



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

Consultation Paper | CP19/15

Contractual stays in financial contracts governed by third-country law

May 2015

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This consultation paper proposes a new rule for the Prudential Regulation Authority (PRA) Rulebook requiring the contractual adoption of UK resolution stays in certain financial contracts governed by third-country law (that is, the law of a jurisdiction outside the European Economic Area).

The Bank of England and the PRA reserve the right to publish any information which it may receive as part of this consultation.

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Responses are requested by Wednesday 26 August 2015.

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1 Overview

Introduction

1.1 This consultation paper (CP) sets out a proposal for a rule that would apply to Prudential Regulation Authority (PRA)-authorised UK banks, building societies and PRA-designated UK investment firms, as well as their qualifying parent undertakings ('firms') in respect of financial contracts governed by third-country law (that is, the law of a jurisdiction outside the European Economic Area (EEA)). The proposed rule would prohibit firms from creating new obligations or materially amending an existing obligation under such a financial contract without the required counterparty agreement. The prohibition applies unless the counterparty has agreed in writing to be subject to similar restrictions on early termination and close-out to those that would apply as a result of the firm's entry into resolution (or the write down or conversion of the firm's regulatory capital at the point of non-viability) if the financial contract were governed by the laws of the United Kingdom. In addition, relevant firms that are parent undertakings would be obliged to ensure that their subsidiaries that are credit institutions, investment firms or financial institutions⁽¹⁾ also trade on this basis.

1.2 The proposed rule is intended to reduce the risk of contagion from the failure of a relevant firm and support its orderly resolution by ensuring that resolution action taken against a relevant firm would not immediately lead to the early termination of its financial contracts governed by third-country law while its financial contracts governed by the laws of the United Kingdom or another European Union (EU) jurisdiction were stayed.

1.3 The CP is relevant to PRA-authorised UK banks, building societies, PRA-designated UK investment firms and their qualifying parent undertakings, which for this purpose comprise financial holding companies and mixed financial holding companies, as well as credit institutions, investment firms and financial institutions that are subsidiaries of these firms, regardless of their location. The CP and proposed rule are also relevant to counterparties of the above-listed entities to the extent that counterparties have financial contracts with such entities governed by third-country law.

Background

1.4 During the financial crisis, public funds were used to deal with distress in a number of banks. The crisis revealed serious shortcomings in the existing tools available to authorities for preventing or tackling failures of systemic banks, highlighting the dilemma of 'too big to fail'. Much work has been done since the financial crisis to address this problem, both at the international and national level. Among the policy solutions has been the development of comprehensive bank recovery and resolution regimes, such as that set out in the EU Bank

Recovery and Resolution Directive (BRRD).⁽²⁾ These are intended to provide the tools for handling national and cross-border bank failures, and to seek to reduce the potential public cost of future financial crises.

Resolution stays

1.5 A key aspect of effective resolution is ensuring that, once a firm enters resolution, its counterparties in derivatives and other financial contracts⁽³⁾ (such as repo/reverse repo, securities financing and other, similar transactions subject to contractual set-off and netting arrangements) cannot terminate and close out their positions solely as a result of the firm's (or a related entity's) entry into resolution.

1.6 A suspension, or 'stay', on the exercise of early termination rights in these circumstances assists in avoiding a disorderly, value-destructive close-out of financial contracts and liquidation of collateral that could accelerate contagion and undermine financial stability and promotes the continuity during resolution of a variety of critical economic functions.

1.7 The BRRD, as transposed into the Banking Act 2009 (Banking Act), gives the Bank of England, as resolution authority, the power to suspend temporarily the termination rights of any party⁽⁴⁾ to such a contract, provided that the UK institution continues to perform its payment and other substantive obligations under the contract (the temporary stay).⁽⁵⁾ It further provides that a resolution action (or pre-resolution action) by the Bank of England, the PRA or the Financial Conduct Authority cannot give rise to a counterparty's right to terminate a contract with a UK credit institution or investment firm or to exercise rights over collateral (the general stay).⁽⁶⁾

Cross-border limitations

1.8 The BRRD ensures that a UK stay would automatically be recognised and given effect throughout the EU. Where a contract is governed by the law of a non-EU country, however, it is unclear that a court in that jurisdiction would enforce the UK stay over the contractual terms unless the law of that jurisdiction expressly recognised foreign resolution actions.

1.9 As a result, counterparties under contracts governed by third-country law would potentially be able to exercise early termination rights in resolution, while counterparties under contracts governed by UK law (or the law of another EU Member State) would be prevented from doing so. The

(1) As such terms are defined in the Capital Requirements Regulation (575/2013) (CRR) on prudential requirements for credit institutions and investment firms.

(2) Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms.

(3) For the definition of 'financial contract' see paragraph 2.5 of this CP and the draft rule text in the appendix.

(4) Other than 'excluded parties' (payment and securities settlement systems, central counterparties and central banks), as defined by section 70D(1) of the Banking Act.

(5) Section 70C(1) of the Banking Act.

(6) Section 48Z(6) of the Banking Act.

mismatch that would result on resolution could significantly increase the adverse effect of a UK firm's failure.

Financial Stability Board initiatives to improve cross-border recognition of resolution

1.10 This proposal arises in the context of the efforts of the Financial Stability Board (FSB) and its member authorities, including the Bank of England, to address the problem of 'too big to fail', in particular by improving the reach of domestic resolution regimes through measures to ensure the effective recognition of resolution actions across borders.

1.11 In its 2011 publication, *Key Attributes of Effective Resolution Regimes for Financial Institutions (KAs)*,⁽¹⁾ the FSB recognised the need for 'transparent and expedited processes to give effect to foreign resolution measures' in order to resolve banking groups that trade in multiple jurisdictions and under multiple legal systems. In September 2014 the FSB published a Consultative Document⁽²⁾ with specific proposals to improve cross-border recognition of resolution actions. In the Consultative Document, the FSB called on FSB member jurisdictions to enact, in line with the KAs, statutory cross-border recognition frameworks as the long-term solution to this problem, and proposed elements for such a regime that FSB member jurisdictions should consider including in their legislation. As an interim solution, the FSB also proposed contractual approaches that could be implemented in the near term to achieve cross-border recognition of particularly critical elements of resolution, including restrictions (stays) on early termination rights in financial contracts.

1.12 The International Swaps and Derivatives Association (ISDA) 2014 Resolution Stay Protocol (the ISDA Protocol),⁽³⁾ an industry initiative supported by the Bank of England and other FSB member jurisdictions and regulatory authorities, is an example of the kind of contractual approach intended by these recommendations. The ISDA Protocol applies to bilateral over-the-counter (OTC) derivatives documented under the 1992 or 2002 ISDA Master Agreement. If both parties adhere to the ISDA Protocol, it serves to amend the terms of their master agreement to incorporate the stay recognition provisions. Eighteen of the world's largest dealer banks adhered to the ISDA Protocol when it came into effect on 1 January 2015. The PRA expects a similar solution to be developed this year for the standardised documentation for securities financing and repo transactions. The PRA anticipates that firms will take advantage of these standardised amendments in complying with the proposed rule.

1.13 FSB member authorities, including the Bank of England, have committed to support the ISDA Protocol and similar industry initiatives, including with regulation where necessary. The proposal in this paper is part of a co-ordinated effort

among regulatory and resolution authorities in the United Kingdom, France, Germany, Japan, Switzerland and the United States to require banks and other financial institutions to incorporate recognition of the domestic resolution stay regime into their financial contracts where these are governed by foreign law.

1.14 The proposed rule is also part of broader co-operation between the PRA, as competent authority, and the Bank of England, as resolution authority, to reduce the impact of bank failure. If the proposed rule is made, the PRA and the Bank of England will both monitor the rule's effect on firms' activity in this area and take steps to address any gaps where necessary. Such steps could take the form of a PRA supervisory requirement or a Bank of England requirement to remove an impediment to effective resolution, as may be appropriate in light of the facts of the individual case and the objectives of each authority.

Statutory obligations

1.15 In discharging its general functions of making rules, and determining the general policy and principles by reference to which it performs particular functions, the PRA must, so far as reasonably possible, act in a way that advances its general objective to promote the safety and soundness of the firms it regulates, including by seeking to minimise the adverse effect that the failure of a firm could be expected to have on the stability of the UK financial system.⁽⁴⁾

1.16 The proposed rule is intended to limit the market contagion and risk to financial stability that might otherwise result from mass close-out of financial contracts following a firm's entry into resolution. The PRA believes the proposal in this CP will advance the PRA's general objective.

1.17 In making its rules and establishing its practices and procedures, the PRA must have regard to the Regulatory Principles as set out in Financial Services and Markets Act 2000 (FSMA), including proportionality.⁽⁵⁾ In addition, when consulting on draft rules, the PRA is required to consider the impact on mutuals,⁽⁶⁾ and any equality and diversity effects.⁽⁷⁾

Impact on mutuals

1.18 The PRA has a statutory obligation to state whether the impact of proposed rules on mutuals will be significantly different from the impact on other firms.⁽⁸⁾ The proposed new

(1) Available at www.financialstabilityboard.org/publications/r_1111104cc.pdf and subsequently updated in October 2014 at www.financialstabilityboard.org/wp-content/uploads/r_141015.pdf.

(2) Available at www.financialstabilityboard.org/wp-content/uploads/c_140929.pdf.

(3) Available at www2.isda.org/functional-areas/protocol-management/protocol/20.

(4) Section 2B of the Financial Services and Markets Act 2000 (FSMA).

(5) Section 3B of FSMA.

(6) Section 138K of FSMA.

(7) Section 149 of the Equality Act 2010.

(8) Section 138K of FSMA.

rule would apply to mutuals (other than credit unions). The impact on mutuals, however, would not be different from the impact on other, similarly placed firms.

Impact on competition

1.19 When discharging its general functions in a way that advances its primary objectives the PRA has a secondary objective to facilitate effective competition, insofar as reasonably possible, in the markets for services provided by PRA-authorized persons when they carry on regulated activities.⁽¹⁾

1.20 As a result of the introduction of the BRRD, counterparties of UK firms trading under contracts governed by UK law (or the law of another EU Member State) are subject to a stay on termination rights, whereas counterparties trading under contracts governed by third-country law may not be subject to the stay. This mismatch results in a situation where counterparties trading under UK law or the law of another EU Member State cannot terminate their positions while counterparties trading under third-country law potentially can. The proposed rule would remove this distinction. It would ensure that firms operate in a harmonised environment in respect of the applicability of stays and act to minimise, to the extent practicable, unjustified differences in regulatory treatment, both of which should facilitate effective competition.

1.21 Other jurisdictions are working to implement domestic stays and impose similar requirements to extend the applicability of their respective resolution regimes to those contracts not governed by their domestic law. These efforts aim to capture significant cross-border activities globally, discouraging market fragmentation in light of a favourable degree of harmonisation.

1.22 On a going-concern basis as well as at the time of actual resolution, firms and market participants more broadly would be able to determine clearly and rapidly that resolution stays are recognised on a cross-border basis. Greater transparency should enhance the predictability of, and confidence in, resolution regimes and promote the well-functioning of the relevant markets.

Equality and diversity

1.23 The PRA may not act in an unlawfully discriminatory manner. It is also required under the Equality Act 2010 to have regard to the need to eliminate discrimination and to promote the equality of opportunity in carrying out its policies, services and functions.⁽²⁾ To meet this requirement, the PRA assesses the equality and diversity implications of any new policy proposals considered. The PRA believes that the proposal in this CP does not give rise to equality and diversity implications.

Cost benefit analysis

1.24 The PRA is also required to perform a cost benefit analysis (CBA) of the impact of its policy proposals. A CBA is included in Chapter 4.

Responses and next steps

1.25 This consultation closes on Wednesday 26 August 2015. Views are welcome on the issues raised in the CP. Please address any comments or enquiries to CP19_15@bankofengland.co.uk.

1.26 In particular, respondents may wish to comment on the following proposals:

- the group subsidiaries that are included within the scope of the rule;
- the contracts to which the requirement applies, including the exclusions; and
- the timing and structure of the transitional arrangements.

1.27 The PRA also invites firms to include in their response their own assessment of the impact of the proposal, including where relevant quantitative information on the number of contracts, master agreements and counterparties affected.

2 The proposed rule

2.1 This chapter explains the elements of the PRA's proposed rule.

The contractual stay requirement

2.2 The proposed rule would apply to PRA-authorized UK banks, building societies and PRA-designated UK investment firms as well as their qualifying parent undertakings⁽³⁾ ('firms') in respect of specified financial contracts governed by the law of a non-EEA jurisdiction. It would prohibit firms from creating new obligations or materially amending an existing obligation under such a financial contract without the required counterparty agreement. The prohibition applies unless the counterparty has agreed in writing to be subject to similar restrictions on termination, acceleration, close-out, set-off and netting as would apply as a result of the firm's entry into resolution (or the write down or conversion of the firm's regulatory capital

(1) Section 2H of FSMA.

(2) Section 149 of the Equality Act 2010.

(3) As defined in section 192B of FSMA and the Financial Services and Markets Act 2000 (Prescribed Financial Institutions) Order 2013, a 'qualifying parent undertaking' is, for the purposes of the proposed rule, a financial holding company or a mixed financial holding company (as such terms are defined in the CRR) incorporated or with a place of business in the United Kingdom. It would not include a mixed activity holding company (that is, a holding company whose subsidiaries are not exclusively or mainly credit institutions, investment firms or financial institutions).

at the point of non-viability)⁽¹⁾ if the contract were governed by the laws of the United Kingdom (and, where the relevant firm is not a credit institution or investment firm, as if it were one).

2.3 Firms would also be obliged to ensure that, where their subsidiary credit institutions, investment firms and financial institutions⁽²⁾ trade in these products under third-country law, the subsidiaries also obtain agreement to the stay from their counterparties. Affected subsidiaries would include banks, brokers, asset managers and other providers of related financial services as well as intermediate holding companies.

2.4 The focus of the rule on banking and investment firm groups matches the scope of the existing resolution framework under the Banking Act. By extending the reach of the stay to other group entities, the proposed rule would reduce the risk of contagion between the parent firm and the rest of the group, improve the feasibility of resolution of a UK banking group and reduce the scope for regulatory arbitrage.

2.5 The rule is based on the definition of 'financial contract' in the BRRD, except that the rule would not apply to short-term interbank borrowing and would make clear that all derivatives and master currency agreements are in scope. As a result the rule would apply to obligations created under:

- securities contracts including: contracts for the purchase, sale or loan of a security or a group or index of securities; options on a security or a group or index of securities; or repo or reverse repo transactions on a security or a group or index of securities;
- commodities contracts including: contracts for the purchase, sale or loan of a commodity or a group or index of commodities; options on a commodity or a group or index of commodities; or repo or reverse repo transactions on a commodity or group or index of commodities;
- futures and forwards contracts, including contracts (other than a commodities contract) for the purchase, sale or transfer of a commodity or property of any other description, service, right or interest for a specified price at a future date;
- swap agreements including: swaps and options relating to interest rates; foreign exchange agreements; currency; equities/equity indexes; debt/debt indexes; commodities/commodity indexes; weather; emissions or inflation; total return, credit spread or credit swaps; or any similar agreement;
- all other derivatives;⁽³⁾ and

- master agreements for any of the above or for contracts for the sale, purchase or delivery of a currency.

2.6 Obligations under financial contracts entered into with designated payment and securities settlement systems, recognised central counterparties, central banks⁽⁴⁾ or central governments, however, would be excluded.

Timing and transitional arrangements

2.7 Subject to the transitional arrangements set out below, the rule would apply in respect of obligations created under relevant financial contracts on or after 1 January 2016. Firms could not create new obligations under existing master agreements unless those agreements were appropriately amended. For this purpose the PRA considers that the rollover or renewal of a transaction entered into prior to the applicable date of the rule would constitute a new obligation that must contain the appropriate contractual terms.

2.8 The rule would also apply to obligations created prior to the applicable date of the rule if a material amendment is made to the substantive terms of a relevant obligation. This would not include changes that occur automatically by the terms of the contract, such as interest or exchange rate resets, nor would it apply to simple administrative changes. It aims to prevent firms from avoiding the application of the rule by actively changing the commercial parameters (such as interest or exchange rate, date of payment or reference asset) of an existing obligation in a way that would achieve the commercial intent of an ongoing trading relationship without technically creating a 'new obligation'.

2.9 The PRA proposes to stagger the effective date of the rule by counterparty type, as follows:

- 1 January 2016: credit institutions and investment firms.
- 1 July 2016: asset managers (and the funds they manage), insurers and other counterparties that act on an agency basis.
- 1 January 2017: all other counterparties.

2.10 The PRA considered staggering the effective date of the rule on the basis of the type of financial contract involved (for

(1) The Bank of England is obliged in the circumstances set out in sections 6A and section 81AA of the Banking Act to write down or convert to equity a relevant firm's regulatory capital instruments at the point of non-viability (PONV). The Banking Act (in section 48Z) classifies the PONV write down or conversion as a 'crisis prevention measure', ie a pre-resolution regulatory action. While the proposed rule would apply to a stay relating to a PONV write down or conversion, it would not apply to a stay relating to any other crisis prevention measure.

(2) As defined in the CRR (see footnote 1 on page 5).

(3) As defined in Article 2(5) of the European Market Infrastructure Regulation (648/2012) on OTC derivatives, central counterparties and trade repositories.

(4) These three categories are 'excluded persons', as defined in section 70D(1) of the Banking Act, to whom the temporary stay in section 70C of the Banking Act does not apply.

instance, OTC derivatives and securities financing transactions). In discussions with industry representatives, however, some indicated a preference for amending financial transaction documentation on a counterparty-by-counterparty basis, rather than a product-by-product basis, in order to maintain the benefits of cross-product netting and overall portfolio margining. The PRA further recognises that counterparties that act as agent or have otherwise a fiduciary duty to their clients (such as asset managers and insurers) may need additional time to consult their clients and obtain their consent before they can agree to the necessary amendments on their clients' behalf. It is these considerations that have influenced the PRA's approach to staggering implementation.

Proposed rule text

2.11 The proposed rule is set out in full in Appendix 1.

3 Recording information on financial contracts

3.1 This chapter discusses the PRA's expectations in respect of the information that in-scope firms maintain concerning the financial contracts they and their subsidiaries have entered into.

3.2 The BRRD empowers competent authorities and resolution authorities to require a firm to maintain detailed records of financial contracts. The European Banking Authority (EBA) is currently consulting on draft Regulatory Technical Standards (RTS) under BRRD Article 71(8), which will set out a minimum set of information concerning financial contracts that a firm must be obliged to record if its resolution plan foresees that resolution action will be taken in respect of it.⁽¹⁾ In light of the ongoing work in this area, the PRA does not consider it necessary to impose a separate information obligation to monitor compliance to the proposed rule at this time, but will revisit the issue when the final RTS come into effect.

3.3 While the PRA is not proposing to require firms to record or make regular reporting on their financial contracts, it does expect firms to be able to provide information on their financial contracts, including the governing law and whether the contract contains the necessary recognition provision. If necessary in an individual case, the PRA (or, where appropriate, the Bank of England) may require the relevant firm to provide this information, for instance, as part of Phase 2 of resolution planning or contingent information requests as set out in Supervisory Statement 19/13.⁽²⁾

4 Cost benefit analysis

4.1 This section sets out an analysis of the costs and benefits of implementing the proposed PRA rules in the United Kingdom as required by FSMA.⁽³⁾

Benefits of the proposal

4.2 One of the PRA's objectives is to promote the safety and soundness of the firms it regulates, in particular by seeking to minimise the adverse effect that the failure of a PRA-authorized person could be expected to have on the stability of the UK financial system.⁽⁴⁾ The PRA, in co-operation with the Bank of England as resolution authority, seeks to ensure that firms can fail without causing the type of disruptions experienced in the financial crisis.

4.3 Preventing the close-out of contracts governed by third-country law, whether at entity level or elsewhere within the group, is an important step in supporting these objectives. Contracts governed by third-country law carry the risk of triggering chains of early terminations and realisation of collateral, which can have an immediate effect on financial markets and financial stability (as seen in connection with the failure of Lehman Brothers). The application of stays, to the fullest extent practicable, most effectively addresses these risks.

4.4 It is necessary to extend the scope of the stay to critical players in financial markets across counterparty types and locations to address effectively the systemic nature of contagion risk, but also to improve market transparency and clarity with respect to the effect of entry into resolution and to minimise any competitive disadvantage that may accrue to affected firms. This is described in paragraph 1.20.

4.5 Disorderly termination of third-country law contracts alone could materially impact firms and undermine resolvability, deterring authorities' ability to ensure continuity of their critical economic functions. In particular, where the United Kingdom is home authority for a group with cross-border activity, extending the reach of the stay to third-country law contracts entered into by firms or their relevant subsidiaries is crucial to enable the stabilisation of the entire group.

4.6 By enabling the stabilisation of firms in an orderly resolution and by limiting the scope for resolution to lead to widespread close-out of positions or collateral and the accompanying damage to financial markets, the proposed rule

(1) Details of the proposed RTS can be found on the EBA's website at [www.eba.europa.eu/documents/10180/1006126/EBA-CP-2015-04+\(CP+on+Detailed+records+of+financial+contracts\).pdf](http://www.eba.europa.eu/documents/10180/1006126/EBA-CP-2015-04+(CP+on+Detailed+records+of+financial+contracts).pdf).

(2) *PRA Supervisory Statement SS19/13*, 'Resolution planning', updated in January 2015; www.bankofengland.co.uk/pradocuments/publications/ss/2015/ss1913update.pdf.

(3) Section 138J of FSMA.

(4) Section 2B of FSMA.

provides significant benefit in preserving the stability of the UK financial system, promoting effective competition and transparency, and preventing the costs associated with market disruptions.

Costs of the proposal

4.7 For firms that do not enter into contracts governed by third-country law, there will be no economic impact or direct cost as a result of the proposed rule.

4.8 There will be compliance costs, however, for affected firms and their relevant subsidiaries which are required to obtain counterparty agreement in writing to give effect to this rule. Due to insufficient data on the relevant markets, in particular the number of contracts and counterparties affected, the PRA assesses that it is not reasonably practicable to quantify these costs. Surveys carried out with firms and industry groups indicate that contracts governed by third-country law represent approximately 20% of the relevant markets.⁽¹⁾ The PRA recognises that this portion may nonetheless represent a significant number of client agreements and that the rule will impose a logistical burden on affected firms to amend these agreements to comply with the rule. In particular, counterparties that act as agent or have otherwise a fiduciary duty to their clients may need additional time to consult their clients and obtain consent before they can agree to the necessary amendments on their clients' behalf. The existing ISDA Protocol and the extension of the Protocol technology to other standardised financial contracts will facilitate compliance. The PRA expects firms will take advantage of the economies that these standard amendments provide.

4.9 The PRA does not expect compliance with the proposed rule to have an impact on a firm's regulatory capital requirements for counterparty risk associated with the relevant financial contracts.

4.10 It is estimated that compliance could take several months for larger and more complex client bases. As a result, the PRA proposes transitional arrangements and compliance periods, staggered by counterparty type, as described in paragraph 2.9.

4.11 The PRA is not proposing to impose specific recording or reporting requirements on firms in connection with the proposed rule for the reasons set out in Chapter 3. While firms will need to be able to show compliance with the proposed rule, the PRA does not expect this to impose material costs on firms.

4.12 In theory, the introduction of contractual recognition of stays for contracts governed by third-country law could impact credit management practices. The assessment of loss given default could change to reflect the inability to close out

positions at the point of resolution. If this leads to some increase in the interest rate investors are willing to accept for riskier and more systemic firms, the increase should reflect a proper valuation of the risk of failure and account for effective resolution regimes. Experience from the introduction of domestic stays, however, did not indicate any impact on credit management practices.

4.13 In addition, counterparties are protected by important statutory safeguards on the use of the stay. Foremost among these safeguards are the obligation of continued payment performance and the guarantee of not being made worse off relative to an insolvency scenario (the 'no creditor worse off' principle), which protect counterparties from potential adverse economic impact resulting from resolution measures. Another key safeguard is the protection of netting arrangements, rights of set-off and credit support arrangements (including title transfer arrangements), which preserves the intended economic structure of counterparties' exposure to firms in resolution. Collateral arrangements are similarly protected, in that the collateral attached to a secured liability may not be transferred unless the underlying obligation is also transferred.

(1) In July 2014, the PRA and other FSB regulatory authorities carried out a global data collection exercise to assess the level of cross-border activity in uncleared OTC derivatives markets among the 18 financial groups which adhered to the ISDA Protocol on its inception in January 2015. It was estimated that approximately 20% of the outstanding notional in these markets involves a foreign counterparty under financial contracts governed by third-country law. Although more limited, the information available on global securities financing markets indicates a similar level of cross-border activity.

Appendix

1 PRA Rulebook: CRR firms and non-authorised persons: stay in resolution instrument 2015

PRA RULEBOOK: CRR FIRMS AND NON-AUTHORISED PERSONS: STAY IN RESOLUTION INSTRUMENT 2015

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (the PRA’s general rules);
 - (2) section 137T (general supplementary powers); and
 - (3) section 192JB (rules requiring parent undertakings to facilitate resolution).
- B. The PRA exercises the following powers in the Act to make those terms in the Glossary that are used in this instrument in rules applicable to qualifying parent undertakings:
- (1) section 192JB (rules requiring parent undertakings to facilitate resolution); and
 - (2) section 137T (general supplementary powers).
- C. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

- D. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook: CRR Firms and Non-Authorised Persons: Stay in Resolution Instrument 2015

- E. The PRA makes the rules in the Annex to this instrument.

Commencement

- F. This instrument comes into force on [DATE].

Citation

- G. This instrument may be cited as the PRA Rulebook: CRR Firms and Non-Authorised Persons: Stay in Resolution Instrument 2015.

By order of the Board of the Prudential Regulation Authority

[DATE]

Annex

In this Annex, the text is all new and is not underlined.

Part

STAY IN RESOLUTION

Chapter content

- 1. APPLICATION AND DEFINITIONS**
- 2. STAY IN RESOLUTION**
- 3. TRANSITIONAL PROVISIONS**

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to a *BRRD undertaking* which is:

- (1) a *CRR firm*;
- (2) a *financial holding company*; or
- (3) a *mixed financial holding company*.

1.2 A *BRRD undertaking* that is a *parent undertaking* must ensure that a *subsidiary* which meets the condition in 1.3 complies with the requirements of this Part as if it were a *BRRD undertaking* subject to those requirements.

1.3 The condition in 1.2 is that the *subsidiary* is:

- (1) a *credit institution*;
- (2) an *investment firm* or an *undertaking* which would be an *investment firm* if it had its head office in an *EEA State*; or
- (3) a *financial institution*; and

is not a *BRRD undertaking* which falls within 1.1.

1.4 In this Part, the following definitions shall apply:

AIF

has the meaning given in point (a) of Article 4(1) of the *AIFMD*.

AIFMD

means Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

crisis prevention measure

has the meaning given in section 48Z of the Banking Act 2009.

excluded person

has the meaning given in section 70D(1) of the Banking Act 2009.

financial arrangement

includes the following contracts and agreements:

- (a) financial contracts as defined in point 100 (a) to (d) of Article 2(1) of the *BRRD*;
- (b) a derivative as defined in Article 2(5) of Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4th July 2012 on OTC derivatives, central counterparties and trade repositories; and
- (c) a master agreement in so far as it relates to:

- (i) any of the contracts or agreements referred to in points (a) and (b);
or
- (ii) a contract for the sale, purchase or delivery of the currency of the UK or any other country, territory or monetary union.

Special Resolution Regime

means the provisions of Part I of the Banking Act 2009 and any measure taken under that Part.

termination right

has the meaning given in section 70C(10) of the Banking Act 2009.

UCITS

has the meaning given in point (ao) of Article 4(1) of the *AIFMD*.

- 1.5 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 STAY IN RESOLUTION

- 2.1 A *BRRD undertaking* must not create a new obligation or materially amend an existing obligation under a *financial arrangement* that is governed by the law of a *third country* unless the condition in 2.2 is met.
- 2.2 The condition is that the counterparty to the *financial arrangement*, other than a counterparty which is an *excluded person* or a central government, agrees in writing that it shall be entitled to exercise *termination rights* under the *financial arrangement* to the extent that it would be entitled to do so under the *Special Resolution Regime* if:
- (1) the *financial arrangement* were governed by the laws of the *UK*; and
 - (2) where the *BRRD undertaking* is not a *CRR firm*, the *BRRD undertaking* were a *CRR firm*.
- 2.3 For the purpose of 2.2, section 48Z of the Banking Act 2009 is to be disregarded to the extent that it relates to a *crisis prevention measure* other than the making of a mandatory reduction instrument by the Bank of England under section 6B of the Banking Act 2009.

3 TRANSITIONAL PROVISIONS

- 3.1 From 1 January 2016 this Part applies in relation to a *financial arrangement* under 2.1 where the counterparty is:
- (1) a *credit institution*;
 - (2) an *investment firm*; or
 - (3) an *undertaking* which would be an *investment firm* if it had its head office in the *EEA*.

3.2 From 1 July 2016 this Part also applies in relation to a *financial arrangement* under 2.1 where the counterparty is:

- (1) an *asset management company*;
- (2) an *AIF*;
- (3) a *UCITS*;
- (4) an *insurer*; or
- (5) a counterparty that acts on an agency basis.

3.3 From 1 January 2017 this Part applies in relation to all *financial arrangements* under 2.1 where the counterparty is not an *excluded person* or a central government.