

IMPORTANT INFORMATION ABOUT

BANK RECOVERY AND RESOLUTION DIRECTIVE (“BRRD”)

This note does not constitute and is not intended to provide legal advice. If you have any questions or concerns, you should speak to your own legal adviser.

Save where the context otherwise required, the following words and phrases shall have the following meanings in this document:

“Bank Recovery and Resolution Directive” or “BRRD”	means Directive 2014/59/EU;
“BRRD Entity”	means EEA or UK based entities within the scope of the BRRD or UK BRRD respectively, including credit institutions, certain investment firms and/or their EEA/UK subsidiaries or parents). For the avoidance of doubt, this includes Sova Capital Limited;
“BRRD Resolution Authority”	means any resolution authority empowered to apply the resolution tools or exercise the resolution powers under the BRRD or UK BRRD;
“UK BRRD”	means the UK’s amended version of the BRRD, which includes UK Banking Act 2009 (Part I) 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), applicable from the Effective Date;
“Effective Date”	means 31 December 2020, end of transition period agreed between the EEA and the UK as part of the UK exit from the EU.

The BRRD introduced resolution tools for BRRD Resolution Authorities to ensure that such authorities have additional powers when dealing with firms that are within the scope of the BRRD. These tools, described more fully below, are: (1) the “bail-in” tool, (2) the “sale of business” tool, (3) the “bridge institution” tool, and (4) the “asset separation” tool.

Broadly, the BRRD introduced powers to: (a) take control of a BRRD Entity and exercise all the rights and powers conferred upon its shareholders, other owners and its management body or to remove or replace it; (b) transfer all or some of the shares or other instruments of ownership issued by, or some or all of the assets, rights or liabilities of (which may include instruments issued by), a BRRD Entity; (c) reduce or write off the principal amount of, or outstanding amount due, in respect of certain liabilities of a BRRD Entity or to convert such liabilities into ordinary shares or other instruments of ownership of that entity; (d) cancel debt instruments issued by a BRRD Entity (other than certain secured liabilities); (e) reduce or write off the nominal amount of shares or other instruments of ownership of a BRRD Entity and to cancel such shares or other instruments of ownership; (f) require a BRRD Entity to issue new shares or other instruments of ownership or other capital instruments, including preference shares and contingent convertible instruments; (g) except for certain secured liabilities, amend or alter the maturity of debt instruments and certain other liabilities issued by an BRRD Entity or amend the amount of interest payable under such instruments and liabilities, or the date on which the interest becomes payable, including by suspending payment for a temporary period; (h) close out and terminate financial contracts or derivatives contracts; and (i) override certain default provisions, contracts, or other agreements, including provisions that would otherwise allow a party to terminate a contract or accelerate the payment of an obligation.

When exercising such powers, the BRRD mandates that the BRRD Resolution Authorities have powers to:

- (a) remove rights to acquire further shares or other instruments of ownership;
- (b) discontinue the listing and admission to trading of financial instruments;

(c) (cancel or modify the terms of a contract to which a BRRD Entity is a party or substitute a recipient as a party; and (d) provide for continuity arrangements necessary to ensure that resolution steps are effective and, where relevant, any business of the BRRD Entity transferred to a third party may be operated by such party.

The exercise of the resolution tools is subject to preconditions, namely: (a) the BRRD Entity must have been determined as failing or likely to fail (e.g., the institution is infringing or likely to infringe the requirements for continuing authorisation by the competent authority; the assets of the institution are, or it is considered will be in the near future, less than its liabilities; or the institution is, or is considered will be in the near future, unable to pay its debts or other liabilities as they fall due); (b) there must be no reasonable prospect that alternative measures will prevent failure within a reasonable timeframe; and (c) any resolution action must be necessary and in the public interest.

The BRRD also permits EU Member States to use financial stabilisation tools to provide public financial support in exceptional circumstances. These tools include the “public equity support” tool, whereby a EU Member State participates in the recapitalisation of a BRRD Entity, and the “temporary public ownership” tool, whereby a EU Member State may take the BRRD Entity into temporary public ownership. Under the BRRD, these tools are only permitted to be used as a matter of last resort and require a specified level of contribution to loss absorption and recapitalisation by existing shareholders and creditors before they may be used.

The resolution tools and powers described in this appendix are in addition to early intervention measures under the BRRD which include: (a) removing or replacing one or more members of the management body; (b) requiring changes to the BRRD Entity’s business strategy; (c) implementing one or more measures set out in the BRRD Entity’s recovery and resolution plan; and (d) requiring changes to its legal or operational structure.

There remains uncertainty regarding the specific factors which the BRRD Resolution Authority would consider in deciding whether to exercise its resolution tools and powers in relation to a BRRD Entity.

A BRRD Resolution Authority will have considerable discretion in relation to how and when it may exercise its powers and accordingly you may not be able to refer to publicly available criteria in order to anticipate a potential exercise of such power and its potential effect in respect of any BRRD Financial Instruments that you may hold or obligations or liabilities you are owed.

Bail-in

The bail-in tool involves (for the purpose of stabilisation and loss absorption) recapitalising a BRRD Entity by cancelling all, or a portion of, the principal amount of, or interest on, certain (typically unsecured) of its liabilities, and/or converting such liabilities into another security, including ordinary shares of the surviving entity, if any.

A BRRD Resolution Authority must apply the bail-in tool in accordance with a preference order specified by the BRRD for write-downs or debt conversions: (i) common equity tier 1 items, (ii) additional tier 1 instruments, (iii) tier 2 instruments, (iv) other subordinated debt and (v) other eligible liabilities.

“sale of business”, “bridge institution”, and “asset separation” resolution tools

The sale of business, bridge institution, and asset separation resolution tools include broad powers to transfer assets or liabilities of a BRRD Entity. The BRRD Resolution Authority has the power to:

- (i) sale of business tool - direct the sale of the entity or the whole or part of its business on commercial terms;
- (ii) bridge institution tool - transfer all or part of the business of the entity to a bridge institution (an entity created for such purpose that is wholly or partially in public control); and
- (iii) asset separation tool - separate assets, rights or liabilities of an entity by transferring assets to one or more publicly owned asset management vehicles to allow them to be managed with a view to maximising their value through eventual sale or orderly wind-down (this tool can only be used together with another resolution tool).

In all cases, the exercise of such powers will not require your consent to be effective and will not need to comply with procedural requirements under general company or securities law.

Impact of resolution tools and powers

The impact on BRRD Financial Instruments and liabilities or obligations of a BRRD Entity in resolution (particularly in respect of bail-in) depends on the rank of the instrument, liability or obligation, which may have changed due either to the specified order of preference for the bail-in tool or due to the introduction, required by the BRRD, of depositor preference (specification of the resolution creditor hierarchy of deposits from natural persons and micro, small and medium sized enterprises).

In the event of the use of the resolution tools, the value of BRRD Financial Instruments may be reduced to zero and or liabilities may be converted into ordinary shares or other instruments of ownership for the purposes of stabilisation and loss absorption and the exercise of the resolution tools and powers may limit a BRRD Entity's ability to satisfy liabilities or obligations (including repayment obligations). The terms of existing BRRD Financial Instruments (e.g., date of maturity or interest rates payable) could be altered and payments could be suspended.

The BRRD requires the resolution tools and powers to be exercised in accordance with the general principle that no creditor shall incur greater losses than would have been incurred if the BRRD Entity had been wound up under normal insolvency proceedings, (the "no creditor worse off" principle). This means that, in certain circumstances, you may have a right to compensation if the treatment that you receive as a result of a BRRD Resolution Authority exercising a BRRD resolution power or tool is less favourable than the treatment that you would have received under normal insolvency proceedings.

This assessment must be based on an independent valuation of the BRRD Entity. Compensation payments, if any, may be considerably later than contractual payment dates (in the same way that there may be a delay in recovering value in the event of insolvency).

Notwithstanding the foregoing, the exercise by a BRRD Resolution Authority of any of the above resolution powers or tools (including the bail-in tool) could cause you to lose some or all of any investment you make in BRRD Financial Instruments.

There can be no assurance that the use of any resolution tool or power by a BRRD Resolution Authority or the manner in which they may be exercised will not materially adversely affect your rights as a holder of BRRD Financial Instruments, the market value of any investment you may have in BRRD Financial Instruments and/or a BRRD Entity's ability to satisfy any liabilities or obligations it has to you.

Brexit impact

Whilst the UK was a member of the EU, the UK implemented the BRRD.

On 31 January 2020, the UK left the EU and entered a 'transition period' which ended on 31 December 2020 ("the Effective Date"). The UK has since transposed the BRRD into UK laws with some amendments, this amended version is referred to as the UK BRRD. The UK BRRD is largely the same as the EU BRRD in its effect for UK financial institutions in scope. The key change being that under a bail-in tool, Sova Capital Limited will, as of the Effective Date, be required to include a bail-in clause in relevant contracts which are not governed by English law (previously this was only relevant to contracts not governed by EEA law).