

NEW EURO AREA MODEL COLLECTIVE ACTION CLAUSE

The existing euro area model collective action clause ('CAC') became mandatory in all new euro area government securities with a maturity over one year issued on or after 1 January 2013 as a result of Article 12 of the Treaty Establishing the European Stability Mechanism (the 'ESM Treaty').

The most significant innovation made in the existing model CAC (the '2012 Euro Area CAC') was to introduce aggregated voting under which different series of bonds could be aggregated together for voting purposes (referred to in the CAC as a 'cross-series modification'). In broad terms, this form of aggregated voting is achieved through a 'double limb' voting arrangement which requires both a positive vote (above an individual series threshold) at the level of each affected individual bond issuance together with an overall aggregated positive vote (above an aggregate threshold) by reference to all affected series of bonds taken as a whole.

The 2012 Euro Area CAC has been in use in all euro area sovereign issuances since 1 January 2013, subject to certain exceptions (e.g. tapping of issuances originally made prior to 1 January 2013 and in respect of certain non-transferable retail savings instruments).

THE DECISION TO UPDATE

At the Euro Summit held on 14 December 2018, the Heads of State and Government of euro area member states confirmed the commitment to reform the 2012 Euro Area CAC, following an announcement by euro area finance ministers earlier that month. These announcements were made as part of policy measures intended to strengthen Economic and Monetary Union.

The EFC Sub-Committee on EU Sovereign Debt Markets (the 'EFC Committee') took on the role of producing the update to the 2012 Euro Area CAC which is again in the form of common terms of reference and is available [here](#).

An explanatory note and voluntary supplemental provisions, have been published alongside this updated CAC (the 'Single-limb CAC').

In an amendment to Article 12 of the ESM Treaty which states "Single-limb aggregated voting shall apply to all new euro area government securities, with maturity above one year, issued on or after 1 January 2022", the Single-limb CAC is effectively required to be included in all such new euro area government securities issued on or after that date (see Timing-Ratification Process below).

In a manner which is consistent with the implementation of the 2012 Euro Area CAC, the use of the Single-limb CAC is subject to certain exceptions, including in respect of certain non-transferable retail savings instruments and for tapping issuances originally made prior to the mandatory introduction of the Single-limb CAC.

This ability to tap pre-existing issuances is subject to annual limits which will restrict the volume of new tap issuances by reference to both pre 2012 and pre Single-limb CACs.

Main Purpose of the Single-limb CAC

The main stated purpose of the reform to the 2012 Euro Area CAC used for euro area government securities is to introduce a so called 'single-limb' aggregated voting mechanism. The explanatory note explains that this is 'to improve the process of orderly debt restructuring in the euro area, as well as to reduce the risk of holdout creditors'.

Where different series of bonds are being aggregated for voting purposes (again referred to as a 'cross-series modification'), the single-limb approach requires only that the specified aggregated voting threshold is met and so does not include any voting threshold at the individual bond series level (of the type which is required under the double-limb approach).

Single-Limb Voting and uniformly applicable safeguard

The explanatory note issued with the Single-limb CAC refers to the endorsement by the International Monetary Fund of the ICMA Enhanced Model CAC containing single-limb aggregated voting, which is now the market norm in sovereign bond issuances outside of the eurozone. One key feature of the ICMA Enhanced Model CAC is the 'uniformly applicable' investor safeguard which accompanies the use of aggregated single-limb voting. The Single-limb CAC also has a uniformly applicable investor safeguard where the issuer wishes to use single limb voting in respect of a reserved matter. Whilst the terminology used is the same, the scope of the uniformly applicable safeguard in the Single-limb CAC is different from that used in the ICMA Enhanced Model CAC.

The uniformly applicable safeguard used in the Single-limb CAC contains many more elements and the full definition (Section 1(k) of the Single-limb CAC) is set out in Annex 1. Please note also that through Section 2.3 of the Single-limb CAC additional provisions relating to the use of single-limb voting in respect of reserved matters are incorporated which serve to clarify various technical issues which could otherwise have been open to interpretation.

Voting Structures under the Single-limb CAC

Under the ICMA Enhanced Model CAC, both single-limb and double-limb aggregated voting is available in respect of reserved matter modifications. In addition, single series voting (i.e. not involving any aggregation of voting across different series of bonds) is available in respect of both reserved matter and non-reserved matter modifications.

A different approach to voting structures is taken in the Single-limb CAC, where the following are available:

- single-limb voting in respect of reserved matter and non-reserved matter modifications; and
- single series voting (i.e. not involving any aggregation of voting across different series of bonds).

However, the Single-limb CAC does not contain double-limb aggregated voting. One consequence is that, should a euro area member state need to revisit the payment terms of its bonds in the future, it would not be able to combine, in a single aggregated voting pool, bonds issued with the Single-limb CAC with any bonds issued with the 2012 Euro Area CAC (nor indeed with any bonds issued before the use of the 2012 Euro Area CAC became mandatory and any associated tap issuances).

Voting Thresholds

The voting thresholds under the Single-limb CAC as compared with the voting thresholds under the 2013 Euro Areas CAC are set out below:

MATRIX

	Single-limb CAC	2012 Euro Area CAC
Single series voting (no aggregation of different series of bonds)	<p><i>Reserved matter:</i> at least 75% at a meeting; or at least 66⅔% by written resolution.</p> <p><i>Non-reserved matter:</i> more than 50% whether at a meeting or by written resolution.</p>	<p><i>Reserved matter:</i> at least 75% at a meeting; or at least 66⅔% by written resolution.</p> <p><i>Non-reserved matter:</i> more than 50% whether at a meeting or by written resolution.</p>
Double-limb voting (aggregation of different series of bonds)	N/A	At least 75% taken in the aggregate at a meeting; or at least 66⅔% taken in the aggregate by written resolution AND more than 66⅔% of each series at a meeting; or more than 50% of each series by written resolution. NOTE: Reserved matters only.
Single-limb voting (aggregation of different series of bonds)	<p>Reserved matter: at least 66⅔% whether at a meeting or by written resolution. NOTE: Uniformly applicable requirement applies.</p> <p>Non-reserved matter: more than 50% whether at a meeting or by written resolution. NOTE: Uniformly applicable requirement does not apply.</p>	N/A

Other Points to Note:

Where a meeting is used, it must be duly called in accordance with the terms and condition of the bond or bonds in question.

There are no quorum requirements for meetings relating to single-limb aggregation. For all other meetings, the following quorum requirements apply:

- (a) Reserved matter: at least 66⅔% of the aggregate principal amount then outstanding;
- (b) Non-reserved matter: at least 50% of the aggregate principal amount then outstanding.

In the Single-limb CAC any meeting may be conducted by electronic or other then customary means without necessarily requiring two or more persons to be physically present in the same location contemporaneously.

Reserved Matters

The list of reserved matters in the Single-limb CAC differs slightly from that used in the 2012 Euro Area CAC. There are still 14 paragraphs ((i) to (xiv) inclusive) and some changes simply reflect the use of single-limb aggregation with the associated 'uniformly applicable' investor safeguard, any proposed change to which is now captured by paragraph (xiv). There has been some minor re-ordering in paragraphs (v) and (vi) without altering the scope.

There is one material change which is discernible only through the simple deletion of a footnote to paragraph (xi) (this paragraph makes a change of governing law of the bonds a reserved matter). In the 2012 Euro Area CAC, paragraph (xi) is footnoted for inclusion where the bonds are governed by foreign law. As is highlighted in the explanatory note accompanying the Single-limb CAC, the majority of the euro area sovereign issuances are governed by domestic law and the updated CAC 'treats a change of the law governing a bond as a reserved matter whether a bond is governed by domestic or foreign law'.

Other Points of Note

The disenfranchisement rules under which certain bonds held by or on behalf of the issuer are treated as not being outstanding for voting purposes remain unchanged. The key point remains that there is a broad range of institutions with autonomy of decision making within the eurozone and, broadly, any bonds held by any such institution, however connected with the issuer, are not disenfranchised.

The 2012 Euro Area CAC contained a provision (in Section 2.4) which permitted the issuer to alter the series of bonds being aggregated in a cross series modification after voting had occurred, subject to certain conditions. That flexibility has been removed in the Single-limb CAC.

The special rules relating to zero coupon and index linked bonds remain unchanged.

There are minor changes to the information required to be made available before a vote is taken to reflect the inclusion of single-limb aggregated voting.

Timing - Ratification Process

Implementation of the Single-limb CAC is to be made through an agreement amending the ESM Treaty, which has been published and is available [here](#).

This Agreement amending the ESM Treaty contains provisions dealing with the conditions which need to be satisfied in order for it to enter into force. These are on page 40 and provide:

"ARTICLE 4

Ratification, approval or acceptance

1. This Amending Agreement shall be subject to ratification, approval or acceptance by the signatories. Instruments of ratification, approval, or acceptance shall be deposited with the Depositary.

2. The Depositary shall notify the other signatories of each deposit and the date thereof.

ARTICLE 5

Entry into force and accession

1. This Amending Agreement shall enter into force on the date when instruments of ratification, approval or acceptance have been deposited by all the Signatories."

On 7 December 2021 the Economic and Financial Sub-Committee on EU Sovereign Debt Markets issued a press release dealing with the timing of the introduction of the updated CAC to reflect that fact that, in some euro area member states, the applicable legal process set out in Article 4 and 5 above is insufficiently advanced. As a result the updated CAC will be introduced in all euro area member states on the first day of the second month following the entry into force of the Amending Agreement to the ESM Treaty. One consequence is that the schedule of annual limits arising through new tap issuances which restricts the volume of both pre 2013 and pre Single-limb CACs (as referred to on page 2 earlier) needs to be revised. The new schedule is set out in the 7 December 2021 press release which is available [here](#).

Conclusion

The Single-limb CAC will incorporate single-limb aggregated voting into euro area government securities. This updated CAC was originally intended to be in use as from 1 January 2022 but will now be implemented shortly after the conditions required for the Amending Agreement to the ESM Treaty to enter into force are met. The enhanced voting power for issuers under this updated CAC is subject to more stringent investor safeguards than those used in other single-limb aggregation CACs seen in the marketplace. The issuer does not have the ability to use double-limb aggregated voting under the Single-limb CAC and so voting bonds containing the updated CAC together in a single voting pool with bonds with earlier formulations of CACs will not be feasible.

This migration to single-limb aggregated voting will add the most powerful issuer voting mechanism currently available into euro area government securities and should assist in achieving more orderly outcomes where an issuer's circumstances require it to revisit payments terms on its bond issuances.

ANNEX 1

UNIFORMLY APPLICABLE INVESTOR SAFEGUARD

- (k) 'uniformly applicable' means a modification by which holders of debt securities of all Relevant Series are invited to:
- (i) exchange, convert or substitute their debt securities or amend the terms and conditions of their debt securities on a basis which would have the effect of reducing the principal amount outstanding by the same proportion under all Relevant Series;
 - (ii) exchange, convert or substitute their debt securities or amend the terms and conditions of their debt securities on a basis which would have the effect of extending the respective date on which principal amounts are payable under all Relevant Series by either the same period or by the same proportion;
 - (iii) exchange, convert or substitute their debt securities on the same terms for (x) the same new instrument or other consideration or (y) a new instrument, new instruments or other consideration from an identical menu of instruments or other consideration;
 - (iv) amend the terms and conditions of the debt securities such that each Relevant Series is amended on a basis which would, following implementation of such amendments, result in the amended debt securities having identical provisions (other than provisions which are necessarily different having regard to different currency of issuance);
 - (v) in relation to the following reserved matters only, namely the reserved matters set out in any of the sub-paragraphs (h)(v), (h)(vii), (h)(viii), (h)(ix), (h)(x), (h)(xi), (h)(xii), (h)(xiii) and (h)(xiv), amend the same term or terms in the terms and conditions of the debt securities such that each Relevant Series is amended on a basis which would, following implementation of such amendments, result in the amended debt securities being the subject of an identical amendment; or
 - (vi) amend the terms and conditions of the debt securities such that each Relevant Series is amended on a basis which would, following implementation of such amendments, result in one or more interest payment dates being extended by the same period other than where such an extension results from any extension of maturity in which case sub-paragraph (k)(ii) shall apply.

As the uniformly applicable definition cross refers to some elements of the reserved matter definition, that second definition is also set out in full below:

- (h) 'reserved matter' in relation to the Bonds means any modification of the terms and conditions of the Bonds or of any agreement governing the issuance or administration of the Bonds that would:
- (i) change the date on which any amount is payable on the Bonds;
 - (ii) reduce any amount, including any overdue amount, payable on the Bonds;
 - (iii) change the method used to calculate any amount payable on the Bonds;

- (iv) reduce the redemption price for the Bonds or change any date on which the Bonds may be redeemed;¹
- (v) change the place of payment of any amount payable on the Bonds;
- (vi) change the currency of any amount payable on the Bonds or impose any condition on or otherwise modify the Issuer's obligation to make payments on the Bonds;
- (vii) except as permitted by any related guarantee, release any guarantee issued in relation to the Bonds or change the terms of that guarantee;²
- (viii) except as permitted by any related security agreement, release any collateral that is pledged or charged as security for the payment of the Bonds or change the terms on which that collateral is pledged or charged;³
- (ix) change any payment-related circumstance under which the Bonds may be declared due and payable prior to their stated maturity;⁴
- (x) change the seniority or ranking of the Bonds;
- (xi) change the law governing the Bonds;
- (xii) change any court to whose jurisdiction the Issuer has submitted or any immunity waived by the Issuer in relation to legal proceedings arising out of or in connection with the Bonds;⁵
- (xiii) change the principal amount of outstanding Bonds or, in the case of a cross-series modification, the principal amount of debt securities of any other series required to approve a proposed modification in relation to the Bonds, the principal amount of outstanding Bonds required for a quorum to be present, or the rules for determining whether a Bond is outstanding for these purposes; or
- (xiv) change the definition of a reserved matter, cross-series modification or uniformly applicable or Relevant Series.

and has the same meaning in relation to the debt securities of any other series save that any of the foregoing references to the Bonds or any agreement governing the issuance or administration of the Bonds shall be read as references to such other debt securities or any agreement governing the issuance or administration of such other debt securities.

¹ To be included if the Bonds are redeemable.

² To be included if the Bonds are guaranteed.

³ To be included if the Bonds are collateralised.

⁴ To be included if the Bonds are subject to acceleration.

⁵ To be included, as appropriate, if the Issuer has submitted to the jurisdiction of a foreign court or expressly waived its immunity.

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