PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Seventeenth Delegated Legislation Committee

DRAFT SECURITISATION (AMENDMENT) (EU EXIT) REGULATIONS 2019

Wednesday 27 February 2019

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Sunday 3 March 2019

The Committee consisted of the following Members:

Chair: David Hanson

† Beckett, Margaret *(Derby South)* (Lab)
† Cadbury, Ruth *(Brentford and Isleworth)* (Lab)
† Dunne, Mr Philip *(Ludlow)* (Con)
† Glen, John *(Economic Secretary to the Treasury)*
Hepburn, Mr Stephen *(Jarrow)* (Lab)
† Hughes, Eddie *(Walsall North)* (Con)
† Knight, Julian *(Solihull)* (Con)
† Linden, David *(Glasgow East)* (SNP)
† McCarthy, Kerry *(Bristol East)* (Lab)
† Mak, Alan *(Havant)* (Con)
† Menzies, Mark *(Fylde)* (Con)
† Reynolds, Jonathan *(Stalybridge and Hyde)* (Lab/Co-op)
† Rowley, Lee *(North East Derbyshire)* (Con)
† Shelbrooke, Alec *(Elmet and Rothwell)* (Con)
† Smith, Jeff *(Manchester, Withington)* (Lab)
† Walker, Thelma *(Colne Valley)* (Lab)
† Whittaker, Craig *(Lord Commissioner of Her Majesty's Treasury)*

Dominic Stockbridge, *Committee Clerk*

† attended the Committee

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[David Hanson *in the Chair*]

Draft Securitisation (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 Securitisation (Amendment) (EU Exit) Regulations 2019.

It is a pleasure to serve under your chairmanship, Mr Hanson.

This statutory instrument is part of a programme of legislation under the European Union (Withdrawal) Act 2018 aimed at ensuring that, if the UK leaves the EU without a deal or an implementation period, there continues to be a functioning legislative and regulatory regime for financial services in the UK. The SI will fix deficiencies in EU law on securitisation to ensure that it continues to operate effectively after the UK leaves the EU. The approach taken in the legislation aligns with that taken in other SIs laid under the EU withdrawal Act, providing continuity by maintaining existing legislation at the point of exit, but amending where necessary to ensure that it works effectively in a no-deal context.

The SI concerns securitisation, a process by which financial assets such as loans can be pooled into a single financial instrument called a security, which can then be sold to investors. Securitisation allows banks to transfer some of the risk associated with the assets they hold to investors, freeing up regulatory capital to facilitate further lending. Securitisations can themselves be used to finance business activities and reduce the concentration of financial stability risks.

To respond to concerns about the opaqueness and complexity of securitisation transactions, the EU adopted the securitisation regulation, which is based on international standards agreed by the Basel Committee on Banking Supervision. The EU securitisation regulation simplifies and consolidates a patchwork of earlier rules, and introduces the concept of a securitisation that is "simple, transparent and standardised", also referred to as an STS securitisation. Under the regulation, those are incentivised through preferential capital treatment. The securitisation regulation is important for protecting domestic financial stability while ensuring that the benefits of those instruments to firms and the wider economy remain available.

The securitisation regulation will be transferred to the UK statute book by operation of the EU withdrawal Act on exit day, but in a no-deal scenario the UK would be outside the European economic area and outside the EU's legal, supervisory and financial regulatory framework, and that legislation would no longer be operative. The SI makes the necessary amendments to ensure that the provisions continue to work properly in a no-deal scenario.

The SI amends the geographical scope of the EU regulation to ensure that UK investors can continue to have access to the EU market for STS securitisations and to global securitisation markets more broadly. Under the current EU regulation, all parties involved in an STS transaction must be located in the EU. The SI amends that to allow UK counterparties to continue to participate in cross-border STS securitisations where some of the parties are located anywhere in the world, expanding the current scope. That approach is appropriate because most securitisations are structured across borders, and it ensures that third countries are treated equally in the event of a no-deal scenario.

For UK securitisation markets to have maximum depth and liquidity while being subject to the same strict rules introduced by the securitisation regulation, it was important not to constrain the UK market by requiring all parties to be located in the UK. I recognise that that expansion of scope is likely to arouse concerns, but it is also clear that the SI requires at least one of the parties to a securitisation to be located in the UK. The overall effect of that change in scope is to support liquidity in domestic securitisation markets while ensuring that UK supervisors retain effective oversight of securitisation as a whole.

The SI also introduces a transitional regime for the recognition of EU STS securitisations in the UK during a two-year period after the UK leaves the EU. That ensures that UK investors can continue to participate in the EU market for STS securitisations for that limited period. Any STS recognised by the EU during that two-year period will continue to be recognised in the UK until its maturity.

The SI also clarifies the definition of "sponsor" in the securitisation regulation to ensure that, when a sponsor wishes to delegate day-to-day portfolio management to a third party, that third party can be located anywhere in the world and not just in the EU. The securitisation regulation currently limits the location of the delegated firm to the EU. The European Commission has acknowledged that that is an unintended effect and is currently developing an EU-wide solution.

Finally, this SI transfers several functions carried out by the European supervisory authorities to the Financial Conduct Authority and the Prudential Regulation Authority. Most importantly, the SI transfers responsibilities for the authorisation and supervision of trade repositories and the publication of STS notifications to the Financial Conduct Authority. That is appropriate given the FCA's considerable experience in supervising securitisations and it has been preparing for that role in anticipation of the regulation going live on 1 January this year. The Treasury has worked very closely with the PRA and the FCA in drafting the instruments. It has also engaged the financial services industry and will continue to do so. On 19 December, the Treasury published the instrument in draft, along with an explanatory policy note, to maximise transparency to Parliament and industry. An impact assessment was published on 19 February.

In summary, this Government believe that the proposed legislation is necessary to ensure that the UK has a workable regime regulating securitisations, and that the legislation will continue to function appropriately if the UK leaves the EU without a deal or an implementation period. I hope colleagues will join me in supporting the draft regulations, which I commend to the Committee.

9.1 am

Jonathan Reynolds (Stalybridge and Hyde) (Lab/Co-op): It is a pleasure to serve under your chairmanship, Mr Hanson. Once again, the Minister and I are here to discuss a statutory instrument that would make provision for the regulatory framework after Brexit in the event we crash out without a deal. On each occasion, my Front-Bench colleagues and I have spelled out our objections to the Government's approach to the process.

Today we are here to discuss the draft Securitisation (Amendment) (EU Exit) Regulations 2019. Given the impact that securitisation had on the wider economy and its role in the 2008 global economic crisis, I am sure I do not need to remind anyone in the room of the importance of ensuring that the securitisation market is properly regulated and monitored. The Opposition have laid out its wider concerns on the no-deal regulatory provision process for financial services, which incorporates dozens of statutory instruments and the in-flight bill for EU legislation that is in train but not yet implemented. We believe there should have been a consolidated financial services Bill that presented a single overview of the changes proposed, which would allow us thoroughly to scrutinise and assess the new allocation of powers across different regulators and institutions.

This statutory instrument is a case in point. We have already debated one business-as-usual securitisation SI, which was subject to the negative procedure, to implement new European regulations. Now we have another securitisation SI, related to no deal and subject to the affirmative procedure, just a few weeks later. The powers allocated in the other SI are complicated by their interaction with this one, as my hon. Friend the Member for Oxford East (Anneliese Dodds) stated on 13 February in the debate on that instrument.

I want the Minister to clarify some points that are of concern to the Opposition. First, the explanatory memorandum highlights that an exemption is provided to national promotional banks, and that the exemption will continue for UK parties only, namely the British Business Bank. Where does that leave existing securitisation deals with exposure to entities such as the German KfW, given that their preferential treatment will be removed? Will those deals need to be liquidated and novated the British Business Bank? I am sure the Minister agrees that that has the potential to be highly disruptive. What would their legal status be?

Secondly, what long-term plan does the Treasury have to ensure that securitisation regulations will continue to be robust given the volume of powers that will be transferred to the FCA? Much of the securitisation regime has not been developed domestically, as the Minister said, yet we will take full onshore responsibility for regulating and monitoring a regime that might contain substantial risks.

I reiterate my hon. Friend's comments in the debate of 13 February about the new powers bestowed on the FCA, and on which we still do not have full clarity. It seems that under the Treasury's proposed approach of transferring powers that rest with the European systemic risk board, the FCA can permit re-securitisation for specified legitimate purposes in an exemption to the general ban. The general ban prevents the underlying assets of a securitisation from being themselves securitised assets, which as we know is the type of circular activity that caused the issues that in many ways led to the financial crisis. Will the Minister explain what checks and balances will be in place to ensure that the development of this regulation is properly scrutinised and monitored? That is all I have for the Committee this morning.

9.5 am

David Linden (Glasgow East) (SNP): It is always a pleasure to serve under your chairmanship, Mr Hanson. I have a degree of sympathy for the Minister, who I believe is pretty much camped out here in these delegated legislation Committees—I am just the latest in the rota of Scottish National party colleagues to cover a DL Committee.

With only a month until the UK leaves the EU, it is frankly a disgrace that the UK Government are only now getting round to sorting out these details. Time is of the essence when we know the UK is due to leave at the end of next month. Scotland's financial sector has been clear that its interests are best served in the EU single market and customs union. Ten years after the crash, our financial services sector needs meaningful reform, not new problems stemming from Brexit. Instead of planning how to minimise the damage, we should instead be using our time here to plan a successful future inside the EU.

We know that this statutory instrument will not stop the tide of financial services jobs and assets leaving the UK because of Brexit. Financial services firms are voting with their wallets already and have moved assets worth $1 trillion from the UK to the rest of Europe since the Brexit referendum, according to EY. According to Bloomberg, Deutsche Bank AG is repatriating at least €400 billion to Frankfurt, with JPMorgan taking €200 billion, Goldman Sachs €60 billion, CitiGroup €50 billion and Morgan Stanley €40 billion.

We know the impact that these Brexit shenanigans are having on our economy, and I do not think this SI will do anything much to stem that tide of financial services jobs leaving the UK. While I will not be pushing this to a vote, I want to put that on the record. What we see here is a British Parliament and a British Government that are making no sense whatsoever and are not serving Scotland's interests.

9.7 am

John Glen: I acknowledge the points made by the hon. Members for Stalybridge and Hyde and for Glasgow East. I accept the wider concerns raised about the extensive use of this mechanism. I have never described it as the perfect solution, but it is a necessary solution to the risk of a no deal situation. I am determined that, by the time we get to the end of this process on 11 March, we will have a functioning regulatory regime in place, but the volume of SIs has been considerable. It was a blessed relief when the hon. Member for Glasgow East convened a three-hour debate on bank closures the other week and gave me a change of venue.

The hon. Member for Stalybridge and Hyde raises three specific points. The first was the removal of preferential treatment for exposures to national promotional banks and how that affects UK firms holding such exposures. Under the EU securitisation regulation, exposures to national promotional banks are exempt from the requirements, so in a no-deal scenario the UK would

[John Glen]

fall outside the scope of the exemption in the EU and domestic institutions such as the British Business Bank would not be able to benefit from the EU's exemptions.

This SI removes the exemption for EU national promotional banks such as the one the hon. Gentleman mentioned, ensuring that under the domestic regime only UK national promotional banks would be able to benefit from the exemption. This is in line with the Government's general approach to treating the EU as a third country if there is no deal and no implementation period. We have raised the point with industry and we understand that it is not likely to create significant difficulties for UK firms.

The hon. Gentleman went on to raise an issue that has been raised previously, and perfectly reasonably, about the adequacy of the resources of UK regulators to handle their new responsibilities. It is important to make clear to the Committee that the purpose of the EU securitisation regulation is to encourage and to ensure that the mistakes of the financial crisis in respect of securitisation are not repeated. By keeping securitisations simple in form and making them more transparent, that will be achieved.

Under the regulation that applied from only January this year, the PRA and FCA already carry out most of the functions conferred on them by this SI. The main responsibilities transferring into the FCA relate to the authorisation and supervision of a small number of trade repositories and the publication of STS notifications on its website. It is not anticipated that that will create a significant new burden. The FCA has specialist securitisation expertise and has made extensive preparations, including training for supervisors in anticipation of the implementation of the regulation and the onshoring of the requirements. It has also carried out an assessment of the resource implications and will keep those under review to ensure that it can deliver on its responsibilities, so I do not have any significant or meaningful concerns about that.

As to checks being made to ensure that the developments in regulation are scrutinised, it is worth noting that the SI does not make any substantive policy changes. To ensure that the UK regime is operative after exit, the UK regulators maintain full oversight of UK STS securitisations after exit, and will have sufficient enforcement powers where there is non-compliance. The regulators will monitor the market, and the Financial Policy Committee will also play a role in ensuring the functioning of the regime.

The hon. Member for Glasgow East raised the issue of moving high volumes of capital out of the UK. The Treasury is in frequent contact with firms and regulators regarding their contingency planning for EU exit. The political declaration reflects the full ambition of our proposals, set out in the White Paper, and is a strong and credible basis for moving our negotiations with the EU forward into the implementation period, to achieve a deal that works in our mutual interests. I acknowledge the significant footprint of financial services firms in Scotland, and in Edinburgh and Glasgow particularly. We believe that what is set out will serve their interests well. While we have been clear that passporting will come to an end after we leave the EU, we are seeking a relationship that will allow for cross-border trade in financial services, and allow firms to continue European operations within the UK.

I think that those were all the points that were raised. The SIs being brought forward are needed, and the one before the Committee is particularly needed, to ensure that EU law on securitisation continues to operate effectively in the UK if we leave the EU without a deal or implementation period, which is not the Government's policy. I hope that the Committee have found this morning's sitting informative and will join me in supporting the regulations.

Question put and agreed to.

9.12 am

Committee rose.