities not captured under the SRB impracticability categories.

4. Conditions for impracticability

The bank's notification (unless made by category below) should include a determination that the liability in question satisfies one of the conditions of impracticability as defined in Article 1(1) of Commission Delegated Regulation (EU) 2021/1527:

a. the inclusion of the contractual term would constitute a **breach of the laws, regulations or administrative provisions of the third country** governing the liability;

b. the inclusion of the contractual term would be **contrary to an explicit and binding instruction from a third country authority**;

c. the liability arises from **instruments or agreements concluded in accordance with international standardised terms or protocols** that the bank is unable to amend;

d. the liability is governed by **contractual terms that the bank has to accept in order to be able to participate in or to utilise the services of a non-EU body**, and which the bank is unable to amend;

e. the liability is owed to a commercial or trade creditor and relates to **provision of goods or services that, while not critical, are used for daily operational functioning of the bank and the bank is unable to amend the terms of the agreement**.

With regard to c, d and e, banks are considered unable to amend the instruments or agreements or contractual terms where they can be concluded only under the terms set by the counterparty or by the applicable standard terms or protocols.

4.1. Categories of liabilities

Article 55(7) BRRD requires resolution authorities to specify, if deemed necessary, categories of liabilities for which banks may reach the conclusion that it is impracticable to include the relevant bail-in recognition clauses, based on the conditions above. The SRB has specified the following preliminary categories that banks may use (see Annex 1):

- **Liabilities resulting from trade finance operations** under internationally agreed frameworks and protocols.
- **Liabilities resulting from project finance activities** under official standardised terms.
- **Liabilities to FMI service providers,** where the services are provided on standard terms not susceptible to bilateral negotiation, including

  (i) liabilities to FMIs including trading venues, clearing houses, central counterparties, central securities depositories and securities settlement systems that are designated as such under their respective domestic legislation and subject as such to domestic supervision and/or oversight; and

  (ii) liabilities to FMI intermediaries related to the use of payment, clearing, settlement and custody services including custodians, clearing members of central counterparties and settlement agents within securities settlement systems.

- **Minor operating liabilities, arising from (non-critical) business operations**[10], where the terms of the contract are set by the provider and not bilaterally negotiated, such as travel tickets or utility bills.

4.2. Points of attention

Banks should ensure that their notifications are in line with the conditions defined in Commission Delegated Regulation (EU) 2021/1527 and provide adequate reasoning why those conditions are met.

- When reporting in categories in N.01.01 column 0150, banks are expected to use the specific wording: trade finance, project finance, FMI services, minor operating liabilities. When reporting in categories in N.01.02, banks are expected to use the associated category number, as per Annex I.[11]

- When reporting reasons in N.01.02 column 0030, banks should use wording aligned to the relevant basis provided in Annex I, where this is appropriate.

The contingent nature of a liability cannot be seen as a cause of impracticability per se. However, contracts for contingent liabilities can still be notified as impracticable as long as they meet one of the conditions above, or fall within one of the categories listed.[12]

5. Requirement to include bail-in recognition clauses

5.1. Conditions for requiring the inclusion[13]

In cases where the SRB does not assess the inclusion of the clause as impracticable,

- the bank will always be required to include the bail-in recognition clause where
    - the nominal amount of the liability created by the relevant agreement or instrument is equal to/more than EUR 20 million, or
    - its remaining maturity[14] is equal to/longer than six months.
- when neither of the thresholds is met, the bank will be requested to include contractual bail-in recognition clauses only if the SRB considers it necessary to ensure resolvability. For this purpose,

[10] Where not already excluded by Article 44(2)(g)(ii) BRRD.

[11] N 01.01-c0150 is a free text field (i.e. a string) and N 01.02-c0010 must contain a number (i.e. an integer), as per the EBA Reporting Framework 3.0.

[12] Please refer to the EBA feedback on the public consultation in Section 5.3 of the report at https://www.eba.europa.eu/eba-publishes-final-draft-technical-standards-impracticability-contractual-recognition-under-brrd.

[13] Article 55(2) BRRD.

[14] The date upon which all principal and interest of the liability must be repaid (based on the transaction contractual documentation), in accordance with the instructions in Annex II of Commission Implementing Regulation (EU) 2021/1751.

the SRB will take into account elements such as the amount and type of the agreement or instrument; the feasibility of using resolution tools; the ranking of the liability in normal insolvency proceedings under national law; the maturity of the liability and the revolving nature of the contract.

In addition, the bank may also be required to amend its practices concerning the application of the impracticability exemption, such as the inclusion of liabilities under the SRB's pre-defined categories.[15]

5.2. Timeframe for the SRB to require the inclusion[16]

The SRB will assess the complete notification, and, if necessary, require the inclusion based on the conditions above within three months of the date of receipt. This period may be extended by three months[17] in complex cases and, if so, the bank will be informed of the extension and rationale.

If the SRB does not require the inclusion of a bail-in recognition clause within that timeframe, the obligation to include the clause (in the contracts notified) will not be imposed.

[15] Article 55(2) third subparagraph BRRD.
[16] Article 55(2) BRRD.
[17] By 6 months during a transition period of one year.

Annex I: Categories of liabilities

#[17]	Category	Definition	Typical types of Liability /Instrument[18]	Typical basis for condition/category	Delegated Regulation 2021/1527 condition
10	**Trade Finance**, international standardised terms	Liabilities deriving from trade finance activities, where governed by contracts under international standardised terms.	Guarantee/counter-guarantee e.g. demand guarantee. Performance guarantee e.g. bid bonds, performance bonds, advance payment bonds, retention bonds, tender bonds. Letter of credit, e.g. import letter of credit, export letter of credit, sight letter of credit, standby letter of credit (SLOC) e.g. financial or performance SLOC.	Issued e.g. under International Chamber of Commerce (ICC) Uniform Rules for Demand Guarantee (URDG) 458 or 758, ICC Uniform Custom & Practice (UCP) 600, URDG 758 or (International Standby Practices) ISP 98	c
20	**Project Finance**, official terms	Liabilities deriving from project finance type activities, where governed by contracts under officially standardised terms by a third country authority.	Performance guarantee, e.g. bid bonds, performance bonds, advance payment bonds, retention bonds, tender bonds.	Where templates issued by a third country authority must be used without alteration, or Where terms/conditions are imposed under official tender procedures (e.g. government authority/statutory body tenders a project).	b or c

[17] For different insolvency rankings within the same category, please use incremental numbers, as column 0010 in N.01.02 is the key to that template. For example, if the institution wishes to notify two types of trade finance liabilities with different insolvency rankings, it should do so using (in column 0010) the numbers 10 and 11 in different rows.

[18] These instruments are artificially separated for readability – in practice there is overlap (instruments such as bid or performance bonds may be structured as e.g. demand guarantees or SLOCs) and there may be differences in terminology.

#[17]	Category	Definition	Typical types of Liability /Instrument[18]	Typical basis for condition/category	Delegated Regulation 2021/1527 condition
30	**FMI services**[19], standard terms imposed by service provider	Liabilities arising from direct or indirect membership/participation in trading venues, payment or settlement systems, trade repositories or CCPs established in third countries and subject to rulebooks or other standard contracts. Liabilities arising from FMI services provided by FMI intermediaries, where the service contracts are not individually negotiated.	Positions in CCPs. Membership fees, liabilities in respect of default fund contributions. Intraday credit offered by FMI service providers, e.g. payment systems or securities settlement systems or FMI intermediaries such as custodian banks.[20]	Issued under the rulebook or set of contracts applicable to FMI members or participants; or under FMI services contract with other FMI services provider, relating to the provision of payment services, as well as payment, custody, clearing and settlement services in relation to securities and derivatives, provided the agreements are on standardised terms set by the service provider.	d
40	**Minor operating liabilities**, standard terms imposed by service provider	Liabilities owed to commercial or trade creditors arising from the non-critical business operations of the company, where the terms of the contract are set by the provider and not bilaterally negotiated.	Some liabilities under accounts payable: e.g. travel tickets, hotel bills, utility bills, invoices for (non-critical) IT or accounting services.	Issued under standard non-negotiable contract issued by service provider.	e

[19] In this context, FMI services also cover membership of trading venues and trade repositories.

[20] Note that the short duration of these exposures makes them likely to be exempt from bail-in under Article 44(2)(f) BRRD.