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OFFICIAL REPORT

Eleventh Delegated Legislation Committee

DRAFT FINANCIAL REGULATORS' POWERS (TECHNICAL STANDARDS ETC.) AND MARKETS IN FINANCIAL INSTRUMENTS (AMENDMENT) (EU EXIT) REGULATIONS 2019

Wednesday 20 February 2019

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The Committee consisted of the following Members:

Chair: Sir Gary Streeter

Bradshaw, Mr Ben *(Exeter)* (Lab)
† Clark, Colin *(Gordon)* (Con)
† Clifton-Brown, Sir Geoffrey *(The Cotswolds)* (Con)
† Doughty, Stephen *(Cardiff South and Penarth)* (Lab/Co-op)
† Glen, John *(Economic Secretary to the Treasury)*
† Grant, Peter *(Glenrothes)* (SNP)
† Huddleston, Nigel *(Mid Worcestershire)* (Con)
† Kerr, Stephen *(Stirling)* (Con)
Malhotra, Seema *(Feltham and Heston)* (Lab/Co-op)
† Mann, Scott *(North Cornwall)* (Con)
† Merriman, Huw *(Bexhill and Battle)* (Con)
† Quince, Will *(Colchester)* (Con)
† Reynolds, Jonathan *(Stalybridge and Hyde)* (Lab/Co-op)
† Smith, Jeff *(Manchester, Withington)* (Lab)
Walker, Thelma *(Colne Valley)* (Lab)
† Whittaker, Craig *(Lord Commissioner of Her Majesty's Treasury)*
† Zeichner, Daniel *(Cambridge)* (Lab)

Yohanna Sallberg, Elektra Garvie-Adams, *Committee Clerks*

† attended the Committee

Eleventh Delegated Legislation Committee

Wednesday 20 February 2019

[Sir Gary Streeter *in the Chair*]

Draft Financial Regulators' Powers (Technical Standards etc.) and Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2019

8.55 am

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

That the Committee has considered the draft Financial Regulators' Powers (Technical Standards etc.) and Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2019.

May I first say what an enormous pleasure it is to serve under your chairmanship, Sir Gary? It certainly feels like a long time since I was your researcher 22 years ago.

As the Committee will be aware, particularly Front Benchers, the Treasury has been undertaking a programme of legislation to ensure that, if the UK leaves the European Union without a deal or an implementation period, there continues to be a functioning legislative and regulatory regime for financial services in the United Kingdom. This instrument forms part of that work.

There are two components to the instrument. The main component follows on from the Financial Regulators' Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018, debated and made in October 2018, which transferred responsibility for fixing deficiencies in level 2 binding technical standards—BTS—to the UK financial services regulators. Consistent with the approach taken in that SI, this transfers responsibility for any new BTS adopted by the EU Commission since the previous SI was laid to ensure that those can also be fixed ahead of exit day. The second, smaller component of this morning's SI makes minor correcting amendments to the Market in Financial Instruments (Amendment) (EU Exit) Regulations 2018 that was debated and made in December 2018 to ensure that it operates as intended if the UK were to leave the EU without a deal. The approach taken in the legislation aligns with that of other SIs being laid under the European Union (Withdrawal) Act 2018, providing continuity by maintaining existing legislation at the point of exit, but amending it where necessary to ensure that it works effectively in a no-deal context.

As I set out during the financial regulators' powers SI debate on 10 October, as a result of the UK leaving the EU the Government had to decide how to allocate responsibility for the huge body of financial services legislation being brought on to the UK statute book by the European Union (Withdrawal) Act. A significant volume of the legislation consists of EU level 2 BTS, which run to between 7,000 to 8,000 pages. The technical standards do not take policy decisions, but set out at a granular level the requirements that firms need to meet to implement policy set out in higher EU legislation.

Common examples of technical standards are those that set out the processes for firms to provide supervisory information to regulators, including the specific form templates that firms should use. The responsibility for developing and drafting the technical standards currently lies with the European supervisory authorities—ESAs—and they are then adopted by the European Commission. The European (Withdrawal) Act will bring the technical standards into UK law at the point of exit in the event that we do not reach an agreement with the EU on an implementation period. Many of the technical standards will be deficient and will require fixing to work effectively in a UK stand-alone regime.

The financial regulators' powers SI that was debated last October delegates the European Union (Withdrawal) Act power to fix deficiencies to the UK financial services regulators so that they can ensure onshored technical standards operate effectively from exit day. It sets out the procedure and requirements that the regulators must follow for amending technical standards in future. The SI listed all EU BTS that were in force at the point when the SI was laid. However, since the 2018 regulations were made, further BTS have been adopted by the Commission. It is a live process. The European (Withdrawal) Act will operate to bring the new BTS into UK law at exit day—automatically, as envisaged and as set out previously—and they contain deficiencies that need to be addressed to ensure that they work effectively in the UK after exit. It will be helpful for me to illustrate those deficiencies, because there will be references to the European Securities and Markets Authority versus the Financial Conduct Authority. They are not deficiencies in the functioning, but meaningful corrections to the wording will have to be made.

Responsibility for fixing any deficiencies in these new BTS needs to be transferred to the UK regulators. The draft instrument does that by adding the new BTS to the schedule of the financial regulators' powers SI, bringing them into scope of those regulations. Specifically, it adds BTS relating to the benchmarks regulation, the European long-term investment funds regulation, the market abuse regulation, the bank recovery and resolution directive and the capital requirements regulation, all of which have been recently adopted by the Commission.

In addition, the draft instrument also makes minor amendments to the Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018, to ensure that it effectively addresses deficiencies in the retained EU law relating to markets in financial instruments. The changes affect schedule 3 to the regulations, which deal with the transfer of functions to the Treasury and the regulators.

Regulation 3 of the draft instrument corrects a number of minor errors. Regulation 3(a) corrects a reference to regulation 396/2014 to regulation 596/2014. One wrong digit meant that the provision being amended did not refer to the market abuse regulation, as intended, and consequently the Treasury's power to make equivalence determinations in relation to regulated markets would not work effectively. Regulation 3(b) removes a provision relating to EU arrangements between member states, which was overlooked. It enables the Treasury to set out the criteria under which the operations of a trading venue in a host member state are to be considered to be of substantial importance for the functions of the markets

and the protection of investors in that state. This provision will be redundant once the UK is no longer a member state.

Regulation 3(c) corrects an incorrect cross-reference. Regulation 3(d) removes a reference to repealed legislation in paragraphs 7A(2) and (3)(a) of the schedule to the recognition requirements regulations. Regulation 3(e)(i) changes the word "notifications" to "applications", which more accurately reflects what the relevant regulator rules do. Regulation 3(e)(ii) removes a reference to an FCA rule that has now been repealed. Regulation 3(f) removes a reference to regulation 46 of the markets in financial instruments regulations 2017, which is being repealed.

While every effort is made to avoid mistakes in legislation, mistakes happen from time to time in all Departments. I assure the committee that the onshoring SIs have been through all the usual internal and external checks that secondary legislation normally goes through. The Treasury has also worked closely with the financial regulators to develop these instruments, and industry has had the opportunity to check drafts that we have published.

Considering the volume of onshoring legislation that we have been preparing, these mistakes are not out of line with those that happen from time to time in the normal legislative process. So far, we have laid 53 statutory instruments, amounting to around 1,000 pages, and I think this is the 23rd debate under the affirmative procedure. The number of mistakes identified in onshoring SIs has been low, with most being minor and technical in nature. These drafting errors in the MIFI SI were picked up as part of continuing preparations to ensure that the UK's regulatory regime operates effectively from exit. This SI therefore ensures that the MIFI SI will function as intended from exit day in a no-deal scenario.

In terms of industry engagement and transparency, the Treasury has worked closely with the regulators in the drafting of the draft instrument. The regulators will also undertake a public consultation on any deficiency fixes they propose to make to the technical standards covered by this SI. We have also engaged extensively with the financial services industry on the two key instruments to which the draft instrument relates.

In summary, the Government believe that the proposed legislation is necessary to ensure that recently adopted binding technical standards continue to operate effectively once brought into UK law by the EU (Withdrawal) Act 2018, and that the Markets in Financial Instruments SI effectively addresses the deficiencies in retained EU law if the UK leaves the EU without a deal or an implementation period. I hope colleagues will join me in supporting the draft regulations. I commend the draft regulations to the Committee.

9.49 am

Jonathan Reynolds (Stalybridge and Hyde) (Lab/Co-op): It is a pleasure to serve under your chairmanship, Sir Gary. Once again, the Minister and I are here to discuss a draft instrument that makes provision for the regulatory framework after Brexit in the event that we crash out of the EU without a deal. On each of those occasions, my Front-Bench colleagues and I have spelled out our objections to the Government's approach to secondary legislation. The Minister knows and appreciates that. This is the first of two meetings we will have today, and I will not read my speech out twice, but I will simply say that the more I see of this process, the less convinced I am that it is a good way to make such a substantive body of law.

The regulations amend the Financial Regulators' Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018, which, as the Minister described, simply list the EU regulations for which the Financial Conduct Authority, the Prudential Regulation Authority and the Bank of England are the appropriate regulator. In particular, they allocate the FCA a further set of EU regulations, taking its current figure by my count to a whopping 93. As we have raised in previous debates, it would be helpful to understand how it has been decided which powers will go to the FCA, the PRA, the Bank of England or the Treasury and how much resourcing will be given to those institutions. The Minister tends quite correctly to say that the functions of the Commission are going to the Treasury and those of ESMA are going to the FCA, but the picture is more complicated than that simple binary transfer of power. He knows that the Opposition are concerned about this unprecedented transfer of powers via secondary legislation, as any good Opposition would be, especially as there has been little consultation about the FCA specifically acquiring the powers.

Many bodies could take on powers of financial regulation alongside the FCA, the PRA, the Bank of England and the Treasury. Aspects of financial regulation could be seen as being within the purview of a democratic Parliament. There has been little explanation in statutory instruments about why other bodies, including Parliament, should not have principal oversight of former EU regulations. It is also not clear that the FCA has been given support or resourcing to discharge the major increase in powers it has been given. Without support or resourcing, the FCA will not be able to discharge new regulatory capacities effectively or responsibly. The explanatory memorandum confirms that the Treasury has not undertaken a consultation on the instrument, but it seems clear that some stakeholders have been consulted by necessity. Will the Minister clarify that point?

The explanatory memorandum also states:

> "The financial services regulators plan to undertake public consultation on any changes they propose to make to BTS or rules made under the powers conferred upon them by the Financial Services and Markets Act 2000 using the powers delegated to them by the 2018 Regulations."

It would be helpful to have further clarification on that, not least the statutory requirements for consultation. The words "plan to undertake…consultation" seem uncertain. According to the explanatory note, an

> "impact assessment…on the costs of business, the voluntary sector and the public sector will be available from HM Treasury".

However, the explanatory memorandum states:

> "An Impact Assessment has not been prepared for this instrument because in line with Better Regulation guidance, HM Treasury considers that the net impact on businesses will be less than £5 million a year. Due to this limited impact, a de-minimis impact assessment has been carried out."

The explanatory memorandum continues:

> "There is no, or no significant, impact on business, charities or voluntary bodies, as this instrument relates to maintenance of existing regulatory standards...The impact on the public sector is

[Jonathan Reynolds]

that UK financial services regulators (the Bank of England/Prudential Regulation Authority, the Financial Conduct Authority and the Payment Systems Regulator) will be responsible for fixing deficiencies in BTS so that they operate effectively from exit day, and will have ongoing responsibility for making any technical standards required under retained EU law on financial services".

It states:

"The allocation of responsibility is therefore a manageable impact."

Will the Minister confirm whether there has been an impact assessment? Either way, can we see the evidence base for those assertions?

It is ten years since the fall of Lehman Brothers and the beginning of the global financial crisis, and the Government need to reflect on how the imperative of ensuring financial stability will be met, or otherwise, by these arrangements. I am becoming increasingly alarmed by the Government's unfolding approach to regulating financial services, which seems to have no overall plan, no indication of how the different pieces of legislation fit together and, ultimately, no clarity. Rather than pushing through such a large volume of piecemeal secondary legislation, it is clear we need a consolidated piece of primary legislation.

Will the Minister explain why the Government need to update the Financial Regulators' Powers (Technical Standards etc.) (Amendments etc.) (EU Exit) Regulations 2018 and the Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018, which were made in October 2018? It suggests they are making decisions as they go along, rather than having a coherent plan. I listened to the distinction that the Minister made, which was that new legislation has to be covered by the regulations, but surely that is the purpose of the in-flight Bill, which we dealt with on the Floor of the Chamber recently. In addition, part 3 makes minor technical amendments to correct the Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018.

The Minister was frank about the errors that have been found, and right to say that for such a large volume of legislation the amount of those errors is relatively minor. As he may remember, however, Labour voted against the regulations and called for greater scrutiny, and there are still legitimate concerns about the strength of the process.

This statutory instrument must be understood in the context of the Government's chaotic approach to no-deal preparations, which has been characterised by significant transfers of power to the Treasury, the FCA, the PRA, and the Bank of England through statutory instruments. When Britain voted to leave the EU, I believe that was to empower Parliament to debate and make these decisions, not to concentrate them in the hands of a few civil servants and Ministers. As legislators we have to get this right. This is not just about the principle of democracy and accountability; this is about robust law-making that is clear, comprehensive, coherent, and enforceable.

9.10 am

Sir Geoffrey Clifton-Brown (The Cotswolds) (Con): I welcome the Minister to his place and I have one simple question that I am sure he will be able to answer: if there is a dispute over decisions made by UK regulators during the transitional period and the EU, will that be dealt with through the arbitration procedure?

9.11 am

Peter Grant (Glenrothes) (SNP): It is a pleasure to serve under your chairmanship, Sir Gary, and Members will be relieved to hear that I intend to be brief. That is not a matter of inclination—not my style at all—but a matter of necessity before my voice gives up altogether.

I did not catch the number of statutory instruments that the Minister was so proud to say have been pushed through, or how many still need to be resolved before 29 March, but coming from a Government who boast about easing the burden of regulation on businesses, that seems more than a shade ironic. None of those regulations are designed to make anything better—at best, they will keep us where we would have been had the Government's unilateral decisions following the referendum been different.

Having set the ball rolling, set the timetable, and created the danger of a no-deal Brexit, and having identified the avalanche of legislation that will be needed to cope with that, the Government failed to timetable the legislation properly. That is why, two years after article 50 was triggered, there is such a panic to get all these regulations through, and why Parliament is sitting now when Members should be back in their constituencies working. That was done not to give time to debate regulations such as these, but to allow the clock to tick forward for another four or five sitting days, so that the regulations can legally be considered before 29 March.

It is extremely concerning, although perhaps no wonder, that major financial services, businesses and employers have already decided that they do not have confidence in the United Kingdom, London or Scotland as centres of financial services to the same extent as they did previously. That does not mean that those services will disappear but—depending on which analysts we believe—between €1 trillion and €2 trillion of assets are being, or have been moved out of the United Kingdom as a result of Brexit. It will take a long time for that confidence to be restored and those jobs to return.

The Minister has consulted the financial services sector. Because of the time limit that the Government placed on themselves, I understand that there was no time for a full-scale consultation with everybody who might be affected, but it is a pity that they did not listen more to the financial services sector before they set the ball rolling in the first place. In Scotland, and in the City of London, the financial services sector is clear. If they have to do Brexit, which they do not think is a good idea, we should stay in the single market, as that would immediately ease a lot of the concerns about the application of regulations post-Brexit.

Would any of the secondary legislation that the Minister has been or will be responsible for between now and 29 March have been necessary if the Government had listened to financial institutions and agreed to stay in the European single market? After all, that would have been perfectly compatible with the referendum decision of 2016.

9.14 am

John Glen: I acknowledge the thoroughness of the scrutiny from the hon. Members for Stalybridge and Hyde and for Glenrothes, and my hon. Friend the Member for The Cotswolds, and I will address their specific points. I will refrain from going into a full disputation on the opening points made by the hon.

Member for Stalybridge and Hyde. We have gone through this matter several times. All I can say is that we are able to bring to Committee only those statutory instruments that fit within the purview of the withdrawal Act as debated. And, despite the corrections that we are having to make today, I submit that this has been a thorough process.

The hon. Member for Glenrothes said that it was with some pride that I spoke about 53 statutory instruments. There is no pride; there is just a sense of clarity about the thoroughness and rigour of this approach, which includes 30 affirmative discussions in SI Committees.

The hon. Member for Stalybridge and Hyde asked how it was decided which BTS go to the FCA and so on; he asked about the allocation mechanism across the regulators. Frankly, they are allocated according to the functions of the regulators that were given to them previously by primary legislation, and BTS will go to the Prudential Regulation Authority in line with that. The hon. Gentleman asked about the resourcing. I am very confident that the regulators are making adequate preparations and effectively allocating resources ahead of March 2019. They have considerable experience and technical expertise in regulating the financial services sector to high standards—that is why the City of London remains, despite the unwelcome uncertainty, a vibrant place for financial services at this time—and they have actively participated in a wide range of groups developing technical policy and regulatory rules and chaired a number of committees and taskforces with considerable experience in implementing EU legislation. That means that the responsibilities of EU bodies can be reassigned efficiently and effectively, providing firms, funds and their customers with confidence after exit.

The hon. Gentleman asked a question about what role is foreseen for Parliament to hold regulators to account. Parliament will continue to be involved in every aspect of the process to onshore EU financial services regulation. All the changes that the Treasury will propose to level 1 legislation and delegated Acts will be put before Parliament to approve. Any transfer of responsibility to the regulators, including any transfer of powers to make technical standards, will be put before Parliament to approve through affirmative procedure SIs. The Treasury will continue to work closely with the Bank of England, the PRA, the FCA and the Payment Systems Regulator on how we fix deficiencies in EU financial services regulation, including binding technical standards.

The hon. Gentleman asked whether the FCA has a statutory obligation to consult. Yes, that is clearly set out in the regulators' powers SI for future amendments. The regulators are consulting on all their deficiency fixes.

The hon. Gentleman asked why these additional binding technical standards were not incorporated in the relevant EU exit SIs and why they are only now being picked up. The mandates to produce these technical standards will already have transferred, post exit, the responsibility for them to UK regulators, but this SI transfers the responsibility to UK regulators for fixing deficiencies in new standards that have come into force since we laid the original SI. This SI is about making sure that our regulators are able to ensure that those are fixed in time for the standards to operate effectively from exit day.

The hon. Gentleman asked about an impact assessment. The reason why there is not one is the de minimis impact; there will be no impact on industry from this SI. It concerns the regulators' functions and makes minor amendments to MIFI. That has already been impact-assessed.

My hon. Friend the Member for The Cotswolds asked about a dispute between the EU and our regulators. A process for consultation is set out in the financial regulators' powers SI. Where regulators do not agree on a joint approach, they can each make separate provision in relation to the parts of the financial services industry they are responsible for regulating, so there is inherently some discretion there, but in the context of the accountability I set out, there are checks to that. However, through this process, there will not be any policy deviation from what has already been agreed.

I hope I have addressed the points that were raised. I recognise that going through all these statutory instruments is an arduous process, and I acknowledge the comments made by the hon. Member for Stalybridge and Hyde about the undesirability of the process. Of course, if we get a deal, which is the Government's intention and policy, these SIs will not be required. However, it is important that we ensure that recently adopted binding technical standards continue to operate effectively and that the markets in financial instruments SI effectively addresses the deficiencies in retained EU law if the UK leaves without a deal or an implementation period.

I hope I have adequately responded to the points that were raised, and I hope the Committee has found the sitting informative and will be able to support the draft regulations.

Question put and agreed to.

9.20 am

Committee rose.