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OFFICIAL REPORT

Eighteenth Delegated Legislation Committee

PROSPECTUS (AMENDMENT ETC.) (EU EXIT)
REGULATIONS 2019

Tuesday 8 October 2019

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The Committee consisted of the following Members:

Chair: IAN PAISLEY

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|---|---|
| † Dodds, Anneliese (<i>Oxford East</i>) (Lab/Co-op) | † Mann, Scott (<i>North Cornwall</i>) (Con) |
| † Duncan Smith, Mr Iain (<i>Chingford and Woodford Green</i>) (Con) | † Penrose, John (<i>Weston-super-Mare</i>) (Con) |
| Farrelly, Paul (<i>Newcastle-under-Lyme</i>) (Lab) | † Rowley, Lee (<i>North East Derbyshire</i>) (Con) |
| † Fellows, Marion (<i>Motherwell and Wishaw</i>) (SNP) | † Selous, Andrew (<i>South West Bedfordshire</i>) (Con) |
| Fitzpatrick, Jim (<i>Poplar and Limehouse</i>) (Lab) | † Smith, Jeff (<i>Manchester, Withington</i>) (Lab) |
| † Freer, Mike (<i>Lord Commissioner of Her Majesty's Treasury</i>) | † Sobel, Alex (<i>Leeds North West</i>) (Lab/Co-op) |
| † Glen, John (<i>Economic Secretary to the Treasury</i>) | † Walker, Thelma (<i>Colne Valley</i>) (Lab) |
| † Harrison, Trudy (<i>Copeland</i>) (Con) | † Yasin, Mohammad (<i>Bedford</i>) (Lab) |
| † Keegan, Gillian (<i>Chichester</i>) (Con) | Rob Page, <i>Committee Clerk</i> |
| | † attended the Committee |

Eighteenth Delegated Legislation Committee

Tuesday 8 October 2019

[IAN PAISLEY *in the Chair*]

Prospectus (Amendment etc.) (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 Prospectus (Amendment etc.) (EU Exit) Regulations 2019 (S.I. 2019, No. 1234).

It is a pleasure to serve under your chairmanship, Mr Paisley. The Government had previously made all necessary legislation under the European Union (Withdrawal) Act 2018 to ensure that, in the event of a no-deal exit on 29 March 2019, there was a functioning legal and regulatory regime for financial services from exit day. Following the extension of the article 50 process, new EU legislation has become applicable, and under the EU withdrawal Act that new legislation will form part of UK law at exit. Further deficiency fixes are therefore necessary to ensure that the UK's regulatory regime remains prepared for exit.

This statutory instrument amends the EU prospectus regulation and related legislation, including a previous EU exit instrument—the Official Listing of Securities, Prospectus and Transparency (Amendment etc.) (EU Exit) Regulations 2019, or “the official listing instrument”. The official listing instrument fixed deficiencies in the prospectus regime as it applied before 21 July 2019. This instrument will ensure that the UK continues to have an effective prospectus regime after exit, taking into account the new EU prospectus regulation, which applied across the EU from July of this year.

The EU prospectus regulation contains the standardised rules that govern the format, content, approval and distribution of the prospectus that issuers must produce when securities are offered to the public or admitted to trading on a regulated market in a European economic area state. Deficiency fixes to the new EU prospectus regulation are necessary to reflect the fact that, after exit, the UK will be outside the EU single market and the EU's regulatory and supervisory framework for financial services. The amendments in this instrument follow the same approach as the amendments made in the official listing instrument to the UK prospectus regime as it applied before 21 July 2019.

First, in line with the approach that the Government are taking to all onshored financial services legislation, this instrument transfers functions currently within the remit of EU authorities—in particular, the European Securities and Markets Authority—to the appropriate UK bodies. Such functions—for example, the development of technical rules on certain provisions of the EU prospectus regulation—will now be carried out by the Financial Conduct Authority. That is appropriate, given the FCA's expertise in applying the UK prospectus regime and the major role that it has already played in the EU to

develop technical standards. Where the EU prospectus regulation confers a delegated legislation-making power on the Commission, the powers are converted into regulation-making powers conferred on the Treasury. Use of those powers by the Treasury will need the approval of Parliament.

Secondly, this instrument removes the obligation for UK authorities to share information with the relevant EU and member state authorities. The obligations will no longer work appropriately once the UK is outside the EU's joint supervisory framework. For the purposes of supervisory co-operation, that means that the EU will be treated like other third countries. The FCA will still be able to co-operate with EU regulators, using the existing framework in the Financial Services and Markets Act 2000, as it currently does with other third countries on a discretionary basis. The UK is committed to maintaining a high level of supervisory co-operation with the EU and its member states after exit.

Thirdly, post exit, EEA issuers wishing to access the UK market will be required to have their prospectus, or their registration document—the part of a prospectus that contains information on the issuer—approved directly by the FCA, as any other third country issuer would. Currently, an EEA issuer's prospectus or registration document approved by another EEA regulator can be passported for use in the UK.

This instrument introduces transitional arrangements that will allow any prospectus approved by an EEA regulator and passported into the UK before exit to continue to be used, and supplemented with additional information, up to the end of its normal period of validity. The instrument also permits registration documents passported into the UK before exit to continue to be used as a constituent part of a prospectus in the UK, pending approval of the full prospectus by the FCA after exit. For both a full prospectus and a registration document, the period of validity is usually up to 12 months after it was originally approved.

An exemption for certain public bodies from the obligation to produce a prospectus under the EU prospectus regulation is maintained, but is extended to the same set of public sector bodies of all third countries post exit. That is in line with the approach taken in the official listing instrument previously. Members of the Committee will remember that this issue was discussed during the debate on that instrument in March; I think that the hon. Member for Oxford East raised these points then. Like then, I believe it makes sense to extend this exemption more broadly to ensure that UK capital markets continue to be attractive to public body issuers.

The EU prospectus regulation allows issuers to incorporate information from certain documents that are available electronically elsewhere, by making reference to them in a prospectus. This includes information approved by the regulator of another EEA state. To provide a smooth transition, this instrument sets out that information contained in relevant documents approved by an EEA regulator before exit day can continue to be incorporated by reference in a UK prospectus going forward. Any prospectus that incorporates information in this way will still require FCA approval before it can be used in the UK.

Lastly, the instrument ensures that matters in relation to the UK prospectus regime and transparency framework will continue to apply to Gibraltar as they did prior to

the UK's departure from the EU. This is in line with the approach taken in other EU exit instruments. Throughout the drafting process, the Treasury has worked closely with the FCA and engaged with the financial services industry—TheCityUK in particular, as a convenient body to develop this instrument.

Before I conclude, I want to address the procedure under which this instrument has been made. Along with three other financial services exit instruments, it was made and laid before Parliament on 5 September, under the made-affirmative procedure provided for in the EU withdrawal Act. This is an urgent procedure that brings an affirmative instrument into law immediately, before Parliament has considered the legislation. But the procedure also rightly requires that Parliament must consider and approve a made-affirmative instrument if it is to remain in law.

The Government have not used this procedure lightly, and it must be remembered that across Departments we have already laid over 600 exit SIs under the usual secondary legislation procedures. However, as we draw near to exit day, it is vital that we have all critical exit legislation in place, including legislation necessary to ensure that our financial services regulatory regime continues to function effectively from exit. It would have been reckless to leave that until the last minute. Industry and our financial regulators need legal certainty on the regime that will apply from exit. Without addressing the deficiencies that will arise from the EU's prospectus regulation, there would be significant legal uncertainty and disruption for issuers and regulators. Confidence in the UK's role as an international hub for the issuing of securities would be undermined.

To conclude, this Government believe that the legislation is necessary to ensure that, if the UK leaves the EU without a deal, the UK's prospectus regime can continue to function appropriately post exit. I hope colleagues across the Committee will join me in supporting these regulations. I commend them to the Committee.

9.2 am

Anneliese Dodds (Oxford East) (Lab/Co-op): It is a pleasure to serve on this Committee with you, Mr Paisley, in the Chair. As ever, I am grateful to the Minister for his explanatory remarks. As he indicated, the instrument tries to deal with some of the issues relating to passporting to the extent that these have changed with what are essentially updates to the prospectus regulation on the EU side. As he set out, it creates a transition period of 12 months for prospectuses passported into the UK. It makes provisions that mean EEA issuers wishing to issue securities in the UK will be required to secure approval of their prospectus from the FCA. Most of the changes appear to be technical, but I would like to probe a couple of issues a little further with the Minister. He has already mentioned some of them and can probably anticipate the ones that I want to ask about.

My first question is about the issue that the Minister mentioned a moment ago—the provisions in regulation 32 that extend exemptions of certain public bodies in EEA states to the same set of public bodies in both the UK and all countries outside the UK. Obviously, in various other instruments the Government have chosen to apply exemptions to countries only with equivalent regulations to those adopted by the UK. The explanatory notes suggest that restricting the exemption to UK

public bodies only was the only other possibility considered. I am curious to know why that is the case. Even under World Trade Organisation rules it would have been possible to adopt the same approach overall, which would have been to say that there would be an assessment of equivalence. It is not necessary to have a free-for-all.

Will the Minister outline what analysis has been done of the different options for this exemption and the potential impact of opening this up to all countries? It seems to constitute a material change and it is questionable whether it is coherent with the withdrawal Act. I accept that I lost that argument before, but it would be helpful to understand whether the Government have done more work on that, because it seems to me to be a major issue.

Secondly, I am confused about the process for ensuring the equivalence of accounting standards, which seems to be going round in circles. I am sure the Minister will remember that back in February, I raised the point that it appeared that the Government were not going to carry over the presumption that international financial reporting standards would be sufficient. That would potentially have placed a big burden on Ministers, who would have had to work through whether those standards would be sufficient and assess different accounting standards and so on.

The Government seemed to acknowledge that situation in April, which was great. As the explanatory note lays out, the Government

“laid a Direction in Parliament stating that IFRS as adopted by the EU would be considered equivalent...for the purpose of preparing a prospectus”

and so forth. However, the explanatory note also notes that

“this Direction will be amended to refer to the EU Prospectus Regulation”

and that

“this amendment is not contained within this instrument.”

More work still needs to be done to clarify that it will be possible to continue to assume that IFRS standards as adopted by the EU will be equivalent. Will the Minister enlighten us on when the amendment referred to in the explanatory note will be laid? As I am sure the Minister is aware, his Government have imposed a particular timetable.

Finally, as the Minister mentioned, the regulations create a 12-month transition period for approved prospectuses and registration documents approved by an EEA regulator. That clearly gives a 12-month breathing space, but we still do not appear to have a clear indication from the Government about their long-term view of passporting and seeking equivalence. The Minister referred to legal uncertainty for issuers. I would argue that that uncertainty is already there in the concern about what will happen after a year.

I am sure the Minister is aware of recent research that indicates the fastest and deepest fall in financial services over the last few months since the time of the global financial crisis. That is linked to some of the issues about regulatory equivalence tied to market access. I would be grateful to hear about that from the Minister; we did talk a little about it last night. Will he provide an indication of the Government's thinking on equivalence on financial services into the future? That is the context; the regulations are clearly trying to set up an interim situation for one year, but I am sure that any issuers and

[Anneliese Dodds]

others involved in financial services will be saying, “Well, we really need to know what the situation is going to be after a year.” We have not had an indication on that from the Government as part of their description of the current negotiations that they are having with the EU. As I have already said, financial services did not seem to be really mentioned at all last week.

9.8 am

Marion Fellows (Motherwell and Wishaw) (SNP): The SNP’s position is quite clear. The statutory instrument is part of an attempt to patch up the damage to our financial services caused by a Brexit that Scotland did not vote for. I note that, as ever, the hon. Member for Oxford East makes good and cogent points; she is well able to pick holes and to identify what could be problems for the Government. She brought back memories of my youth, when I studied financial regulations—they are not, it has to be said, always happy memories.

The Government should realise the damage that exit from the EU will do and has already done to the Scottish economy. As the hon. Member for Oxford East said, there is a real lack of confidence in the financial sector as a result of this round of EU exit negotiations, and the lack of clarity for businesses in the sector is having an effect. Since 2016, \$1 trillion-worth of assets have been moved from the UK to the EU, and that money could have been used to help bring a better future to the UK, and especially to Scotland. It is another piece of Brexit red tape, the pace of which continuously demonstrates how poorly the Government is prepared for Brexit.

The Government are changing a vast number of regulations, and this change increases the regulatory burden on businesses that are already suffering from Brexit uncertainty. Can the Minister respond to the technical points raised by the hon. Member for Oxford East? We are all very interested in the answers. Does the Minister really think that this is the best way forward for the UK and Scotland?

9.10 am

John Glen: I appreciate the three points raised by the hon. Member for Oxford East. In typical fashion, she has got to the heart of some of the core matters of the SI. I will address regulation 32, the accounting standards and the wider point she makes about the 12-month transition. I will then deal with the points raised by the hon. Member for Motherwell and Wishaw on the broader effect of this process on the financial services industry.

On the first point—the consideration we have given to the risk of extending public bodies exemption to all third countries—we have worked closely with the FCA in the drafting of the instrument to ensure that investors remain suitably protected, and we believe this approach offers the most appropriate balance between investor protection and maintaining the attractiveness of the UK’s capital markets. It is in line with the approach taken in the previous official listing SI that we discussed.

As with all investments, there is a risk that public bodies offering securities could fail, and a prospectus might help an investor to understand that risk. However,

there is generally more information available to potential investors on public bodies, such as sovereign issuers and state bodies that currently make use of the exemptions, than on corporate entities. For that reason, we feel that it is justified. We will, of course, keep the arrangements under review and consider them if they appear to expose investors to disproportionate risk—there is no complacency on that point.

The hon. Member for Oxford East made a second point on accounting standards. She raised the issue of the appropriateness of the Government to specify the accounting standards deemed equivalent to UK international accounting standards, and she asked whether we are making new decisions. Unlike the delegated Act under the EU prospectus directive, the delegated Act under the EU prospectus regulation does not explicitly state which third countries’ accounting standards have already been deemed equivalent for the purpose of preparing a prospectus. The ambiguous drafting of the EU prospectus regulation leaves the position unclear, which might create uncertainty for market participants on which accounting standards are permitted post-exit.

To ensure consistency and clarity for market participants, the instrument explicitly provides for a new article on the accounting standards that are permitted to be used when preparing a prospectus for use in the UK, and its introduction is supported by the FCA. The article does not go beyond what is currently permitted under the EU regime; it does not designate any new third countries’ accounting standards that were not previously explicitly stated in the prospectus directive, as equivalent for the purpose of preparing a prospectus. All the current equivalent regimes for accounting standards will continue to be equivalent after exit.

The hon. Member for Oxford East asked about the 12-month transition and suggested that there is a gap and an inadequacy in the long-term view, and that this impacts on the resilience of the City. I recognise that uncertainty is unwelcome, and the Government are working to secure a deal. In a situation where that is not secured, there will need to be a considerable amount of additional work in the light of the new reality. At the suggestion of many groups in the City, we have started a review that looks at an air traffic control mechanism to deal with all the regulations that exist coming in from the City. That call for evidence will conclude on 18 October, and there will be a series of further regulatory reviews, but their nature and scope will be determined by the outcome of the process that we are in during this month.

A lot of work is going on to look at the financial services industry and its competitiveness. What we need to do is get that balance between systemic stability, which all parties have been committed to ensuring since the crash, and the future.

The hon. Member for Motherwell and Wishaw referred to her party’s position on Brexit. In the interest of time and of trying to get the heart of the concerns about the financial services, I will focus on the area that I am familiar with. I have grave sympathy with her for having had to study these matters, but I guess that was her choice.

The hon. Lady refers to the \$1 trillion of assets that has been moved offshore. The City has made modest and consistent contingency arrangements. There is no

denying that it would be undesirable for extra costs to accrue, but in the context of this significant decision of the UK as a whole—although I acknowledge that her view on that is different—those decisions have been made.

This process actually avoids red tape, because it keeps us completely aligned with where we are as members of the EU. The fact that a de minimis assessment was made illustrates that it will not cost the industry additional sums. I take seriously the footprint of financial services across the United Kingdom—including in Edinburgh and Glasgow, where it is significant, as the hon. Member for Motherwell and Wishaw knows better than I. We will

do everything we can to take appropriate measures in all circumstances to safeguard the health of the financial services industry.

In conclusion, the instrument is needed to ensure that the UK has an effective prospectus regime and that the legislation functions appropriately after the UK has left the EU. I hope that I have answered the points thoroughly, that the Committee has found the sitting informative, and that it will join me in supporting the regulations.

Question put and agreed to.

9.17 am

Committee rose.

