



HM Treasury

Bank Resolution (Recapitalisation) Bill - Code of Practice draft chapter

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(Recapitalisation) Bill - Code
of Practice draft chapter



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Notice: Bank Resolution (Recapitalisation) Bill - Code of Practice draft chapter

Sections five and six of the Banking Act 2009 set out that HM Treasury must issue a Code of Practice (the Code) alongside the special resolution regime. The Code supports the legal framework of the special resolution regime and provides guidance as to how and in what circumstances the authorities will use the powers they are granted under the Banking Act 2009. The Bank of England, Prudential Regulation Authority, Financial Conduct Authority and the Treasury have a statutory obligation to have regard to the Code.

Following the introduction of the Bank Resolution (Recapitalisation) Bill (the Bill) to Parliament, the Government has produced this draft chapter of the Code covering the use of the recapitalisation mechanism created by the Bill.

This draft chapter sets out how the recapitalisation mechanism will be used, including the firms it is intended for use on, how the Bank of England will determine the funds required from the Financial Services Compensation Scheme and assess the relative costs of using the mechanism compared to insolvency, and Bank of England accountability. It also clarifies certain aspects of the policy, following the Government's engagement with industry and Parliament.

This draft chapter may change, including as a result of any amendments made to the Bill during the parliamentary process and consultation with the Banking Liaison Panel. Further, consequential amendments will be made to the Code as a whole to reflect the changes made by the Bill. For the time being, any cross-references to the existing Code of Practice remain squared bracketed to reflect these may change in due course.¹

The Government intends to issue a finalised version of the Code in full when the Bill comes into force.

¹ [SRR_CoP_December_2020.pdf \(publishing.service.gov.uk\)](#)

The Bank Resolution (Recapitalisation) [Act 2025]

1. The Bank Resolution (Recapitalisation) [Act 2025] (BRRRA 25) introduced a mechanism to allow the Bank of England to use funds from the banking sector to cover certain costs associated with resolving a failing banking institution.
2. BRRRA 25 amends the Banking Act 2009 and the Financial Services and Markets Act 2000 to do the following:
 - allow the Bank of England to require the FSCS to provide funds to recapitalise a failing banking institution;
 - allow the FSCS to recover these funds by charging levies on all UK banks and building societies; and
 - allow the Bank of England to require the banking institution in resolution to issue new shares to facilitate the use of FSCS funds to meet the failing institution's recapitalisation costs.
3. The recapitalisation mechanism can only be deployed in connection with the exercise of a stabilisation power under Part 1 of the Banking Act 2009 to achieve a sale of all or part of the institution to a private sector purchaser or the transfer of the institution to a bridge bank.

Scope of application

4. The recapitalisation mechanism is available to allow the Bank of England to respond flexibly to circumstances at the time of failure. Before using the mechanism, the Bank of England would need to have determined that the conditions for use of stabilisation powers were met (see paragraph [4.2]).
5. The recapitalisation mechanism is primarily designed to support the resolution of small banks for whom the Bank of England has set a preferred resolution strategy of modified insolvency or transfer where the Bank of England is satisfied that all the conditions for the use of stabilisation powers are met. Where special resolution conditions three and four are

not met, the Bank of England will continue to place a failing banking institution into insolvency.

Box A.1 Glossary: loss-absorbing resources

MREL resources: Equity and debt liabilities that are maintained by an institution in order to meet a minimum requirement for own funds and eligible liabilities (MREL) as required by the Bank of England.

Non-MREL resources: Liabilities that are in scope of the bail-in tool but that are not MREL resources. These liabilities may not be readily available to be bailed in. Liabilities may be excluded from a specific bail-in in whole or in part at the discretion of the Bank in one or more exceptional circumstances set out in the Banking Act. Certain liabilities are statutorily excluded from being bailed-in.

6. The Bank of England would be able to use the recapitalisation mechanism where it has judged that it is necessary to recapitalise the failing institution, in order to achieve a sale of all or part of the institution to a private sector purchaser or the transfer of all or part of the institution to a bridge bank in pursuit of the special resolution objectives, and the failing firm holds insufficient resources. Firms with a preferred resolution strategy of modified insolvency or transfer are unlikely to have sufficient resources that can be readily written down, bailed-in or converted into equity to help restore the firm to viability. See Box A.1 for a glossary of resources that can be bailed in.
7. The Bank of England will not assume use of the new mechanism when setting a preferred resolution strategy of bail-in and the corresponding MREL requirements for a large bank.
8. For any firm, before any use of the mechanism in conjunction with a transfer, the Bank of England would be expected to write down or otherwise expose to loss any MREL resources maintained by the firm above minimum capital requirements that are readily available for bail-in.
9. The new mechanism would not be used to manage the failure of a third-country branch operating in the UK. This is because the responsibility for resolving such a firm ultimately lies with the relevant home resolution authority. In addition, the UK already has a number of separate powers that it can use with respect to branches, as set out in Chapter 6A of the Banking Act 2009.

Calculating the request for funds

10. The Bank of England is responsible for calculating the amount to require from the FSCS. The pre-resolution valuation set out in section 6E of the Banking Act 2009 will inform that calculation.² The valuation process is consistent with the approach followed for use of all stabilisation powers and informs the Bank of England's decision on what, if any, resolution action is appropriate.

Bridge bank

11. When exercising a stabilisation option to transfer a failing firm to a bridge bank, the Bank of England would have regard to a number of factors to determine the required recapitalisation payment. The Bank of England would consider the amount of capital that is required to restore the capital ratio of the firm in resolution to the extent necessary to sustain sufficient market confidence and enable it to continue to meet, for at least one year after the resolution action takes place, the conditions for authorisation and to continue to carry out the activities for which it is authorised. The decision on the extent of capital required to sustain market confidence over the period would be informed by the valuation, whether the capital position of the institution after the resolution would be appropriate in comparison with the current capital position of peer institutions, and the Bank's determination of the level required taking these factors in to account over the projected period.
12. Where the Bank of England exercises its mandatory reduction power under Section 6B of the Banking Act 2009, the recapitalisation payment would be set on the basis of the amount deemed necessary from the expected position of the firm after that mandatory reduction. The target capitalisation would be the same as provided for under the definition of the "shortfall amount" set out in section 12AA of the Banking Act 2009.
13. Where the Bank of England uses the bail-in tool in connection with effecting the transfer to a bridge bank, the Bank of England will exercise its discretion as to the extent to which that target capitalisation is met through bailing in non-MREL resources or a recapitalisation payment under section 214E of FSMA 2000, in such a way as is consistent with the special

² When resolution action is deemed sufficiently urgent, the Bank of England may perform a provisional valuation, which would then be replaced by an independent valuation, as set out in section 48X of the Banking Act 2009.

resolution objectives (see section 4 of the Banking Act 2009). In such instances, the Bank of England would first look to write down or otherwise expose to loss all readily available MREL resources before requiring a recapitalisation payment from the FSCS, if required. Further unsecured liabilities that are eligible for bail-in may also be bailed in, with consideration given to the impact on financial stability and market confidence, among other factors.

Private sector purchaser

14. When the Bank of England uses a stabilisation option to transfer a failing banking institution to a private sector purchaser, the Bank of England will follow the process outlined in [9.37-9.41] to pursue a sale. In determining if any recapitalisation payment is necessary, the Bank of England will consider many of the same factors in determining the level to which the failing firm must be recapitalised. However, when assessing whether funds are required from the FSCS, the Bank of England will also have regard to the desirability for the purchaser to make appropriate contributions to the recapitalisation.
15. In the case of a partial property transfer, the Bank of England will need to establish an appropriate transfer perimeter to achieve the special resolution objectives. It may be necessary to ensure resources are available to support a sale, or absorb any losses arising through disposal, of assets and liabilities, or costs expected to operate and, if necessary, to wind up parts of a failed institution that are not transferred. In taking forward a partial property transfer, the appropriate contribution from, and allocation of costs to, a purchaser would be established.
16. In any resolution, the Bank of England would take into account other potential costs that may arise when determining whether to require funds from the FSCS. This includes those associated with the operation of a bridge bank and costs to HM Treasury (see section on “Eligible costs and expenses” below).
17. The Bank of England is not limited in the number of times it can require a recapitalisation payment from the FSCS in respect of a single resolution. Subsequent recapitalisation payments may be required if, for example, unforeseen circumstances cause the sum already required to be insufficient, or where the Bank of England is operating a bridge bank and further funds are required. Throughout a resolution, authorities will continue to coordinate and have

regard to the special resolution objectives. Any decision to request further recapitalisation payments will involve consideration of the special resolution objectives and engage the governance outlined below in terms of assessing the affordability, and, if necessary, public funds implications. This will include consideration of whether it is more appropriate to pursue an insolvency.

Eligible costs and expenses

18. Where the Bank of England uses the recapitalisation mechanism, it would be able to use the funds provided through the mechanism to cover certain costs associated with a resolution as specified in BRRRA 25. This includes costs of recapitalising the firm in resolution. It also includes expenses incurred by the Bank of England, the Treasury or a Bank of England-owned company in connection with the recapitalisation of the institution or exercise of the stabilisation power. This may include ancillary expenses incurred by these persons, such as the costs of operating these entities, executing a sale, or receiving professional advisory, accountancy or legal advice. It may also include any compensation due to relevant parties under sections 49 to 62 of the Banking Act 2009.
19. In determining whether to include certain expenses when calculating the recapitalisation payment required from the FSCS, the Bank of England would carefully consider what is reasonable and prudent in a particular resolution scenario.

FSCS and PRA levies

20. The FSCS will recoup the funds provided to the Bank of England via levies under PRA rules section 213(3)(b) of FSMA 2000, in accordance with section 213(5) of FSMA 2000. The same class of firms will be subject to the levies as is the case for depositor payouts under insolvency, with the exception of credit unions, who are not subject to levies related to the recapitalisation mechanism under section 214E of FSMA 2000, as they are not covered by the special resolution regime.
21. There is a limit on the amount the FSCS can levy on each funding class within a given year. For the deposit-taking class, this is set by the PRA, who review the cap on an ongoing basis and set it in line with its safety and soundness objective. The PRA will consider affordability and determine (as required under the Deposit Guarantee Scheme Regulations 2015) whether the FSCS can levy.

22. In the event that the Bank of England requires a recapitalisation payment, the FSCS would look to meet the payment in the first instance either through cash at hand or commercial borrowing. Where the Bank of England calls for more funds than the FSCS can provide due to the levy limit or PRA determination that a levy is unaffordable to industry, or the FSCS's commercial borrowing limit, the FSCS will be able to request to borrow from the National Loans Fund (NLF). This loan (including interest) would be repaid via the FSCS levy. Levies to repay such loans would be expected to be spread over multiple years, in keeping with the limit set by the PRA on what the FSCS can levy within a given year.
23. As set out in [4.10], the Treasury has sole responsibility for decisions with implications for public funds. This includes the NLF, and so the Treasury may arrange for money to be paid out of the NLF in pursuance to a request from FSCS, if the Treasury deemed doing so to be necessary in the public interest.
24. In keeping with its approach to exercising its stabilisation powers, the Bank of England would make its decision as to whether to use the recapitalisation mechanism on an individual firm-by-firm basis. As a result, it is possible that the Bank of England could request funds from the FSCS to meet the costs of resolving multiple firms simultaneously. The limits on the amount the FSCS can levy in such a case would continue to apply. As set out above, where the FSCS requires additional funding to meet the Bank of England's request in this case, it would be able to request to borrow from the NLF, subject to approval from the Treasury.
25. Section 214F of FSMA 2000 sets out that Bank of England must reimburse the FSCS for any recapitalisation payment, or part of a recapitalisation payment, that is not needed to cover the eligible costs and expenses associated with the resolution. This could be because these costs and expenses were lower than the Bank of England had expected, or if there are any recoveries from the sale or winding up of part of the failed institution. The FSCS will seek to use any potential recoveries to offset the levy it uses to recoup the payment made to the Bank of England.

Taking account of relative costs to the FSCS

26. The decision to request a recapitalisation payment from the FSCS would be taken by the Bank of England, in consultation with the relevant authorities, as part of its assessment of the

resolution conditions. When assessing the third and fourth resolution conditions, the Bank of England must consider whether resolution is necessary in the public interest having regard to the Special Resolution Objectives, and whether one or more of the Special Resolution Objectives would be met to a lesser extent if the institution were put into insolvency. The Bank must therefore weigh the various potential outcomes against these objectives when considering different courses of action.

27. As part of the pre-resolution valuation, an estimate would be made of the likely outcomes in insolvency. This would inform a judgement on the estimated costs to the FSCS of making payouts to covered depositors and potential recoveries to the FSCS.
28. Such an estimate would be expected to consider, among other things:
- the covered depositor base of the institution;
 - potential recoveries from the failed institution's estate;
 - the position of eligible depositors in the creditor hierarchy;
 - interest payments on any borrowing; and
 - potential durations for the insolvency and associated costs.

Where appropriate, estimated ranges would be included.

29. The assessment of the cost to the FSCS under the recapitalisation mechanism is determined by the amount requested. There would also be interest payments in the event the FSCS is required to borrow. These would ultimately be borne by levy payers. The extent and value of interest payments would depend on the circumstances at the time, including whether the FSCS has borrowed commercially or from the NLF and the amount of time taken to repay any loans.
30. To aid in the assessment of the relative costs to the FSCS, the PRA would produce an estimate of the levy amount across the deposit-taking class for both insolvency and the recapitalisation mechanism.
31. When resolution action is considered sufficiently urgent, the Bank of England may perform a provisional valuation, which would consider the relative costs to the FSCS of different

options. This provisional valuation should, to the extent possible, follow the same methodology as an independent valuation, as set out in section 6E of the Banking Act 2009. This provisional would then be replaced by an independent valuation as detailed in section 48X of the Banking Act 2009.

32. The Bank of England would take into account the information contained in its assessments of the costs of both the recapitalisation mechanism and the estimated insolvency counterfactual, when making its assessment of whether the resolution conditions are met. As noted, the Bank of England is required to have regard to the special resolution objectives to ensure its decision is in pursuit of the public interest, and that the objectives would not be met to the same extent by winding up the firm. The Bank of England will therefore consider all appropriate options and impacts, as well as the assessments of the relative costs to the FSCS. This would include, among other things, the objective to protect public funds, and the potential wider impacts of an insolvency on financial stability through contagion to the rest of the financial system and on individual banking customers.

Reporting

33. The Banking Act 2009 sets out requirements for the Bank of England to report to the Chancellor of the Exchequer when it exercises certain powers under the SRR:

- Section 79A requires the Bank of England to report to the Chancellor about the exercise of the power to make share transfer instruments and property transfer instruments as soon as is reasonably practicable after the end of one year beginning with the date of the first transfer.
- Section 80 requires the Bank of England to report to the Chancellor on the activities of a bridge bank as soon as reasonably practicable after each year of its existence.
- Section 80A requires the Bank of England to report to the Chancellor about the exercise of a bail-in instrument and the activities of the failed bank.

34. Whilst the Treasury would have discretion to specify any contents of a report on a case-by-case basis, it is expected that when the recapitalisation mechanism is used, such reports to the Chancellor would include the following:

- an explanation of the choice to use the recapitalisation mechanism;
- how the resolution conditions and objectives were considered and had regard to;
- an assessment of the costs of using the recapitalisation mechanism compared to an estimated insolvency counterfactual (or, as appropriate, other resolution options), in line with the expectations set out in paragraphs [26-32]; and
- an explanation of why any ancillary costs were considered reasonable and necessary.

35. With the exception of reports made under section 79A, the Chancellor must lay reports in Parliament. However, in the event that the recapitalisation mechanism is used, it is expected that such reports would be laid in Parliament, however the Treasury may omit certain information from reports where they judge that doing so would be in the public interest.

5% and 8% thresholds

36. Section [11.5] sets out that shareholders and creditors of a failing banking institution must contribute an amount equal in value to at least 8% of the liabilities of the institution before resolution financing arrangements may be used. Further, the resolution financing arrangement may not exceed an amount equal to 5% of the liabilities of the institution. Henceforth, these are referred to as the 8% and 5% thresholds. Section [11.6] sets out these thresholds in relation to bank holding companies.

37. These thresholds will not be enforced when the recapitalisation mechanism under section 214E of FSMA 2000 is used on a banking institution with a preferred resolution strategy of modified insolvency or transfer. This is because the recapitalisation mechanism is primarily designed for use on small banks, which may have insufficient resources to write-down without creating other risks to the resolution objectives through writing down more senior creditors. If 8% of liabilities cannot be written down, it is unlikely that resolution finance equal to 5% of liabilities will be sufficient to recapitalise the firm and restore market confidence. The enforcement of the 5% and 8% thresholds could therefore impede the use of the recapitalisation mechanism in instances where it would be in the public interest to use it.

38.To reflect this, section 78A of the Banking Act specifies that the requirement for the Bank of England to inform the Treasury in writing whether or not a condition for financial assistance has been met in relation to a particular bank does not apply where the Bank of England has required a recapitalisation payment from the FSCS. This will facilitate the Bank of England's use of the recapitalisation mechanism for failing small banks where meeting the requirements may have undesirable adverse effects on the special resolution objectives.

39.Where larger banks maintain liabilities that can be bailed-in and are eligible for MREL, these liabilities (at a minimum) should generally be written down or otherwise exposed to loss before any use is made of the recapitalisation mechanism. It is therefore expected that, for banks with a bail-in resolution strategy that have met their MREL requirements, the 8% and 5% thresholds will be adhered to in resolution, to the extent that this is consistent with the special resolution objectives.

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