PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Tenth Delegated Legislation Committee

DRAFT OFFICIAL LISTING OF SECURITIES, PROSPECTUS AND TRANSPARENCY (AMENDMENT ETC.) (EU EXIT) REGULATIONS 2019

Tuesday 19 February 2019

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Saturday 23 February 2019

The Committee consisted of the following Members:

Chair: Sir David Amess

† Black, Mhairi *(Paisley and Renfrewshire South)* (SNP)
† Burden, Richard *(Birmingham, Northfield)* (Lab)
† Campbell, Sir Alan *(Tynemouth)* (Lab)
† Caulfield, Maria *(Lewes)* (Con)
† Clarke, Mr Simon *(Middlesbrough South and East Cleveland)* (Con)
† Cleverly, James *(Braintree)* (Con)
† Dodds, Anneliese *(Oxford East)* (Lab/Co-op)
† Foster, Kevin *(Torbay)* (Con)
† Glen, John *(Economic Secretary to the Treasury)*
† Glindon, Mary *(North Tyneside)* (Lab)
† Harrison, Trudy *(Copeland)* (Con)
† Kyle, Peter *(Hove)* (Lab)
† Merriman, Huw *(Bexhill and Battle)* (Con)
† Paterson, Mr Owen *(North Shropshire)* (Con)
† Rimmer, Ms Marie *(St Helens South and Whiston)* (Lab)
† Walker, Thelma *(Colne Valley)* (Lab)
† Whittaker, Craig *(Lord Commissioner of Her Majesty's Treasury)*

Peter Stam, *Committee Clerk*

† **attended the Committee**

Tenth Delegated Legislation Committee

Tuesday 19 February 2019

[Sir David Amess *in the Chair*]

Draft Official Listing of Securities, Prospectus and Transparency (Amendment etc.) (EU Exit) Regulations 2019

2.30 pm

The Economic Secretary to the Treasury (John Glen): I beg to move,

That the Committee has considered the draft Official Listing of Securities, Prospectus and Transparency (Amendment etc.) (EU Exit) Regulations 2019.

It is a great pleasure to serve under your chairmanship, Sir David. The Treasury has been laying statutory instruments under the European Union (Withdrawal) Act 2018 to ensure that the UK continues to have a functioning regulatory and legislative regime for financial services should it leave the EU with no deal or implementation period. The regulations are part of that work and fix deficiencies in UK legislation that relate to the UK's prospectus and listing regimes, as well as its transparency framework, to ensure that they function appropriately after exit.

The approach taken in the statutory instrument is consistent with that of other statutory instruments being laid under the 2018 Act in maintaining existing legislation at the point of exit where possible to provide continuity, but amending relevant legislation where necessary to ensure that it works effectively in a no-deal context. It amends the legislation that implements the prospectus directive, the transparency directive, the consolidated admissions and reporting directive—CARD—and related legislation to ensure that the UK continues to have an effective prospectus and listing regime and an effective transparency framework to regulate activity in the UK's capital markets.

The prospectus directive harmonises rules across the European economic area to govern the format, content, approval and distribution of prospectuses. Prospectuses contain information on issuers seeking admission to trade on a regulated market or issuers seeking to offer securities to the public. The transparency directive provides for EU-wide transparency requirements that ensure that issuers with securities, such as bonds or shares, who are admitted to trading on an EU-regulated market publicly disclose certain information. CARD sets out the rules governing the admission of securities to official stock exchange listing and the information to be published on those securities.

The UK legislation implementing the prospectus directive, the transparency directive and CARD needs to be amended, given that the UK will be outside the EU's legal, financial regulatory and supervisory framework in a no-deal scenario. The amendments will ensure that the UK continues to have a functioning prospectus regime, listing regime and transparency framework in that scenario.

First, under the prospectus directive, certain public bodies are exempt from the requirement to produce a prospectus. The statutory instrument extends the exemption to the same set of public bodies in all third countries post exit. If a UK-only approach were taken, EEA public bodies that currently access the UK market would be obliged to produce a prospectus to issue securities in the UK, which they would not be required to do when issuing in the EEA. Additionally, extending the exemption to public sector bodies of third countries is consistent with the UK treating EEA member states and third countries equally.

Secondly, under the current arrangements, EEA issuers can passport prospectuses approved by another EEA regulator for use in the UK. Post exit, the statutory instrument will require EEA issuers to obtain the Financial Conduct Authority's approval of their prospectuses when seeking access to the UK's capital markets. That is in line with our current treatment of third countries and with the approach taken across other financial services statutory instruments laid under the 2018 Act.

The statutory instrument also introduces grandfathering arrangements that enable any prospectus approved by an EEA regulator and passported into the UK before exit to continue to be eligible in the UK up to the end of its validity, which is usually 12 months after initial approval. That includes prospectuses that are supplemented with further information as necessary.

Furthermore, the explanatory memorandum for the statutory instrument states:

"in a no deal scenario, HM Treasury intends to issue an equivalence decision, in time for exit day, determining that EU-adopted IFRS"—

international financial reporting standards—

"can continue to be used…to prepare financial statements"

for UK transparency and prospectus requirements. That decision will enable EEA state-registered issuers in the UK that are making an offer of securities, or that have securities admitted to trading on a UK-regulated market, to continue to use EU-adopted IFRS when producing their consolidated accounts. The decision aligns with the Government's approach to provide post-exit regulatory continuity. It is supported by the FCA and has been welcomed by industry.

Additionally, the SI will transfer responsibility for powers and functions currently held and carried out by EU authorities to the appropriate UK institutions. Specifically, it transfers powers to the Financial Conduct Authority from the European Securities and Markets Authority—ESMA—to create and amend certain binding technical standards. It also transfers powers to the Treasury from the European Commission, including the ability to make delegated Acts pursuant to the relevant legislation. The transfer of functions is consistent with the current split between the regulatory role of ESMA and the legislative power of the Commission. The SI also makes further amendments to other retained UK and EU legislation to ensure that the prospectus regime, listing regime and transparency framework function correctly in the UK once it leaves the EU.

Finally, the SI removes the requirements for the FCA to share information and co-operate with EU regulators, as such an obligation would not be appropriate as of exit day, given that there will be no guarantee of reciprocity. The FCA, however, will continue to have the ability to

co-operate with EU counterparts through the existing framework in the Financial Services and Markets Act 2000, consistent with the current arrangements with all other third countries.

Certain provisions of the prospectus regulation have applied since July 2017 and July 2018, and the remainder of the legislation is due to apply from July 2019 after the UK leaves the EU. It is the Government's intention to domesticate the remaining provisions as they will constitute the prospectus regulatory regime from July 2019. However, the European Union (Withdrawal) Act will convert into UK law only EU legislation that is already in force and applies immediately before exit day. Therefore, remaining provisions of the prospectus regulation will be domesticated via a statutory instrument laid under the Financial Services (Implementation of Legislation) Bill and in-flight files legislation. The Bill as currently drafted requires the affirmative resolution procedure for every statutory instrument made under it, provided that Parliament has an opportunity to debate and discuss each file that the Government are implementing.

The UK has played a leading role in shaping the prospectus regulation for the benefit of consumers and industry. It is welcomed by industry and acts to cut the costs to business of producing a prospectus in the UK. In terms of industry engagement and transparency, on 12 December 2018 the Treasury published the instrument in draft with an explanatory policy note published on 21 November 2018 to maximise transparency for Parliament and industry. Throughout the drafting process, the Treasury has been working closely with the FCA and has also engaged the financial services industry using the assistance of TheCityUK as a convening body for the appropriate representative firms and trade bodies on the SI, and it will continue to do so in future.

To conclude, the Government believe that the proposed legislation is necessary to ensure that if the UK leaves the EU without a deal or an implementation period, the UK's prospectus regime, listing regime and transparency framework can continue to function appropriately post exit. I hope colleagues will join me in supporting the regulations. I commend them to the Committee.

2.38 pm

Anneliese Dodds (Oxford East) (Lab/Co-op): It is a pleasure to serve on this Committee with you in the Chair, Sir David. As always, I am grateful to the Minister for his explanation of the statutory instrument. Once again, the Minister and I are here to discuss a statutory instrument that would make provision for a regulatory framework after Brexit in the event that we crash out without a deal. On each occasion, I and my Labour Front-Bench colleagues have spelt out our objections to the Government's approach to secondary legislation. The volume of EU exit secondary legislation is concerning for accountability and proper scrutiny. The Government have assured the Opposition that no policy decisions are being taken. However, establishing a regulatory framework inevitably involves matters of judgment and raises questions about resourcing and capacity.

Secondary legislation ought to be used only for technical, non-partisan, non-controversial changes because it allows limited accountability. Instead the Government continue to push through far-reaching financial legislation via this vehicle. As legislators, we have to get it right. The regulations could represent real and substantive changes to the statute book and they need proper in-depth scrutiny. In this light, the Opposition would like to put on record our deepest concerns that the process is not as accessible and transparent as it should be.

Yet again, we have an SI that changes primary legislation—in this case, FSMA. At the latest count, 288 changes had been made to that Act through Henry VIII powers, as part of the no-deal preparation process. In that connection, I am increasingly concerned about the mission creep that has been evidenced via the progression of SIs that have been laid before Delegated Legislation Committees.

After a discussion in one such Committee this morning about what was and was not facilitated by the EU (Withdrawal) Act 2018, I went back to that legislation to examine exactly what it describes as deficiencies, which are the purported basis for the SI. There is no reference to Ministers being able to determine what may be in the national interest, and to use secondary legislation to enact that. I have no doubt that there would be considerable financial turbulence in the event of no deal—the Minister was absolutely right to emphasise that this morning—but the no-deal SIs, coupled with the 2018 Act, do not provide carte blanche to deal with market turbulence.

The deficiencies mentioned in the 2018 Act do not encompass general problems that might arise and require a public policy response. Instead, they cover specific areas, such as where retained EU law would be redundant because it would have no practical application, or where reference is made to reciprocal obligations that would no longer exist. However, the Minister intimated this morning that it was acceptable for the FCA effectively to adopt a completely different approach to approving benchmarks from that of the European Securities and Markets Authority, if it felt that that was justified by its own objectives and not, I underline, those of the retained EU legislation. We have a similar issue with this SI, to which I will return later.

As with many of the instruments that we have been considering recently, the SI seeks to transfer significant powers to the FCA. First, regulation 19 allows the FCA to make rules requiring disclosure by issuers, but there is little guidance about how it should do that or about the limits of the rules. Will the Minister please provide us with further information in that regard?

Secondly, regulation 27 gives the FCA regulating power to make corporate governance rules relating to the corporate governance of issuers who want to trade securities. I hope that the Minister can explain the rationale for providing that wide-ranging power to the FCA, rather than allowing the Treasury to set those rules, at least in part. I appreciate that it would be done under the purview of the Treasury, but surely in many circumstances there would be more of a direct political impact in that area.

Thirdly, as with the SI we discussed only this morning, we find a new definition, this time that of "debt securities". As before, it would be helpful to understand why the definition is present here.

Fourthly, I want to ask about the process for determining equivalence between UK and non-UK accounting standards in relation to the issuing of securities. The explanatory memorandum appears to suggest that the

[Anneliese Dodds]

creation of an equivalence regime is an aspiration rather than a mechanism provided within the SI. I appreciate that it was probably written quite some time before the latest draft of the SI was, but the power to assess equivalence does appear to be provided, in regulations 67 and 68.

The process of assessing whether other countries' accounting standards are equivalent to the UK's or to the EU's IFRS, which the regulations seem to deem equivalent to the UK's approach, could be very onerous. It would be helpful to understand, first, whether the resource implication has been taken on board, and secondly, and above all, to know the anticipated timing of the process of assuring equivalence. If securities cannot be traded by issuers based in non-EEA countries until their accounting conventions have been deemed equivalent by the FCA, that could surely pose significant problems for the financial markets, even accounting for the fact that existing prospectuses will continue to be able to be passported into the UK under the SI. That would be an issue for new securities but also for those whose prospectuses had expired.

I would have thought that the cost of a potential gap would be rather more than the £700 one-off familiarisation cost per firm that is intimated in the impact assessment. There is an acknowledgement in that assessment that a change to business processes would be needed as a result of the SI, but the costs of that change are not quantified. From what I can see, there is just the one-off familiarisation cost, and we had a discussion about the basis for that this morning.

In the circumstances, it is unclear why the Government seem to have chosen not to assume equivalence for accounting procedures with non-EEA countries where the EU might have already deemed them equivalent for an initial period, with the FCA being able to review that later. In fact, there seems to be an inconsistency here, because a very different approach has been taken when it comes to allowing public bodies to issue securities without having to comply with prospectus requirements. There is a completely open door for those public bodies, even if they are from outwith the EEA.

As the Minister said, the impact assessment states that it is appropriate to enable public bodies to issue securities without their having to comply with prospectus requirements, even if they are from outwith the EEA, because that

> "offers the most appropriate balance between investor protection and maintaining the attractiveness of the UK market, and is therefore the most appropriate option to preserve the continuity of the UK's financial services market—in line with HM Treasury's overall approach to financial services legislation, and the framework set out in the EUWA."

Given what I said previously, I suggest that that exemption is in line with the former but not the latter. It may well be in line with the approach that the Government decide to take to financial services legislation, but it is not clear that it is justified by the 2018 Act.

Fifthly, the explanatory memorandum refers to an SI that was to be laid before the House by the Department for Business, Energy and Industrial Strategy this January—last month—about the future adoption and use of UK-adopted international accounting standards. The Minister seemed to suggest that that would happen only at some unspecified point before exit, so it would help if he could give us more clarity about the timing. BEIS is not the Minister's Department, and I do not know whether the SI has been delayed because of issues with setting up the new UK IFRS endorsement board within the Financial Reporting Council, but given that the explanatory memorandum refers to the SI being laid before the House last month, it would be helpful to know when it will be in place. In the SI that we are debating, reference is made to UK-adopted international accounting standards, so presumably amendments will need to be made to change the language once the BEIS SI has been laid before the House.

Finally, I am pleased that the Minister made it clear that the future elements of the prospectus regulation that have not yet been enacted will be covered by the in-flight files Bill; that was not stated in the explanatory memorandum. I wonder about the extent to which that coheres with the approach taken to benchmarks. This morning it was stated that although all the provisions for benchmarks had not yet commenced, the SI assumed that they would be complied with, whereas with the SI that we are debating it is suggested that additional legislation will be necessary. That is presumably because more substantive changes will come in under these regulations, but clarification would be helpful.

2.48 pm

John Glen: I thank the hon. Member for Oxford East for her examination of the points that have arisen. I will initially address her concerns about the appropriateness of the judgments that the Treasury and I, as a Minister, are making.

I do not think the hon. Lady and I agree on our interpretation of the powers under the 2018 Act. I feel as though we are having quite a lot of scrutiny as we go through the process. Each SI, as I explained, goes through a thorough process of engagement with industry and the regulators, and I do not recognise the notion of mission creep. I acknowledge the concerns that the hon. Lady raised this morning, and I have started to respond to them by letter, which she will receive imminently. I will take account of what she said and look very carefully into the matter, but let me now address some of her specific points.

On the processes that the Government went through to make the equivalence decision, the decision will be made in time for exit day. The position that we have considered is to have the same rules as the EU, and the FCA has provided a technical assessment of the suitability of using the EU-adopted IFRS in the UK. We consider EU-adopted international financial reporting standards to be suitable for the specific purposes of preparing financial instruments for transparency directive requirements, and preparing a prospectus. That is because they enable investors to make a similar assessment of the assets and liabilities, financial position, profits and losses, and prospects of an issuer as financial statements drawn up in accordance with the UK-adopted IFRS, with the result that investors are likely to make the same decision about the acquisition, retention or disposal of its securities.

The intended decision recognises the interconnected nature of the UK and EU regimes, and it has been strongly welcomed by industry. In fact, if we did not

adopt it, we would essentially oblige issuers to adopt a different way of presenting accounts. Arbitrarily asserting a differentiated regime would create burdens for those in the EU and other third parties.

When it comes to consultation engagement, I recognise that we have not undertaken a formal consultation on this statutory instrument, but it was published in draft on 12 December and we worked with the FCA throughout the drafting process to ensure that it was effective and fair. During that process, we engaged with industry, which expressed the view that the SI is not contentious, and that it largely reflects the minor changes to the legislation that will be necessary as a result of our withdrawal from the EU. Minor drafting changes suggested by industry as part of our engagement on the statutory instrument have been incorporated into the final version to improve the clarity of the text.

I will now clarify our approach to the prospectus directive and public bodies exemption. To address a deficiency arising from our withdrawal from the EU, we are extending such exemptions to bodies of that type in all third countries. In the absence of prudential justification, we cannot keep the scope of the existing exemption, which is for EEA bodies only, because we cannot offer preferential treatment to the EEA. We are obliged to treat public bodies in the EEA in the same way as we do other third-country public bodies. Restricting the exemption to UK bodies would exclude EEA public bodies that currently use the exemption, and they would have to start producing prospectuses in order to access the UK's markets. That would negatively impact the attractiveness of the UK's markets.

Our approach offers the most appropriate balance between investor protection and maintaining the effective functioning of the UK's primary markets for capital. The hon. Lady's substantive point was that we have made an arbitrary assessment, which constitutes policy origination. I assert that it is an intelligent interpretation of the most market-appropriate fix in the undesirable and urgent situation of no deal, against the Government's intentions. I have now put that on record as our motivation.

The hon. Lady also raised issues about cost. As the SI largely replicates the current regulatory regime—except for the changes that are necessary to reflect the UK's position outside the EU—it should have no significant impact on UK issuers accessing the UK's capital markets. Such issuers will continue to operate as they did prior to the UK's withdrawal from the EU. For example, they will secure approval for their prospectus directly from the FCA, as they do now. That is intended to minimise, as far as possible, the impact on issuers.

The issuers who are impacted will need to understand the changes, and the hon. Lady raised—as the hon. Member for Wallasey (Ms Eagle) did this morning—the question of how the relevant costs are computed. They are set out in an annexe to the explanatory memorandum, I believe, but I will draw attention to them in the letter that I am drafting to the hon. Member for Oxford East. We expect there to be a one-off cost of approximately £700 per firm, as she acknowledged. Given that the SI is designed to replicate the existing regime, we do not expect there to be any business change that will result in further transitional costs. Our engagement with industry during the drafting of the SI did not highlight such concerns about costs.

Anneliese Dodds: I am grateful to the Minister for those clarifications. To be absolutely clear, the equivalence gap that I was concerned about was not about EU IFRS and whether they are equivalent to UK rules. It was about non-EEA countries' accounting rules and the process by which the FCA deems them to be equivalent. That process does not seem to be set out clearly in the SI. I am concerned that it could take the FCA some time to assess that equivalence, and that within that time costs could be imposed on business. Sorry; I obviously did not express that point sufficiently clearly.

John Glen: I think the hon. Lady probably did express the point clearly, and I did not absorb it properly. The challenge is to make the distinction between third countries and public bodies.

Anneliese Dodds: That is another one.

John Glen: To be honest, I think the best thing is to write to the hon. Lady and set out my response clearly for the record, and also to make it available to the Committee.

The hon. Lady asked what we are doing in the SIs within the remit of section 8 powers on deficiency fixing, and I can say a little more about that. The 2018 Act, which gives Ministers the power to lay the SIs before the House, was debated thoroughly, and it represents the considered view of Parliament as we prepare to leave the EU. The section 8 powers were the subject of particular scrutiny and debate, and we spent approximately 12 hours in Committee debating the clause that grants them. What constitutes a deficiency in retained EU law is clearly defined in section 8 of the Act, and the Treasury is clear that the relevant SIs fall within the scope of that power. I do not think that the scrutiny that has taken place so far would have allowed us to reach this point, if that had not been the case.

On the question of whether the FCA has the resources to carry out the extra functions, we are absolutely clear that it does. It has had the additional resource of 130 full-time equivalents over the past year. Its business plan for 2019-20 will give more detail on that, but it has the discretion to raise more from a levy should that be needed. I accept that £16 million has been diverted to Brexit-related SIs, but I contend that that work is wholly necessary to prepare for the unwelcome outcome of a no-deal scenario without an implementation period.

The hon. Lady asked for an explanation regarding the FCA's sub-delegation powers to legislate. Regulation 72 provides the FCA with the powers to make technical standards for the purposes specified in part 3 of schedule 2 to the SI. Currently, the European Securities and Markets Authority exercises those powers. As the powers relate to technical standards currently made by ESMA, it was considered appropriate to delegate them to the FCA rather than to the Treasury. Again, that is consistent with the financial services legislation domesticated under the 2018 Act.

The hon. Lady also drew attention to the in-flight files Bill. The challenge is that in a no-deal situation without an implementation period, a whole body of work is ongoing, some of which we have been very involved in, as a country within the EU, and some of which we absolutely desire to happen but will not land fully until after exit day. It would be possible to adopt

[John Glen]

the four files at the start of the in-flight files Bill, as per the terms that we discussed on Second Reading, only if we fixed the deficiencies in the language. They would essentially mark the next iteration of an evolution in the regulations on prospectus. In the same way, the general review that would cover the benchmarks we discussed this morning would have to be in the schedule of files. Those would not be the four that are nearly done, so we would have to make a judgment subsequently.

If I may, I will conclude the discussion. I will examine the record, and if there are any outstanding points, I will write to the hon. Lady and make my response available to the Committee. The Government contend that the SI is needed to ensure that the UK has an effective prospectus regime, listing regime and transparency framework. We seek to do that within the letter of the law. If the UK leaves the EU without a deal or an implementation period, we must ensure that we have made the appropriate provisions for the legislation to function. I hope that the Committee has found the sitting informative and will join me in supporting the regulations.

Question put.

The Committee divided: Ayes 9, Noes 8.

Division No. 1]

AYES

Caulfield, Maria	Harrison, Trudy
Clarke, Mr Simon	Merriman, Huw
Cleverly, James	Paterson, rh Mr Owen
Foster, Kevin	Whittaker, Craig
Glen, John	

NOES

Black, Mhairi	Glindon, Mary
Burden, Richard	Kyle, Peter
Campbell, rh Sir Alan	Rimmer, Ms Marie
Dodds, Anneliese	Walker, Thelma

Question accordingly agreed to.

Resolved,

That the Committee has considered the draft Official Listing of Securities, Prospectus and Transparency (Amendment etc.) (EU Exit) Regulations 2019.

3.2 pm

Committee rose.