PARLIAMENTARY DEBATES

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OFFICIAL REPORT

Eighteenth Delegated Legislation Committee

DRAFT INVESTMENT EXCHANGES, CLEARING HOUSES AND CENTRAL SECURITIES DEPOSITORIES (AMENDMENT) (EU EXIT) REGULATIONS 2019

Monday 11 March 2019

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Friday 15 March 2019

The Committee consisted of the following Members:

Chair: Philip Davies

Beckett, Margaret *(Derby South)* (Lab)
Blackman, Kirsty *(Aberdeen North)* (SNP)
† Blunt, Crispin *(Reigate)* (Con)
† Braverman, Suella *(Fareham)* (Con)
† Crouch, Tracey *(Chatham and Aylesford)* (Con)
† Dodds, Anneliese *(Oxford East)* (Lab/Co-op)
† Glen, John *(Economic Secretary to the Treasury)*
Jones, Mr Kevan *(North Durham)* (Lab)
Killen, Ged *(Rutherglen and Hamilton West)* (Lab/Co-op)
† McLoughlin, Sir Patrick *(Derbyshire Dales)* (Con)
† Mercer, Johnny *(Plymouth, Moor View)* (Con)
† Merriman, Huw *(Bexhill and Battle)* (Con)
† Metcalfe, Stephen *(South Basildon and East Thurrock)* (Con)
† Nandy, Lisa *(Wigan)* (Lab)
† Smith, Jeff *(Manchester, Withington)* (Lab)
† Walker, Thelma *(Colne Valley)* (Lab)
† Whittaker, Craig *(Lord Commissioner of Her Majesty's Treasury)*

Yohanna Sallberg, *Committee Clerk*

† attended the Committee

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[Philip Davies *in the Chair*]

Draft Investment Exchanges, Clearing Houses and Central Securities Depositories (Amendment) (EU Exit) Regulations 2019

4.30 pm

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

That the Committee has considered the draft Investment Exchanges, Clearing Houses and Central Securities Depositories (Amendment) (EU Exit) Regulations 2019.

It is a pleasure to serve under your chairmanship again, Mr Davies. The Treasury has laid this statutory instrument under the European Union (Withdrawal) Act 2018 and the European Communities Act 1972. The Treasury has undertaken a programme of legislation to ensure that if the UK leaves the EU without a deal or an implementation period, there will continue to be a functioning legislative and regulatory regime for financial services in the United Kingdom. This statutory instrument, which was debated and approved by the House of Lords on 25 February, is part of that programme.

The regulations address legal deficiencies in parts of the domestic legislation that outline certain regulatory requirements for recognised investment exchanges, European economic area market operators, central counterparties and central securities depositories operating in the UK. Those entities facilitate the trading, clearing and settlement of financial instruments, and are therefore significant for the functioning of the UK's financial markets. Amendments introduced through the instrument are generally technical and do not intend to make policy changes, other than where appropriate to reflect the UK's new position outside the EU and to ensure a smooth transition.

I will describe the key amendments that the instrument makes to the Financial Services and Markets Act 2000. First, as a consequence of the UK exiting the EU, the European Securities and Markets Authority will no longer carry out functions to determine whether third-country CCPs and CSDs can provide services in the UK post-exit. Those responsibilities are being transferred to the Bank of England through other statutory instruments that have previously been debated in Committee. To ensure that the Bank of England can carry out those new functions effectively, the instrument contains appropriate consequential amendments to reflect that in domestic law.

As the definition of a third-country CSD will change—to refer to any CSD located outside the UK, rather than any CSD located outside the EEA—the instrument deletes redundant references to the term "EEA CSD". The instrument also provides the Bank of England with the appropriate supervisory powers over third-country CSDs, such as the power to require information and to inspect any UK branch of a third-country CSD.

Secondly, in line with those changes, a provision within FSMA that currently applies to the Prudential Regulation Authority is being extended to the Bank of England. The relevant provision places a duty on the Bank of England to take such steps as it feels are appropriate to co-operate with other persons, whether in the UK or elsewhere, who have similar regulatory or financial stability functions. That provision is being extended to the Bank of England to ensure that co-operation continues in relation to the new functions that it is taking on as part of the legislation.

Thirdly, the instrument removes the FSMA provisions that relate to the exercise of EEA passporting rights by EEA market operators into the UK, and the provisions that allow recognised investment exchanges to make passporting arrangements into EEA states, given that the UK will be a third country in a no-deal scenario. That means that any EEA market operator currently operating in the UK via a passport could no longer do so from exit day, just as UK-recognised investment exchanges could no longer passport into EEA states.

Instead, EEA market operators that currently make use of passport rights can, if they wish, make use of the third-country regimes for investment exchanges that are provided for in UK law to carry on their activities in the UK. For example, they may seek to apply to the Financial Conduct Authority to become a recognised overseas investment exchange. The FCA published information that outlines how firms can do that on its website on 14 September 2018.

Fourthly, the statutory instrument removes obligations that relate to information sharing and co-operation with EU authorities, again to reflect the UK's position outside the EU in a no-deal scenario. That is consistent with other statutory instruments previously approved by Parliament under the EU (Withdrawal) Act, and does not preclude the UK authorities from co-operating with their EU counterparts in the future.

Specifically, this instrument removes the obligation for the FCA to inform ESMA and the competent authorities of EEA member states when it suspends or removes a financial instrument from trading on a venue that falls under its jurisdiction. However, the FCA will still be required to make such decisions public. In addition, the FCA will no longer be obliged to require venues under its jurisdiction to suspend or remove a financial instrument from trading if the FCA becomes aware that the same instrument has been suspended or removed from trading in an EEA member state.

Finally, this instrument makes a number of amendments and consequential amendments to other legislation, principally the Financial Services and Markets Act 2000 (Recognition Requirements for Investment Exchanges, Clearing Houses and Central Securities Depositories) Regulations 2001. These amendments make various necessary changes to those instruments, such as amending definitions to ensure consistency with definitions used in other EU exit SIs, including the Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018, the Central Counterparties (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2018 and the Central Securities Depositories (Amendment) (EU Exit) Regulations 2018, all of which have previously been debate in this place.

The Treasury has been working closely with the FCA, the Bank of England and industry in respect of these instruments, to maximise transparency. Regulators and

industry have welcomed the Government's approach to this SI. This instrument was first published, with accompanying explanatory notes, for sifting on 30 November 2018. Following a recommendation from the European Statutory Instruments Committee, it was re-laid under the affirmative procedure on 17 January 2019.

In summary, the Government believe that the proposed legislation is necessary to ensure the smooth functioning of financial markets in the UK, if the UK leaves the EU without a deal or an implementation period. I hope that colleagues will join me in supporting these regulations, which I commend to the Committee.

4.36 pm

Anneliese Dodds (Oxford East) (Lab/Co-op): It is a pleasure to serve on this Committee with you in the Chair, Mr Davies. I am grateful, as always, for the Minister's explanation of the SI.

Once again, I want to put on the record the context in which this instrument comes before us. Parliament is currently dealing with an unprecedented number of statutory instruments. The volume and flow of secondary legislation on our exiting the EU, particularly if we leave without a deal, is deeply concerning when it comes to accountability and proper scrutiny. In the light of that, the Opposition want to place on the record our deepest concerns that the regulatory process is not as transparent as it should be.

As with previous instruments, the regulations allow for a major transfer of power to British institutions, in this case to the Bank of England. The instrument gives the Bank the power to determine whether third-country CCPs and CSDs can provide services in the UK post-exit, rather than their being undertaking by ESMA. The Government have maintained, as the Minister has said, that this is a simple transfer of power. However, our job in these Committees is to consider carefully whether the existing infrastructure of those organisations makes them best placed to take on the additional powers and responsibilities.

Will the Minister outline the analysis undertaken by the Treasury in deciding that the powers should be placed with the Bank rather than, for example, the Treasury? Will he also inform us of the work that is being done with the Bank to prepare it to take on these additional responsibilities, and what funding, if any, has been set aside to deal with the increased workload? He described the technical legal changes made by the instrument to facilitate that, but it would be helpful to know what resources have been made available.

In addition, will the Government be offering advice and assistance to EEA operators regarding their transition to becoming categorised as third-country entities? Do the Government feel that the Bank of England is adequately prepared to facilitate that transition? On that note, ESMA has, as I understand it, already recognised London Metal Exchange Clear, London Clearing House and now Intercontinental Exchange Clear Europe as third-country operators in order to avoid any Brexit no-deal cliff edge. I am, therefore, rather unclear as to why the UK Government have not undertaken a similar process for EU clearing houses. It seems that they have tried to pre-empt any cliff-edge chaos by doing that recognition now, rather than waiting for the cut-off to occur.

The arrangements place on the Bank a requirement of co-operation. Will the Minister clarify whether that duty applies to non-UK entities as well? As he has said, several SIs, including that under discussion, remove from UK bodies the duty of co-operation. Some SIs arguably go beyond the scope provided for in the EU (Withdrawal) Act. I know that the Minister disagrees with that argument, but it is a matter for discussion. It would be helpful to understand exactly whether the Bank will have a duty to co-operate only with UK regulatory bodies or with other EU27 actors. If it is the latter, why are we removing the duty of co-operation from the FCA but giving it to the Bank?

Further to those substantive queries, I am also a little surprised by the impact assessment provided to the Committee. I am aware of all the Minister's work to make sure that we receive such assessments on time, so it was good to get one. However, it clarifies that, in seeking recognition as a registered overseas investment exchange, EEA market operators

> "would incur costs by way of the application process—for example, firms will need to use their internal resources to submit the application details required by the FCA, and pay a fee…These costs arise a result of their decision to continue operating in the UK, under the existing regime, once the UK has left the EU. This is an impact of the UK leaving the EU, and not this SI, and so is outside the scope of this Impact Assessment."

It seems a little strange to suggest that an operator continuing to do what it was previously doing somehow does not need to have the impact of such a change assessed. While those costs may not technically fall within the scope of the assessment, we surely need to know about them; they are both relevant and necessary in deciding whether the current strategy towards equivalence and passporting after exit day is adequate.

4.42 pm

John Glen: I thank the hon. Member for Oxford East for her questions. She opened in familiar fashion, with respect to the challenge of volume, flow and transparency. I am sympathetic, to a point, about the volume, which we have both had to tolerate. However, this process was set out in earlier legislation. I accept that there is a dispute over the appropriateness of this mechanism, but these SIs are scrutinised prior to being laid. She made several points on the powers of transfer; the resourcing, preparation and workload of the Bank of England; advice and assistance regarding the EEA; and the requirement for co-operation. I shall endeavour to answer them thoroughly.

On whether the Bank of England will have adequate resourcing to take on the new responsibilities granted to it by the draft instrument, I am confident that it is making adequate preparations and effectively allocating resources ahead of 29 March 2019. It has considerable experience and technical expertise in regulating financial services to high standards, has actively participated in a wide range of groups to develop technical policy and regulatory rules, and has chaired several committees and taskforces. My officials have expressed no doubts with respect to that process. Although I accept that these changes are a burden on the Bank, it is very qualified to deal with them. On resourcing, the transfer of functions from ESMA to the Bank is provided for in separate SIs. I have been in regular contact with the

[John Glen]

Bank and am satisfied that its resourcing issues are resolved through its budgeting process. It has mechanisms to increase that when necessary.

The hon. Lady said that the impact assessments do not take account of the wider impact of no deal, but the impact assessments for these SIs focus narrowly on the changes they make and how businesses will need to respond. It is perfectly reasonable for the hon. Lady to assert that the wider impact of leaving the EU without a deal has not been assessed as part of this impact assessment, and I recognise that that impact is a contested space. However, an impact assessment for the EU (Withdrawal) Act deals with the impact of the parent Act, and the Government also published in November 2018 an analysis of the potential economic impact of that range of scenarios. I must stress that these SIs mitigate the impact of leaving the EU without a deal. If they were not in place, industry would face substantially greater disruption and greater cost if we left without a deal.

Anneliese Dodds: I am grateful to the Minister for his explanation, but the point I was trying to get at was not about the scope of the impact assessment in terms of different types of no-deal scenarios. I was asking why it is believed that this SI would not impact on an overseas investment exchange. The impact assessment states that any cost would be triggered by that overseas operator's deciding that it still wants to operate in the UK, rather than by the requirements of this SI. That strikes me as a little bit peculiar.

John Glen: The issue of hypothecating the cost of a decision made by an entity in another jurisdiction as a consequence of this SI is arguably stretching the range of what would be appropriate and in scope. I think we have assessed that the cost of making this application is £50,000, if I am not mistaken, but I will look into that further and write to the hon. Lady if I can provide further clarification.

It is worth my exploring two further points regarding the co-operation requirements. The PRA has an existing duty under FSMA to co-operate with other authorities, whether in the UK or elsewhere. The SI applies that duty so that the Bank of England is subject to a duty to co-operate with other bodies that undertake similar functions in connection with the Bank's functions under the European market infrastructure regulation, the central securities depositories regulation and the securities financing transactions regulation. The Bank has discretion in how it carries out that duty. Clearly, the Treasury cannot bind how other countries co-operate with UK regulators, but the duty did not exist previously, so we have put that in for those three dimensions.

On the application process, the hon. Lady cited what the European regulators have done. As I think I have said, the FCA published on 14 September 2018 a direction clarifying the way in which an application to become an ROIE would be made. That direction states that the application should be made as soon as possible and not later than six months before the applicant wishes an ROIE recognition order to take effect. The length of the application process varies on a case-by-case basis and depends to a large extent on the quality and timeliness of the information that each applicant provides. There is no mandated application form; the FCA looks to firms to provide written evidence that they are held to requirements in their home jurisdiction that have equivalent effect in the UK regime.

Anneliese Dodds: That is enormously helpful. Can the Minister clarify whether any of them have actually applied in this case? If they need that designation before they can operate and we are in theory leaving on 29 March, surely they need to have started by now.

John Glen: From memory, I think 55 could have applied and I believe 10 have successfully applied in the previous three or four months. If I have made an error, I shall correct it promptly. Regarding why we have not recognised EEA CCPs, this SI does not deal with recognition of overseas CCPs, but I will write to the hon. Lady to clarify the situation.

I hope that deals with the points raised. The Government believe that this legislation is necessary, and I hope the Committee have found my points of clarification sufficiently illuminating to allow us to pass these regulations.

Question put and agreed to.

4.49 pm

Committee rose.