FINANCIAL SERVICES AND MARKETS BILL

Memorandum from His Majesty's Treasury to the Delegated Powers and Regulatory Reform Committee

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Introduction

1. This memorandum has been prepared for the Delegated Powers and Regulatory Reform Committee to assist with its scrutiny of the Financial Services and Markets Bill ("the Bill"). The Bill was introduced in the House of Commons on 20 July 2022. This memorandum identifies the provisions of the Bill that confer powers to make delegated legislation. It explains in each case why the power has been taken and explains the nature of, and the reason for, the procedure selected.

Purpose and effect of the Bill

2. Financial and related professional services play a crucial role in supporting the UK economy by employing 2.3 million people across the UK (with two thirds of them based outside London), contributing nearly £100 billion in taxes and creating £1 in every £10 of the UK's economic output.

3. The Bill is central to the delivery of the government's vision for the future of the financial services sector. It seizes the opportunities of Brexit, tailoring financial services regulation to UK markets to bolster the competitiveness of the UK as a global financial centre and deliver better outcomes for consumers and businesses.

4. The Bill will:
   a. Implement the outcomes of the Future Regulatory Framework Review by:
   i. Revoking retained EU law on financial services and replacing it with an approach to regulation that is designed for the UK by building on the existing model established by the Financial Services and Markets Act 2000 ("FSMA 2000").
   ii. Introducing new secondary statutory objectives for the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA") to provide for a greater focus on growth and international competitiveness, while maintaining their existing primary objectives.
   iii. Ensuring appropriate oversight of the regulators by Parliament and government, and strengthening the regulators' engagement with industry stakeholders.

   b. Make the UK an open and global financial hub by:
   i. Enabling the implementation of financial services Mutual Recognition Agreements ("MRA"), including the UK's ongoing negotiations for a UK-Switzerland MRA.
   ii. Introducing a new equivalence regime for overseas securitisations that are Simple, Transparent and Standardised ("STS") to improve choice for UK investors.

   c. Harness the opportunities of innovative technologies in financial services by:
   i. Establishing regulatory 'sandboxes' for Financial Infrastructure ("FMI"), to allow firms to experiment with new technologies and practices, to provide the services that underpin financial markets.
   ii. Bringing stablecoins (a type of cryptoasset) within regulation when used as a form of payment, paving their way for safe adoption in the UK.

iii. Reducing risk to the finance sector from critical third parties, supporting the safe adoption of cloud services and the benefits they can bring.

d. Bolster the competitiveness of UK markets and promote the effective use of capital by:

i. Implementing the outcomes of the Wholesale Markets Review. This includes removing unnecessary restrictions on where and how trading can happen so that firms have greater choice about where they can trade in order to get the best price for investors, while maintaining high standards of regulation.

ii. Enabling the delivery of reforms following Lord Hill's UK Listing Review, to make the UK's prospectus regime simpler, more agile and more effective.

iii. Providing regulators with greater powers to manage insurers and central counterparties in financial distress.

iv. Introducing a new senior managers and certification regime for certain types of FMI, to strengthen the individual accountability of senior managers and promote high standards of conduct within them.

e. Support the levelling up agenda, promote financial inclusion and consumer protection by:

i. Ensuring that people across the UK continue to be able to access their own cash with ease.

ii. Enabling credit unions to offer a greater range of products and services.

iii. Minimise the risk of consumers being exploited by misleading financial promotions.

iv. Enabling regulatory action by the Payment Systems Regulator ("PSR") to mandate the reimbursement of victims of "authorised push payment" scams.

v. Ensuring greater co-operation between the Financial Ombudsman Service ("FOS"), the FCA and the Financial Services Compensation Scheme ("FSCS").

f. As a global financial sector, certain changes are also required to ensure that the UK's financial services regulatory framework continues to operate effectively by:

i. Improving the funding model for the Bank of England ("the Bank").

ii. Ensuring public sector terrorism reinsurers comply with relevant government controls.

iii. Allowing disciplinary action against formerly authorised firms, addressing an existing loophole.

iv. Reflecting FSCS's reclassified status in legislation.

v. Reducing the risk of unfit persons acquiring controlling stakes in firms.

vi. Making minor and technical amendments to the Banking Act 2009.[1]

[1] Banking Act 2009 c.1.

Approach to delegated powers

5. To support its policy objectives, the Bill includes a number of delegated powers. The majority of these powers are well precedented in similar legislation, for example FSMA 2000 and the Banking Act 2009. The model for financial services regulation established by FSMA 2000 delegates the setting of regulatory standards to expert, operationally independent regulators, the PRA and the FCA, that work within an overall policy framework set by government and Parliament. The government considers that this model remains the most appropriate way to regulate financial services so that the UK benefits from increased regulatory agility. Delivering a comprehensive FSMA 2000 model of regulation requires moving away from the EU legislative approach that was designed to deliver single harmonised approach across 28 member states to one which is both suitably tailored to the UK's position outside the EU and which reflects the unique nature of the UK's financial services sectors.

6. This will involve the repeal of retained EU law relating to financial services, to confer powers on HM Treasury to make secondary legislation, or the regulators to make rules, that replace retained EU law. It is important to note that, while the Bill transfers extensive responsibilities for rulemaking in financial services to the regulators, it balances this with new accountability measures that ensure appropriate democratic input and transparent oversight.

7. More broadly, the powers are drawn as narrowly as possible and have only been used to serve five functions:
    i. to empower the regulators to make the direct rules that financial services firms must comply with, in line with moving from an EU model to a wholly UK model of regulation;
    ii. to allow the government to give effect to decisions that will be taken in the future, following the processes established in the Bill and with appropriate Parliamentary engagement;
    iii. to allow appropriate flexibility in the legislation to enable updates so that the UK can keep pace with market developments and enable alignment to international standards;
    iv. to allow for technical amendments too detailed for primary legislation; and
    v. to make technical fixes to legislation to ensure it works.

8. Provisions are described below in the order in which they appear in the Bill.

Background

FUTURE REGULATORY FRAMEWORK

Removal of Retained EU Law

9. The UK's underlying model of financial services regulation was introduced by FSMA 2000. The FSMA 2000 model delegates the setting of regulatory standards to the independent financial services regulators; the PRA and the FCA (together "the regulators"). Under the FSMA 2000 model, regulatory standards are set by the regulators in their rulebooks and the regulators operate within an overall policy framework set by government and Parliament through a mixture of primary and secondary legislation. This framework operates as a limit to regulators' powers and provides an accountability framework so the regulators can be held to account for how they exercise their powers. The FSMA 2000 model is designed to be responsive to changes and allows HM Treasury and the regulators to react nimbly to emerging risks and new products and practices to bring activities inside the regulatory perimeter in a proportionate manner.

10. The FSMA 2000 model already exists for activities where FSMA 2000 requires the person conducting the activity to be authorised by the PRA or the FCA to carry out the activity. This is dealt with in FSMA 2000 by providing, in section 22, that HM Treasury can specify activities which require authorisation by the FCA and the PRA. Schedule 2 to FSMA 2000 provides examples of the types of activities HM Treasury may specify in regulations, although this Schedule is illustrative and does not restrict the power in section 22 (section 22(3) FSMA 2000). The statutory instrument through which HM Treasury specifies the activities is the Financial Services and Markets Act (Regulated Activities) Order 2001 ('RAO').[2]

11. Financial services regulations need to be updated regularly to take account of new products, practices and markets, and emerging risks and opportunities. This is what FSMA 2000 is designed to do, by delegating the setting of perimeter matters to HM Treasury and regulatory requirements to the regulators, working within an overall policy framework set in primary legislation. The Bill uses the FSMA 2000 model as a guide for new regulatory frameworks.

12. However, during the UK's membership of the EU, and particularly following the global financial crisis, the majority of the UK's financial services regulation was developed and delivered at an EU level through EU legislation, which set a large part of the regulatory standards directly rather than delegating responsibility to the regulators. The FCA and the PRA supervised and enforced these rules. When the UK left the EU, the body of EU legislation that applied directly in the UK at the point of exit was transferred onto the UK statute book through the European Union (Withdrawal) Act 2018 ("EUWA")[3] and secondary legislation made pursuant to EUWA. This is known as retained EU law.

13. Broadly speaking, retained EU law falls into the following categories:

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[2] S.I. 2001/544.

[3] European Union (Withdrawal) Act 2018 c.16.

a. Direct EU legislation, such as an EU regulation or a Delegated Regulation, which applied directly to the UK as a result of the European Communities Act 1972[4] ("the ECA"); this is incorporated into UK law through section 3 of the EUWA.
b. EU obligations, principally those imposed by EU Directives, which were in part incorporated into UK law through the powers in section 2(2) of the ECA; this is incorporated into UK law as "EU-derived domestic legislation" in section 2 of the EUWA.
c. Rights, powers, liabilities, obligations, restrictions, remedies and procedures which stem from retained EU law, and which are saved by section 4 of the EUWA.

14. This approach provided stability and continuity in the immediate period after EU exit, but it was never intended to provide the optimal, long-term approach for UK regulation of financial services. It has led to a complicated patchwork of regulatory requirements across domestic primary and secondary legislation, retained EU law, and regulator rulebooks. It has also resulted in a complicated arrangement for amending regulatory standards, with some regulatory standards fixed and not amendable without primary legislation. It also means that the regulators are restricted in how they can pursue their statutory objectives through their rules, as they are not able to make changes to regulatory standards that are set out directly in retained EU law, except in very limited cases.

15. The government considers that the FSMA 2000 model remains the most appropriate way to regulate financial services in the UK. This Bill makes provisions that will return the UK to the FSMA 2000 model of financial services regulation, where the government and Parliament establish the framework and objectives for the regulators, and the regulators design the detailed rules that apply to firms. Delivering a comprehensive FSMA 2000 model of regulation requires the repeal of retained EU law relating to financial services. HM Treasury and the regulators therefore require additional powers, which are suitably tailored to the UK's position outside the EU, to reflect the unique nature of the UK's financial services sectors and replace retained EU law.

16. The government will commence the repeal of retained EU law in a way which facilitates a smooth transition to a comprehensive FSMA 2000 model. This means the government will not commence the repeal of individual parts of the Schedule unless the regulators have drafted and, where necessary, consulted on rules that are ready to be enforced, where it is appropriate, they are replaced.

[4] European Communities Act 1972 c.68.

Delegated Powers

PART 1 – REGULATORY FRAMEWORK

Revocation of EU law

Clause 1: Revocation of retained EU law relating to financial services and markets

- New provision to enable HM Treasury to exclude specific instruments from Part 5 of Schedule 1 to the Bill.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

17. Clause 1 revokes retained EU law relating to financial services, as specified in Schedule 1.

18. Part 1 of the Schedule captures retained direct principal EU legislation. This means EU Regulations which were made directly under the powers to make legislation granted to EU institutions in the various Treaties which establish the EU. This list is not exhaustive, but it contains all of the EU Regulations which are generally followed. It is possible that there are some EU Regulations which have been superseded which are not listed here.

19. Part 2 of the Schedule captures subordinate legislation made under primary legislation. That means domestic UK secondary legislation, which was made either entirely, or in part, for the purposes of implementing EU Directives or other obligations, or for related purposes.

20. This list is broadly composed of three types of SI:
    a. Statutory Instruments ("SIs") made under section 2(2) of the ECA, which were generally made under the ECA in order to implement EU obligations when the UK was part of the EU. It was common for EU Directives to be implemented in this way, and many EU regulations also required use of the powers in the ECA in order to be properly incorporated into UK law.
    b. SIs made partly under the ECA and other powers. These are included in this list as they include provisions that were made pursuant to powers conferred by the ECA for the purposes of implementing EU law.
    c. SIs made under the EUWA. These SIs were made in order to address deficiencies in retained EU law when the UK left the EU. While these SIs do not directly implement EU obligations, they will no longer function effectively when retained EU law is repealed as they generally make changes to instruments which will themselves be repealed, and so they are included this Schedule. There is also one SI made under the European Union (Withdrawal Agreement) Act 2020[5], which is included for the same reason.

[5] European Union (Withdrawal Agreement) Act 2020 c.1.

21. Part 3 of the Schedule captures EU tertiary legislation. This means instruments which are made under other EU instruments, rather than under EU Treaties. Examples include Delegated Regulations, Implementing Acts, and EU Decisions. Rather than list this category directly in the Schedule, Part 3 of Schedule 1 operates to capture tertiary legislation under EU Regulations related to financial services as captured by Part 1 of Schedule 1 and EU Directives listed in Part 3 of the Schedule 1.

22. Part 4 of Schedule 1 lists primary legislation which is repealed. This repeals Part 9D of FSMA 2000, which relates to rules which are defined in relation to the EU Capital Requirements Regulation[6]; and Chapter 2A of Part 9B of FSMA 2000, which governs Technical Standards, which are a form of EU tertiary legislation for which responsibility has already been transferred to the regulators, and so when they are repealed this Chapter of FSMA 2000 will no longer be needed. Finally, Part 4 repeals sections 137A(6) and 137G(6) of FSMA 2000; these sections set out that the PRA and the FCA cannot modify retained EU law, and so will not be needed when retained EU law has been repealed.

23. Part 5 of Schedule 1 acts as a "sweep up" provision by repealing all EU-derived legislation relating to financial services which is not directly listed or otherwise captured in Schedule 1 (except primary legislation). While the government has attempted to identify all relevant retained EU law in financial services, this has not always been possible. This is due to the length of time that the UK was in the EU, the fact that many EU laws have been updated frequently or superseded over time, and finally because some EU obligations were implemented entirely through domestic instruments. This approach is also necessary to capture instruments which will be made during the transitional period before retained EU law is repealed.

<u>Justification for the power</u>

24. Part 5 repeals all EU-derived legislation in financial services which is not listed or otherwise captured by Parts 1, 2, and 3 of Schedule 1. EU-derived legislation, and how this legislation "relates" to financial services, is provided in Part 5 of the Schedule 1.

25. As a result, Part 5 repeals:
    a. Any unlisted EU regulations relating to financial services;
    b. Any unlisted EU tertiary legislation relating to financial services;
    c. Any unlisted UK secondary legislation which implemented an EU Directive or other obligation related to financial services.
    d. Secondary legislation made under clause 3 of this Bill, which gives HM Treasury a power to amend retained EU law;
    e. Any unlisted or not yet made SIs made under the EUWA relating to financial services.

[6] Capital Requirements Regulation (EU) No. 575/2013.

26. The repeal of unlisted EU-derived legislation follows the definition of EU-derived legislation, it does not capture any domestic primary legislation. Regulator rules are also specifically excluded by clause 7(2)(b).

27. However, in order to ensure that Part 5 does not repeal important provisions which may, in part, implement EU obligations, and to avoid unintended consequences, clause 1(6) provides HM Treasury with a power to exclude subordinate legislation from this "sweep up" provision. This means that instruments, or parts of instruments, listed in regulations made pursuant to clause 1(5) will not be repealed by clause 1(1) of the Bill. The RAO is an example of an instrument which HM Treasury may wish to exclude from Part 5 of the Schedule in such a way, as it is an important part of the functioning of the domestic FSMA 2000 framework, and there are already sufficient existing powers to update it. Clause 1(5) is therefore included in order to avoid the unnecessary complexity of repealing and restating such instruments, and any others.

Justification for the procedure

28. The purpose of the power to exclude subordinate legislation from the "sweep up" provision is to maintain the current situation and therefore the proper functioning of the domestic FSMA 2000 framework. This will ensure key instruments that may be inadvertently captured are excluded. Regulations made under this power will be subject to the negative resolution procedure on the basis the regulations will maintain the status quo of provisions, and so exercising this power will not have any direct effect.

Clause 2 and Part 1 of Schedule 2: Amendments to the Markets in Financial Instruments Regulations

Paragraph 2 of Schedule 2: *Amendments to the Markets in Financial Instruments Regulation (MiFIR)*[7]

- Article 3 of MiFIR (power to make technical standards: pre-trade equity transparency requirements)

  Power conferred on: Financial Conduct Authority
  Power exercised by: technical standards
  Parliamentary Procedure: none

Context and Purpose

29. MiFIR requires regulated markets, multilateral trading facilities and systematic internalisers, to make certain information about a trade in an equity or equity-like instrument public before the trade happens. This is known as pre-trade transparency. Article 3 of MiFIR states that the FCA may specify certain characteristics of pre-trade transparency

[7] Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012.

requirements, including the range of bid and offer prices that those market operators and investment firms must make public. However, the power for the FCA to specify these characteristics is a power to make technical standards, which is currently set out in Article 4 of MiFIR.

30. The Bill substantially amends Article 4 to introduce a new rule-making power relating to waivers (see the entry for paragraph 3 of Schedule 2 below) and to delete the current power for the FCA to develop technical standards to specify the characteristics of pre-trade transparency requirements from Article 4. As the rule-making power cannot be used to specify further detail in respect of the pre-trade transparency requirements in Article 3 (which is being retained), to maintain the FCA's ability to specify characteristics of pre-trade transparency requirements, the Bill moves the power to make technical standards in this regard to Article 3. The Bill makes no changes to the substance of the power.

Justification for taking the power

31. It is necessary to move the power that is currently in Article 4 to retain it and ensure that the FCA can continue to specify the core pre-trade transparency requirements for equity and equity-like financial instruments. As noted above, it is not a new power: the only change is to its location within MiFIR.

Justification for the procedure

32. The Bill makes no change to the procedure for the exercise of the power.

Paragraph 3: Amendments to the Markets in Financial Instruments Regulation

- New Article 4 of MiFIR (power to make rules: waivers for equity instruments)

  Power conferred on: Financial Conduct Authority
  Power exercised by: rules made in accordance with Part 9A of FSMA 2000 (as provided in Article 50D of MiFIR)
  Parliamentary Procedure: none

Context and Purpose

33. As outlined above, MiFIR requires regulated markets, multilateral trading facilities, and systematic internalisers, to make certain information about a trade public before the trade happens in an equity or equity-like instrument, this is known as pre-trade transparency.

34. Pre-trade transparency helps ensure an efficient price discovery process, but in some instances it can impair liquidity. For example, market participants can use pre-trade information to increase their prices or create a shortage of shares, which can result in false indications of liquidity. This can have a negative impact on price formation. To mitigate against this, MiFIR specifies four situations in which the FCA may waive the pre-trade transparency requirements for equity and equity-like instrument. These comprise: the

reference price waiver, for systems that determine prices by reference to a price generated by another system- typically the primary market; the negotiated trade waiver, for transactions that are negotiated bilaterally but are reported on venues; the large-in-scale waiver, for orders considered large-in-scale against normal market size, and; the order management facilities waiver, for orders held in an order management facility of a trading venue pending disclosure.

35. Article 4(4) MiFIR requires the FCA to monitor the application of the waivers it grants and to publish an annual report on how they have been applied in practice, but the FCA has very little say over how the waivers work in practice because of the high level of detail that sits in legislation.

36. The Bill removes these waivers from Article 4 and, in their place, confers a power on the FCA to make rules specifying in which circumstances waivers are available and any conditions that are attached to their use. Calibrating waivers is complex and delegating rule-making powers in this area to the regulators will give them more space for expert judgement.

Justification for taking the power

37. HM Treasury consider the most appropriate way to ensure that the pre-trade transparency regime for equity and equity-like instruments is calibrated correctly and to mitigate against market risk is to delegate responsibility to the FCA, subject to the enhanced accountability framework that is part of this Bill. As the market regulator, the FCA is well placed to make evidence-based decisions about the circumstances in which waivers should apply. This is consistent with the approach taken by the Bill to implement the outcomes of the FRF Review, which is to revoke retained EU law and delegate responsibility for firm-facing requirements to the regulators.

Justification for the procedure

38. There is no parliamentary procedure. The FCA's general rule-making powers in Part 9A of FSMA 2000 do not have formal parliamentary oversight. These powers are specific rule-making powers, which replicate the procedures that apply to the FCA's general rule-making powers, and as such HM Treasury do not consider it appropriate to provide for formal parliamentary oversight. Instead, safeguards provided in Part 9A of FSMA 2000 will apply, in particular, sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA).

Paragraph 4 of Schedule 2: Amendments to the Markets in Financial Instruments Regulation

- Article 4a of MiFIR (power of direction: suspension of pre-trade equity transparency waivers)

Power conferred on: Financial Conduct Authority
Power exercised by: direction

Parliamentary Procedure: none

Context and Purpose

39. The FCA currently has the ability to withdraw waivers under Article 4(5) of MiFIR if it considers that the way in which they are being used is inconsistent with the original purpose of the waiver or if they are being used to circumvent requirements imposed by MiFIR. However, the Bill amends Article 4 of MiFIR and removes the main mechanism in MiFIR that was used to limit the volume of trading that makes use of waivers, known as the Double Volume Cap ("DVC"); as provided in Article 5 MiFIR.

40. The DVC limits the use of the reference price and negotiated trade waivers to 4% of all trading in an instrument at a single venue, and 8% across all venues. When these levels are reached the FCA is currently empowered to suspend the use of the waiver. The DVC was intended to encourage more 'lit' trading (i.e. trading that is subject to transparency requirements) and less 'dark' trading (i.e. trading that is not subject to those requirements). However, research on the impact of dark pools on the integrity and efficiency of markets suggests that the relationship between price formation, execution costs and dark trading is complex. It also suggests that the DVC is set at an arbitrary level and in some cases can negatively impact price formation, which is why the Government is deleting it.

41. In the absence of the DVC and in light of amendments to Article 4, this power of direction will allow the FCA to limit the amount of trading that can take place without pre-trade transparency if there is evidence that the volume of such trading is undermining the efficiency of the price formation process.

Justification for taking the power

42. HM Treasury consider the most appropriate way to ensure that the pre-trade transparency regime for equity and equity-like instruments is calibrated correctly and to mitigate against market risk is to delegate responsibility to the FCA, subject to the enhanced accountability framework that is part of this Bill. As the market regulator, the FCA is well placed to make evidence-based decisions about the circumstances in which waivers should apply and the circumstances in which their use should be suspended to protect the price-formation process.

43. The FCA's power to give directions to suspend waivers is made subject to a number of requirements to help ensure it is used appropriately and consistently with the FCA's statutory objectives. The FCA can only give a direction if it considers it necessary to advance its integrity objective under section 1D of FSMA 2000 and it must also have regard to its consumer protection and competition objectives under, respectively, sections 1C and 1E of FSMA 2000.

Justification for the procedure

44. The proposed power is not subject to parliamentary procedure. There is no formal parliamentary oversight over the regulators' powers to give directions under FSMA 2000.

HM Treasury consider that this is appropriate for the new power of direction at Article 4a of MiFIR as well.

45. However, paragraph 5 of Article 4a requires the FCA to consult HM Treasury before giving a direction, save in certain exceptional circumstances.

Paragraph 7 of Schedule 2: Amendments to the Markets in Financial Instruments Regulation

- New Articles 8 to 11 of MiFIR (powers to make rules: pre- and post-trade transparency requirements (including related waivers/deferrals) for market operators and investment firms operating a trading venue when trading bonds, structured finance products, emission allowances and derivatives. Powers to withdraw waivers/deferrals by notice. Powers to suspend requirements in rules by notice.)

  Powers conferred on: Financial Conduct Authority
  Powers exercised by: rules made in accordance with Part 9A of FSMA 2000 (as provided in Article 50D of MiFIR notice)
  Parliamentary Procedure: none

Context and Purpose

46. MiFIR requires market operators and investment firms operating a trading venue to make public current bid and offer prices and the depth of trading interests at those prices (as advertised through their systems) when trading bonds, structured finance products, emission allowances and derivatives. The publication of this information is known as pre-trade transparency. It also requires market operators and investment firms operating a trading venue to make public the price, volume and time of the transactions executed on the trading venues they operate. The publication of this information is known as post-trade transparency.

47. An EU-wide transparency regime for fixed income and derivatives markets was only introduced in 2018 and was modelled on the transparency regime for equity markets that existed pre-2018. Although it was amended to accommodate for the specific characteristics of non-equity markets, the way that it is calibrated does not go far enough in accounting for fundamental differences between equity markets and fixed income and derivatives markets, especially in view of the variety of different instruments that make up the latter. This has resulted in a number of bespoke illiquid instruments (where transparency does not always aid price formation and is therefore unnecessarily burdensome) falling within scope of the regime, while some liquid and standardised contracts (where more transparency would aid price formation) are not subject to transparency requirements.

48. The Bill removes the detail about pre- and post-trade transparency requirements from legislation and instead gives the FCA rule-making powers to determine which instruments and persons should be subject to pre- and post-trade transparency requirements for fixed income and derivatives instruments. These powers can only be used to aid price formation and allow for the fair evaluation of financial assets and should help to ensure that the correct instruments are in scope.

49. The FCA already has the power, under MiFIR, to waive the obligation for venues to comply with pre-trade transparency requirements and to withdraw a waiver if it observes that it is being used in a way that deviates from its original purpose or if it considers that the waiver is being used to circumvent MiFIR requirements. The FCA also has the power to authorise the deferred publication of the post-trade details about certain transactions based on the size or type of the transactions. However, these powers are limited by the conditions set out in MiFIR. To enable the FCA to develop a better-calibrated and agile regime, the Bill removes the detail about pre- and post-trade waivers and deferrals from the legislation and gives the FCA rule-making powers to determine what waivers and deferrals are to be available, and when and how they should be used.

50. This is consistent with the approach taken by the Bill to implement the outcomes of the FRF Review, which is to revoke retained EU law and delegate responsibility for firm-facing requirements to the expert regulators.

51. The FCA already has the powers, under MiFIR, to suspend the obligations imposed in respect of pre- and post-trade transparency where the liquidity of a class of relevant financial instruments falls below a threshold and is also currently empowered to suspend those obligations if it considers doing this necessary to advance its integrity objective under section 1D of FSMA 2000. However, these powers are limited by the conditions set out in MiFIR. To enable the FCA to develop a more agile regime, the Bill removes time-related and quantitative conditions on the FCA's powers to suspend but continues to subject the use of those powers to the requirement that the FCA must consider suspension to be necessary to advance its integrity objective. To exercise this power the FCA must publish a notice to inform the market about suspensions and to ensure that decisions are transparent. FCA notices are normally published on their website and are visible to the general public.

Justification for taking the power

52. HM Treasury consider the most appropriate way to ensure that the pre- and post-trade transparency regime for fixed income and derivative instruments is calibrated correctly and to mitigate against market risk is to delegate responsibility to the FCA, subject to the enhanced accountability framework that is part of this Bill. As the independent and expert market regulator, the FCA is well placed to make evidence-based decisions about the circumstances in which transparency requirements should or should not apply. In the case of suspension of requirements by notice, the FCA may only, as discussed above, exercise that power of suspension where it considers it necessary for advancing its integrity objective. The FCA is also required to have regard to its consumer protection and competition objectives, ensuring that the wider objectives imposed on the FCA by the FSMA 2000 framework are duly considered in the exercise of this specific power.

Justification for the procedure

53. There is no parliamentary procedure. The FCA's general rule-making powers in Part 9A of FSMA 2000 do not have formal parliamentary oversight. These powers are specific rule-

making powers, applying the procedures that apply to the FCA's general rule-making powers, and as such HM Treasury do not consider it appropriate to provide for formal parliamentary oversight. Safeguards provided in Part 9A of FSMA 2000 will apply to the rule-making powers, notably sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA).

54. In the case of suspension of requirements, exercise by notice without formal parliamentary oversight should allow the FCA to act quickly to address concerns about market integrity for a temporary period. Although there is no formal parliamentary oversight, the FCA is nevertheless required by Articles 9(5)(c) and 11(4)(c) of MiFIR to publish the notice in the manner best calculated to bring it to the attention of those likely to be affected by the suspension.

Paragraph 8 of Schedule 2: Amendments to the Markets in Financial Instruments Regulation

- Article 2 of MiFIR (power to make rules: determining when investment firms need to be recognised as systematic internalisers)

Power conferred on: Financial Conduct Authority
Power exercised by: rules made in accordance with Part 9A of FSMA 2000 (as provided in Article 50D of MiFIR)
Parliamentary Procedure: none

Context and Purpose

55. Systematic internalisers are defined in Article 2(1)(12) of MiFIR as investment firms which on an organised, frequent, systematic and substantial basis deal on own account when executing client orders outside of a regulated market, multilateral trading facility or an organised trading facility without operating a multilateral system. 'Dealing on own account' means that the systematic internalisers executes trades by trading against the systematic internalisers' own proprietary capital (though it does so on behalf of its clients).

56. The MiFID Org Regulation[8] currently specifies quantitative thresholds for determining which firms are systematic internalisers (i.e. what constitutes organised, frequent, systematic and substantial trading). These are calibrated at different levels for each asset class. To confirm whether they exceed the thresholds, investment firms are expected to perform calculations for each financial instrument they deal in on a quarterly basis covering the previous six-month period. To avoid having to undertake the quarterly calculations, which are costly and require a substantial amount of administrative work, the Government understands that a significant number of firms who operate as systematic internalisers have opted into the regime for all financial instruments they trade in. This suggests that the current definition is not working well.

[8] Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing MiFID of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive

57. The Bill removes these quantitative thresholds and instead gives the FCA the power to make rules to determine whether dealing is taking place on a basis that is organised, frequent, systematic and substantial for the purposes of setting the status of systematic internalisers. The FCA will be able to use this power to revert to qualitative criteria (similar to those which were in place prior to MiFIR), whereby whether an investment firm is a systematic internaliser might be determined by criteria indicating that it operates a platform for market making activity for a particular asset class and does not require complex calculations.

Justification for taking the power

58. HM Treasury believe that as the market regulator, the FCA is well placed to make evidence-based decisions about the circumstances when a firm should be classified as a systematic internaliser. This rule-making power will simplify the regime and reduce costs and burdens for firms. It will also help to future-proof the regime, as it will enable the FCA to update its approach in response to changes in markets.

59. This is in line with the broader approach taken in the Bill to repeal retained EU law and delegate responsibility for firm-facing requirements to the regulators.

Justification for the procedure

60. There is no parliamentary procedure. The FCA's general rule-making powers in Part 9A of FSMA 2000 do not have formal parliamentary oversight. These powers are specific rule-making powers, applying the procedures that apply to the FCA's general rule-making powers, and as such HM Treasury do not consider it appropriate to provide for formal parliamentary oversight. In particular, safeguards provided in Part 9A of FSMA 2000 will apply to this rule-making power, notably sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA).

Paragraphs 10 and 11 of Schedule 2: Amendments to the Markets in Financial Instruments Regulation

- New Article 18, Articles 18a to 18b and Article 21 of MiFIR (powers to make rules: pre- and post-trade transparency (including related waivers/deferrals) for, respectively, systematic internalisers and investment firms (including systematic internalisers), when trading bonds, structured finance products, emission allowances and derivatives. Powers to withdraw waivers/deferrals by notice. Powers to suspend requirements in rules by notice.)

  Power conferred on: Financial Conduct Authority
  Power exercised by:
  - *rules made in accordance with Part 9A of FSMA 2000 (as provided in Article 50D of MiFIR), or*
  - *Notice (the powers to set the requirements are exercised by rule, but the powers to suspend requirements and to withdraw waivers/deferrals are exercised by notice)*

Parliamentary Procedure: None

Context and Purpose

61. MiFIR requires systematic internalisers to make public current firm quotes when trading bonds, structured finance products, emission allowances and derivatives. They are also required to disclose information when they are asked for a quote by a client. This is known as pre-trade transparency. It also requires investment firms (including systematic internalisers) to make public the price, volume and time of the transactions once a trade has happened. This is known as post-trade transparency.

62. An EU-wide transparency regime for fixed income and derivatives markets was only introduced in 2018 and was modelled on the transparency regime for equity markets that existed pre-2018. Although it was modified to accommodate the specific characteristics of non-equity markets, the way that it is calibrated does not go far enough in accounting for fundamental differences between equity markets, and fixed income and derivatives markets, especially in view of wide variety of different instruments that make up the latter. This has resulted in a number of bespoke illiquid instruments (where transparency does not always aid price formation and is therefore unnecessarily burdensome) falling within scope of the regime, while some liquid and standardised contracts (where more transparency would aid price formation) are not subject to transparency requirements.

63. The Bill removes the detail about pre- and post-trade transparency requirements from legislation and instead gives the FCA rule-making powers to determine which instruments should be subject to pre- and post-trade transparency requirements for fixed income and derivatives instruments. These powers can only be used to aid price formation and allow for the fair evaluation of financial assets and should help to ensure that the correct instruments are in scope.

64. The FCA already has some powers, under MiFIR, to set the conditions for waivers from the obligation for systematic internalisers to comply with pre-trade transparency requirements. The FCA also has the power to authorise the deferred publication of the post-trade details about certain transactions based on the size or type of the transactions. However, these powers are limited by the conditions set out in MiFIR. To enable the FCA to develop a better-calibrated and agile regime, the Bill removes the detail about pre- and post-trade waivers and deferrals from legislation and gives the FCA rule-making powers to determine what the waivers and deferrals are to be available, and when and how they should be used.

65. The FCA already has the powers, under MiFIR, to suspend the obligations imposed in respect of post-trade transparency where the liquidity of a class of relevant financial instruments falls below a threshold and is also currently empowered to suspend those obligations if it considers doing this necessary to advance its integrity objective under section 1D of FSMA 2000. However, these powers are limited by the conditions set out in MiFIR. To enable the FCA to develop a more agile regime, the Bill removes time-related and quantitative conditions on the FCA's powers to suspend and extends those powers to pre-trade transparency but continues to subject the use of those powers to the requirement

that the FCA must consider suspension to be necessary to advance that integrity objective. To exercise this power the FCA must publish a notice to inform the market about suspensions and to ensure that decisions are transparent. FCA notices are normally published on their website and are visible to the general public.

Justification for taking the power

66. HM Treasury consider the most appropriate way to ensure that the pre- and post-trade transparency regime for fixed income and derivative instruments is calibrated correctly and to mitigate against market risk is to delegate responsibility the FCA, subject to the enhanced accountability framework that is part of this Bill. As the independent and expert market regulator, the FCA is well placed to make evidence-based decisions about the circumstances in which transparency should apply. In the case of suspension of requirements by notice, the FCA may only, as discussed above, exercise that power of suspension where it considers it necessary for advancing its integrity objective. The FCA is also required to have regard to its consumer protection and competition objectives, ensuring that the wider objectives imposed on the FCA by the FSMA 2000 framework are duly considered in the exercise of this specific power. This is consistent with the approach taken by the Bill to implement the outcomes of the FRF Review, which is to revoke retained EU law and delegate responsibility for firm-facing requirements to the expert regulators.

Justification for the procedure

67. There is no parliamentary procedure. The FCA's general rule-making powers in Part 9A of FSMA 2000 do not have formal parliamentary oversight. These powers are specific rule-making powers, applying the procedures that apply to the FCA's general rule-making powers, and as such HM Treasury do not consider it appropriate to provide for formal parliamentary oversight. Safeguards provided in Part 9A of FSMA 2000 will apply to the rule-making powers, notably sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA).

68. In the case of suspension of requirements, exercise by notice without formal parliamentary oversight should allow the FCA to act quickly to address concerns about market integrity for a temporary period. Although there is no formal parliamentary oversight, the FCA is nevertheless required by Articles 18(5)(c) and 21(9)(c) to publish the notice in the manner best calculated to bring it to the attention of those likely to be affected by the suspension.

Paragraph 17 of Schedule 2: Amendments to the Markets in Financial Instruments Regulation

- Article 28a of MiFIR (power of direction: suspension or modification of the DTO)

Power conferred on: Financial Conduct Authority
Power exercised by: direction
Parliamentary Procedure: none

Context and Purpose

69. This paragraph to the Schedule gives the FCA the power to suspend or modify the derivatives trading obligation ("DTO"); as provided in Article 28 MiFIR if necessary to prevent or mitigate disruption to financial markets and if it advances one or more of its operational objectives.

70. The DTO requires financial counterparties and some non-financial counterparties (counterparties being entities which take up opposite sides in a financial transaction) to trade certain classes of derivatives on UK authorised trading venues, or overseas trading venues that have been recognised as equivalent for the purposes of the DTO.

71. In December 2020, the FCA announced that it would use its Temporary Transitional Power (TTP)[9] to modify the application of the DTO. The relief under the TTP applies to UK firms, EU firms using the UK's temporary permissions regime and branches of overseas firms in the UK. These firms can use EU venues, irrespective of the wording of Article 28 MiFIR, when trading with an EU client who does not have access to a venue to which both the UK and EU have granted equivalence to. The FCA's use of their TTP has limited disruption for market participants and limited liquidity fragmentation that would have otherwise arisen from conflicting UK and EU DTOs after the end of the transition period.

Justification for taking the power

72. HM Treasury consider that the FCA's use of the TTP has demonstrated that granting the FCA the power – within certain boundaries – to suspend or modify the DTO can improve market functioning and resilience. This power will therefore help protect UK markets in the event of an unexpected change in global markets or wider market disruption. Safeguards are in place to ensure that the power is used appropriately. Article 28a(1) of MiFIR provides that the FCA may use it only where the FCA considers it necessary for preventing or mitigating disruption to financial markets. Moreover, the FCA may only exercise the power where it considers that it advances one or more of its operational objectives referred to in section 1B(3) of FSMA 2000. In giving a direction the FCA must have regard to the competitiveness and growth objective in section 1EB of FSMA 2000.

Justification for the procedure

73. The power is not subject to parliamentary procedure. There is no formal parliamentary oversight over regulators' powers to give directions. However, the FCA must prepare a statement explaining the purpose of the direction where it gives a direction under Article 28a (Article 28a(6)(a)). Article 28a(7)(b) requires the FCA to lay a copy of the direction and statement before Parliament. Article 28a(5) also requires the FCA to obtain HM Treasury's consent to give a direction. In addition, the FCA must consult the Bank of England, and in some cases the PRA, before giving a direction.

Paragraph 18 of Schedule 2: Amendments to the Markets in Financial Instruments Regulation

- New Article 31 of MiFIR (power to make rules: risk reduction services)

[9] Conferred by regulations 197-205 of FSMA 2000 (Amendment) (EU Exit) Regulations 2019

Power conferred on: Financial Conduct Authority
Power exercised by: rules made in accordance with Part 9A of FSMA 2000 (as provided in Article 50D of MiFIR)
Parliamentary Procedure: none

Context and Purpose

74. The Bill gives the FCA a rule-making power to disapply certain obligations otherwise triggered by transactions carried out as part of a risk reduction service, by reference to those transactions and services, or to the persons providing those services.

75. Post-trade risk reduction services are types of non-price forming trades that are made to reduce risks in derivatives portfolios without changing the market risk of those portfolios. For example, portfolio compression is where counterparties simplify derivative portfolios by terminating derivative contracts and replacing them with other derivative contract(s) of equivalent net value (but lower absolute value) to reduce exposure and lower costs.

76. Currently, under Article 31 of MiFIR, transactions resulting from portfolio compression are exempt from complying with the DTO; the best execution requirement (which obliges firms carrying out investment business to obtain the best possible deal for clients) and transparency obligations. Firms conducting the compression are also exempt from the requirement to operate as multilateral trading facilities or organised trading facilities, but only when providing portfolio compression services.

77. Other types of post-trade risk reduction services are not covered by the MiFIR exemption. Empowering the FCA to extend the exemption to other post trade risk reduction services can help to reduce systemic risk by helping firms to make use of those services by reducing risks in their positions.

Justification for taking the power

78. Exempting more post trade risk reduction services from the DTO, and the other obligations that portfolio compression trades are currently exempt from, could encourage their use and help to reduce systemic risk. HM Treasury consider the most appropriate way to ensure that correct services fall in scope of this regime is to delegate responsibility to the FCA, subject to the enhanced accountability framework that is part of this Bill. As the independent and expert market regulator, the FCA is well placed to make evidence-based decisions about the circumstances in which certain services should qualify as helping to mitigate risk.

79. This is consistent with the approach taken by the Bill to implement the outcomes of the FRF Review, which is to revoke retained EU law and delegate responsibility for firm-facing requirements to the regulators.

Justification for the procedure

80. There is no parliamentary procedure. The FCA's general rule-making powers in Part 9A of FSMA 2000 do not have formal parliamentary oversight. These powers are specific rule-making powers, applying the procedures that apply to the FCA's general rule-making powers, and as such HM Treasury do not consider it appropriate to provide for formal parliamentary oversight. In particular, safeguards provided in Part 9A of FSMA 2000 will apply to this rule-making power, notably sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA).

Clause 2 and Part 2 of Schedule 2: Amendments to the European Markets Infrastructure Regulation

Paragraph 29 of Schedule 2: Amendments to the European Market Infrastructure Regulation ("EMIR")

- Article 6b of EMIR (power to make rules: risk reduction services)

  Power conferred on: Bank of England
  Power exercised by: rules made in accordance with Part 9A of FSMA 2000 (as provided in new Article 84c of EMIR)
  Parliamentary Procedure: none

Context and Purpose

81. Paragraph 29 of Schedule 2 inserts new Article 6b into EMIR[10] to give the Bank of England a rule-making power to disapply the clearing obligation imposed by Article 4 of EMIR in respect of transactions in OTC derivatives carried out as part of a risk reduction service, by reference to those transactions and services, or to the persons providing those services.

82. As noted above, post-trade risk reduction services are types of non-price forming trades that are made to reduce risk in derivatives portfolios without changing the market risk of those portfolios.

83. Currently, the EMIR clearing obligation applies to transactions in OTC derivatives carried out as part of risk reduction services in the same way as other OTC derivatives transactions.

84. Empowering the Bank of England to provide for an exemption from the clearing obligation for post-trade risk reduction services can help to reduce systemic risk by helping to reduce risk in firms' derivatives positions.

Justification for taking the power

85. Exempting post-trade risk reduction services from the clearing obligation could encourage their use and help to reduce systemic risk. HM Treasury consider the most appropriate way

[10] Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories

to ensure that correct services fall in scope of this exemption is to delegate responsibility to the Bank of England. As the independent and expert regulator for these purposes, the Bank of England is well placed to make evidence-based decisions about the circumstances in which certain services should qualify as helping to mitigate risk.

86. This is consistent with the approach taken by the Bill to implement the outcomes of the FRF Review, which is to revoke retained EU law and delegate responsibility for firm-facing requirements to the regulators.

Justification for the procedure

87. There is no parliamentary procedure. The Bank of England's existing FSMA 2000 rule-making powers, to which Part 9A of FSMA 2000 applies with modifications (by virtue of paragraph 10 of Schedule 17A to FSMA 2000), do not have formal parliamentary oversight. These rule-making powers apply Part 9A of FSMA 2000 with similar modifications, and as such HM Treasury do not consider it appropriate to provide for formal parliamentary oversight. In particular, safeguards provided in Part 9A of FSMA 2000 will apply to this rule-making power, notably sections 138C (evidential provisions), 138F (notification of rules) and 138J (consultation by the PRA).

Clause 2 and Part 4 of Schedule 2: Amendments to FSMA 2000 (Markets in Financial Instruments) Regulations 2017

Paragraph 45 of Schedule 2: Amendments to FSMA 2000 (Markets in Financial Instruments) Regulations 2017

- Regulation 15A of FSMA 2000 (Markets in Financial Instruments) Regulations 2017 (power to make rules: position limits and position management controls)

  Power conferred on: Financial Conduct Authority
  Power exercised by: rules made in accordance with Part 9A of FSMA 2000 (as provided in regulation 15A of the Regulations), and paragraph 3 of Schedule 1 to the Regulations
  Parliamentary Procedure: none

Context and Purpose

88. Paragraph 45 of Schedule 2 gives the FCA a rule-making power to require the operators of trading venues to set and enforce position limits and position management controls in respect of specific commodity derivative contracts, as well as classes of commodity derivatives.

89. Position limits were introduced in response to the G20's 2011 commitment to give market regulators effective intervention powers to mitigate against market abuse in commodity

derivatives markets.[11] They restrict the size of a position that a person can hold in a commodity derivative that is traded on a trading venue, or in economically equivalent over-the-counter contracts. They are complemented by position management controls, which operators of trading venues use to help manage and monitor position limits on their venues to ensure that markets function with integrity.

90. The FCA currently has a duty, under regulation 16, to impose limits on the maximum size of a net position that a person can hold in a commodity derivative traded on a UK trading venue. However, not all commodity derivatives are naturally susceptible to high volatility and market abuse – for example, there are markets for niche or illiquid commodities, with few users and low levels of systemic risk. Applying position limits to these types of contracts unnecessarily prevents liquidity from developing, to the detriment of all market participants. The Bill removes the obligation on the FCA to impose limits on all commodity derivatives traded on UK venues and instead gives the FCA a power to impose position limits where necessary.

- Regulation 15A of FSMA 2000 (Markets in Financial Instruments) Regulations 2017 (power to make rules: position limits and position management controls)

  Power conferred on: Financial Conduct Authority
  Power exercised by: rules made in accordance with Part 9A of FSMA 2000 (as provided in regulation 15A of the Regulations), and paragraph 3 of Schedule 1 to the Regulations
  Parliamentary Procedure: none

Context and Purpose

91. Paragraph 45 of Schedule 2 gives the FCA a rule-making power to require the operators of trading venues to set and enforce position limits and position management controls in respect of specific commodity derivative contracts, as well as classes of commodity derivatives.

92. Position limits were introduced in response to the G20's 2011 commitment to give market regulators effective intervention powers to mitigate against market abuse in commodity derivatives markets.[12] They restrict the size of a position that a person can hold in a commodity derivative that is traded on a trading venue, or in economically equivalent over-the-counter contracts. They are complemented by position management controls, which operators of trading venues use to help manage and monitor position limits on their venues to ensure that markets function with integrity.

93. The FCA currently has a duty, under regulation 16 of FSMA 2000 (Markets in Financial Instruments) Regulations 2017, to impose limits on the maximum size of a net position that a person can hold in a commodity derivative traded on a UK trading venue. However, not

[11]https://www.oecd.org/g20/summits/cannes/Cannes%20Leaders%20Communiqu%C3%A9%204%20%20November%202011.pdf
[12]https://www.oecd.org/g20/summits/cannes/Cannes%20Leaders%20Communiqu%C3%A9%204%20%20November%202011.pdf

all commodity derivatives are naturally susceptible to high volatility and market abuse – for example, there are markets for niche or illiquid commodities, with few users and low levels of systemic risk. Applying position limits to these types of contracts unnecessarily prevents liquidity from developing, to the detriment of all market participants. The Bill removes the obligation on the FCA to impose limits on all commodity derivatives traded on UK venues and instead gives the FCA a power to impose position limits where necessary.

94. The intention behind giving the FCA a general rule-making power to require operators of venues to set and enforce position limits is to transfer the setting of position controls from the FCA to trading venues. To mitigate against potential financial stability risks, the power will allow the FCA to identify specific contracts to which trading venues should apply limits. The FCA will also have the necessary powers to establish a framework to support trading venues in setting position limits. This will ensure that there is a consistent approach across the market.

Justification for taking the power

95. This power will enable the FCA to transfer responsibility for position limits and controls to trading venues, subject to an overarching framework set out in FCA rules, whilst ensuring that the FCA has the necessary powers to intervene and set positions directly if it considers they are necessary or expedient to advance one or more of its operational objectives. The FCA must also have regard to its competitiveness and growth objective in section 1EB of FSMA 2000. This approach will strike the right balance between achieving a base level of consistency which ensures the regime continues to apply to contracts that genuinely pose a risk to market integrity, while allowing exchanges to use their visibility of positions to enforce limits which are appropriately tailored to market dynamics. It will mean that strict, universal limits which arbitrarily restrict market activity will be avoided and allow liquidity to develop more effectively in commodity derivatives markets.

Justification for the procedure

96. There is no parliamentary procedure. The FCA's general rule-making powers in Part 9A of FSMA 2000 do not have formal parliamentary oversight. These powers are specific rule-making powers, applying the procedures that apply to the FCA's general rule-making powers, and as such HM Treasury do not consider it appropriate to provide for formal parliamentary oversight. In particular, safeguards provided in Part 9A of FSMA 2000 will apply to this rule-making power, notably, via regulation 15A(7)(b), sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA) of FSMA 2000.

Paragraph 46 of Schedule 2: Amendments to FSMA 2000 (Markets in Financial Instruments) Regulations 2017

- Regulation 16 of FSMA 2000 (Markets in Financial Instruments) Regulations 2017 (power of direction: position limits)

Power conferred on: Financial Conduct Authority
Power exercised by: direction
Parliamentary Procedure: none

Context and Purpose

97. The context for this power is the same as for paragraph 45 of Schedule 2 (set out at paragraphs 88-90 above).

98. This power complements the power that is granted to the FCA as part of paragraph 45 of Schedule 2. It gives the FCA the ability to set position limits on contracts that are in scope of the rules developed under paragraph 45 (the FCA's rulemaking power over trading venues). However, whereas the rules that are made under the power in paragraph 45 will only apply to operators of trading venues, directions made using this power will continue to apply to the holders of commodity derivatives themselves. This is necessary to ensure that the FCA can apply position limits in emergencies where trading venues are not setting appropriate limits themselves.

Justification for taking the power

99. Although the power that is being granted to the FCA under paragraph 45 of Schedule 2 (outlined above) will enable position limits and controls to be set by trading venues, it is possible that there may be instances where the FCA needs to impose limits directly. For example, where a trading venue is not setting appropriate limits itself. This power ensures that in these instances the FCA will be able to apply position limits to persons holding positions in commodity derivative contracts traded on a UK trading venue, where necessary. This is important to ensure that the UK continues to meet its G20 commitment. To ensure that the power is exercised consistently with its statutory objectives, the FCA may only give a direction under this power if it considers that it is necessary to do so to advance one of its operational objectives referred to in section 1B(3) of FSMA 2000.

Justification for the procedure

100. There is no parliamentary procedure. There is no formal parliamentary oversight over regulators' powers to give directions. Exercise by direction without formal parliamentary oversight should allow the FCA to act quickly to address disruption or problems in commodity derivatives markets for a temporary period. Although there is no formal parliamentary procedure, the FCA must (as it is required to do under its existing power to set position limits) publish such position limits set by direction in a manner the FCA considers appropriate.

Clause 2 and Part 3 of Schedule 2: Amendments to the EU Securitisation Regulation 2017

- New provision to enable HM Treasury to make regulations designating a country or territory as equivalent to the UK in relation to specified kinds of securitisations and to specify the due diligence that must be conducted by institutional investors.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

101. Securitisation is the process of pooling various financial exposures (such as mortgages, automobile loans, or consumer loans) to create a financial instrument that can be marketed to investors. This allows lenders (such as banks) to transfer the risks of loans or assets to other banks or investors (such as insurance firms or asset managers). This can help free up lenders' balance sheets to allow for further lending to the economy. Securitisation is an important part of well-functioning markets and a useful source of finance for UK businesses.

102. Under the UK Securitisation Regulation, certain securitisations can be designated as Simple, Transparent and Standardised ("STS"). Such STS securitisations are designed to make it easier for investors to understand and assess the risks of a securitisation investment by excluding more complex features. The UK STS framework is in line with international standards for Simple, Transparent, and Comparable ("STC") securitisation, set by the Basel Committee on Banking Supervision ("BCBS") and International Organisation of Securities Commissions ("IOSCO").

103. The government supports the development of sound securitisation markets, including the growth of the STS securitisation market. To support HM Treasury's legally mandated review of the UK Securitisation Regulation, HM Treasury issued a call for evidence to gather views on the desirability of an STS equivalence regime – a way to recognise non-UK STS securitisations from jurisdictions with STS frameworks that are equivalent to the UK's. Industry respondents to the call for evidence were supportive of HM Treasury creating such a regime to provide more choice for UK investors.

104. This schedule inserts a new Article 28A into Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012 ("the Securitisation Regulation").

105. Paragraph 1 of new Article 28A of the Securitisation Regulation confers on HM Treasury a power to make regulations designating a country or territory as equivalent to the UK in relation to specified kinds of securitisations. Specified securitisations issued in that country or territory will be considered equivalent to securitisations that are designated as STS in the UK. This should provide UK investors with better choice, including a wider range of securitisations eligible for preferential capital treatment for UK firms subject to the Capital Requirements Regulation ("CRR")[13] and Solvency II.

[13] Capital Requirements Regulation (EU) No.575/2013.

106. It also confers a power on HM Treasury to specify the due diligence that institutional investors must conduct before they can hold positions in such securitisations from a designated country or territory. This ensures that the due diligence requirements are set with reference to the particular regulatory framework of that country or territory.

Justification for taking the power

107. This power is being taken to allow HM Treasury to designate, over time, different countries or territories in relation to STS equivalent non-UK securitisations. This is in line with the government's approach to other overseas recognition regimes, such as provisions providing for recognition of certain overseas collective investment schemes and money market funds from approved countries, in sections 22 to 27 of the Financial Services Act 2021.[14]

108. Under the current legislative framework, securitisations issued by originators or sponsors established outside the UK (or the EU, until 31 December 2024) cannot be recognised as STS in the UK. This Bill amends the Securitisation Regulation to allow for specified STS equivalent non-UK securitisations to be recognised in the UK, if they are issued by originators or sponsors established in a country or territory designated by HM Treasury under new Article 28A(1) of the Securitisation Regulation.

109. Article 28A(2) and (3) set out the standard for equivalence, whereby HM Treasury may exercise the power in Article 28(1) only if it is satisfied that the law and practice applying in the country or territory, in relation to securitisations of the descriptions specified, has equivalent effect (taken as a whole) to the requirements for STS securitisations in the Securitisation Regulation and the Securitisation Regulations 2018.[15]

110. Article 28A(4) sets out that HM Treasury must have regard to whether effective cooperation arrangements have been established between the FCA and, where relevant, the PRA and the competent authorities of the country or territory in question, as well as any other matter it considers relevant.

111. Article 28A(5) and (6) set out that HM Treasury may request the FCA to prepare a report on the law and practice of the country or territory in question, when it is considering whether to make, vary or revoke a designation. This request must be made in writing. If HM Treasury asks for a report, the FCA must consult the PRA and provide the report within a reasonable period.

112. Article 28A(7) allows HM Treasury, when exercising the power, to specify the matters that an institutional investor needs to consider when carrying out due diligence assessments required by Article 5, prior to holding a position in an STS-equivalent non-UK securitisation. HM Treasury may also specify the extent to which the person may rely on the matters specified.

[14] Financial Services Act 2021 c.22.
[15] S.I. 2018/2188.

113. This is necessary so that HM Treasury can specify the requirements to be considered by institutional investors, as these requirements exist in the specific country or territory that is being designated. These requirements can only be specified once the country or territory being designated is known. Specificity is important so that institutional investors are clear about exactly what is required, for example to avoid engaging in disproportionately burdensome or insufficiently detailed assessments. It will also avoid an 'unlevel playing field' in terms of due diligence requirements compared to applicable requirements for UK STS securitisations.

Justification for the procedure

114. It is considered appropriate that the regulations made under Article 28A(1) are subject to the negative procedure, given the safeguards set out in Article 28A(2) and 28(3). In addition, HM Treasury would ordinarily consider its exercise of the power having received a detailed report submitted by the FCA.

Clause 3: Removal of retained EU law: power to make further transitional amendments

- New provision to enable HM Treasury to make further transitional arrangements.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure:

- *negative procedure if amending EU tertiary legislation, or domestic legislation made under negative procedure;*
- *affirmative procedure for amendments to all other types of legislation.*

Context and Purpose

115. Clause 1 revokes retained EU law relating to financial services, in the form of direct principal EU legislation, subordinate legislation, EU tertiary legislation, and a limited amount of primary legislation, as specified in Schedule 1.

116. Until the relevant retained EU law is revoked, the regulators will be restricted in how they are able to update regulatory standards, because they are not able to amend those requirements in retained EU law.

117. The government's intention is to replace retained EU law relating to financial services with the appropriate framework and requirements in domestic legislation. Part 1, Chapter 1 of the Bill contains provisions to enable this, including by establishing the appropriate framework to allow provisions in retained EU law to be replaced as appropriate.

118. This includes undertaking a programme of work that will provide for an orderly transition to these new arrangements. It will work closely with the financial services regulators to ensure that the appropriate new provisions are in place (using other powers in the Bill, in some cases) and commence the revocation of the instruments listed in Schedule 1 when the appropriate arrangements have been made to replace the provisions in those instruments, where appropriate. This process is expected to take a number of years.

119. During this period, it is likely that some elements or specific provisions within retained EU law will become ineffective or out-of-date before the repeal is commenced. Financial services regulations need to be updated regularly to take account of new developments in financial markets, or to address emerging risks and opportunities.

Justification for taking the power

120. Without such a power, amendments to retained EU law during the transitional period, where a piece of law has been repealed but that repeal has not yet been commenced, would generally require primary legislation. The government does not consider that it is appropriate to continue to ask Parliament to pass primary legislation in order to update legislation which Parliament has agreed to repeal by passing this Bill.

121. Furthermore, this is very likely to materialise in practice. The Financial Services Act 2021 made several amendments to retained EU law, often very minor one-clause amendments; and a number of other amendments to retained EU law are made through this Bill itself. Due to the vast amount of retained EU law, and the speed at which financial markets evolve, without this clause Parliament will regularly be required to pass primary legislation to continue to maintain retained EU law before it can be repealed.

122. Clause 3 therefore provides HM Treasury with a power to make targeted modifications to retained EU law during this transitional period. The power is constrained by subsection (2) which permits HM Treasury to exercise the power as HM Treasury considers necessary or desirable for one or more of the purposes stated. In addition, in modifying the legislation for the purposes set out in subsection (2), HM Treasury may by regulations also confer powers on a regulator, including the power to make rules or other instruments. The listed purposes closely relate to the regulators' statutory objectives, reflecting the fact that the government's intention for this power is to use it to make important updates to retained EU law to address the fact that, until the revocation of that law takes effect, the regulators will be restricted in their ability to pursue their objectives. These objectives reflect the most important public policy priorities for the UK's financial services sector and will allow important updates to be made to this legislation before its revocation takes effect.

123. The power to amend retained EU law may also be used to make supplementary, incidental, consequential, transitional, transitory or savings provisions for making retained EU law clearer, or delaying or extending EU provisions which are not yet in force. The power cannot be used to modify technical standards, as regulators already have powers to modify technical standards.

Justification for the procedure

124. EU tertiary legislation contains many technical and detailed provisions which, under a FSMA 2000 model of legislation would not have been in primary or secondary legislation, but in the regulators' rules. The matters dealt with in EU tertiary legislation are generally constrained by the principal EU legislation that it was made under. Accordingly, it is considered appropriate to use the negative procedure where the power is being exercised in

relation to EU tertiary legislation. In relation to amendments to domestic legislation made under the negative procedure, for example under section 8 of the EUWA or section 2(2) of the ECA, these may be technical in nature, and Parliament has previously agreed that the negative procedure is appropriate. And so, it is likely that for these instruments it will be a small and technical modification.

125. Amendments to domestic legislation made under the affirmative procedure, or to EU principal regulations, may have significant policy implications and were originally made with the prior consent of Parliament. It is therefore appropriate that amendments to those forms of legislation made using this power should be subject to full Parliamentary scrutiny through the affirmative procedure.

Clause 4: Power to restate and modify saved legislation

- New provision to enable HM Treasury to restate and modify saved legislation.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure:

- *negative procedure if restating EU tertiary legislation, or domestic legislation made under the negative procedure unless restated into primary legislation;*
- *negative procedure if restating EU principal regulations or domestic legislation made under the affirmative procedure without modification unless restated into primary legislation; or*
- *affirmative procedure when restating EU principal regulations or domestic legislation made under the affirmative procedure.*

Context and Purpose

126. Clause 4(1) provides HM Treasury with the power to restate retained EU law. This power is designed to allow HM Treasury to restate into domestic law those elements of retained EU law which should not be moved to the regulators' rulebooks. For example, aspects of retained EU law may confer powers on the regulators or might impose limitations on how regulators' powers should be exercised. It would not be appropriate, or logical, for these provisions to be located in regulators' rulebooks, but they might be required in order to ensure the effective operation of financial services regulation.

127. Clause 4(3) enables HM Treasury to, when restating retained EU law into domestic legislation, restate it in such a manner that the effect is modified. This is governed by the same set of 'purposes' as in clause 3(2).

128. Pursuant to the FSMA 2000 model, these matters would normally either be placed into primary or secondary legislation. Accordingly, HM Treasury will be able to use the power in clause 4(1) to restate these elements of retained EU law through either amending existing primary or secondary legislation or by making new legislation. The power conferred by clause 4(1) also includes, by reference, the power provided in clause 3(4) to confer powers

on HM Treasury or a regulator, including power to authorise the regulators to make rules or issue other instruments.

129. The power in clause 4(1) is not available to restate matters listed in clause 4(7) i.e. UK technical standards or EU tertiary legislation of the kind mentioned in sections 138P(2)(a) of FSMA 2000 or EU tertiary legislation of the kind mentioned in section 138P(2)(b) of FSMA 2000, i.e. onshored EU technical standards.

130. Clause 4(2) allows HM Treasury, when it exercises the powers conferred by clause 4(1), to make modifications to retained EU law. The power of restatement can only be exercised as HM Treasury considers necessary or desirable to (i) clarify the law, or make it more accessible, or (ii) for any of the purposes listed in clause 3(2).

131. Under clause 4(4) HM Treasury will have an ongoing power to modify any element of retained EU law that has been restated pursuant to clause 4(1). This continuing power can only be exercised for the purposes set out in clause 3(2). This will ensure that the legislation can remain up to date in light of developments in financial markets.

Justification for taking the power

132. This power is essential to enable the repeal of retained EU law in clause 1(1). Retained EU law contains a number of key elements which cannot be safely repealed, and often the effect of repealing retained EU law would remove important definitions which determine which activities are subject to regulation at all. This power enables HM Treasury to restate such provisions into domestic legislation.

133. As is clear from Schedule 1, there are hundreds of pieces of retained EU law in financial services. The government has not attempted to review each one to determine what elements must remain in legislation in order for the rest to be safely repealed. Therefore, it is vital that there is a power to restate these provisions at the point that the relevant piece of retained EU law is repealed.

134. The power enables HM Treasury to restate retained EU law with modifications. Without this provision, the UK would remain restricted to replicating the effect of retained EU law, even though the UK is no longer part of the EU. Instead, through restating retained EU law with modifications, the government will be able to adapt important provisions to suit the UK.

Justification for the procedure

135. Where the power is used to restate legislation without modification the negative procedure is considered appropriate unless it has the effect of altering primary legislation, in which case the affirmative procedure is applied. This is because restating a provision without modification would simply have the effect of retaining the status quo and so the negative procedure is appropriate. However, if a provision is restated into primary legislation, this will have the effect of that provision becoming domestic primary

legislation, and so it is appropriate to use the affirmative procedure in this instance, even if that would simply maintain the status quo.

136. Where restatement also has the effect of modifying retained EU law, the negative procedure is applied where this modifies EU tertiary legislation or domestic legislation made under the domestic procedure. This is because EU tertiary legislation contains many technical and detailed provisions which, under a FSMA 2000 model of legislation would not have been in primary or secondary legislation, but in the regulators' rules. The matters dealt with in EU tertiary legislation are generally constrained by the principal EU legislation that it was made under. Accordingly, it is considered appropriate to use the negative procedure where the power is being exercised in relation to EU tertiary legislation. In relation to amendments to domestic legislation made under the negative procedure, for example under section 8 of the EUWA or section 2(2) of the ECA, these may be technical in nature, and Parliament has previously agreed that the negative procedure is appropriate. While this power will have the effect of modifying the status quo, it is likely that for these instruments it will be a small and technical modification.

137. In the case of modifications to EU principal regulations or domestic legislation previously made under the affirmative procedure, the affirmative procedure is considered appropriate and should be subject to full Parliamentary scrutiny.

Clause 5: Power to replace references to EU directives

- New provision to enable HM Treasury to replace references to EU directives

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure when power used in relation to primary legislation, otherwise negative

Context and Purpose

138. Clause 5 confers on HM Treasury the power to modify legislation to remove references to EU directives in domestic legislation which were implemented into the UK financial services legislative framework during membership of the EU. Where HM Treasury exercises this power, there is no requirement that it replaces the removed reference with a new reference.

139. Clause 1(1) repeals retained EU law listed in Schedule 1 to the Bill. Part 3 of that Schedule captures any provision made under the EU directives related to financial services listed in that Part. This includes UK legislation made for the purpose of implementing these EU directives. However, although EU directives no longer bind the UK, there is no general power to remove references to them in legislation. Therefore, the power in this clause permits HM Treasury to replace or remove reference to them. It can be exercised for the purpose of making the law clearer or more accessible or for any of the purposes in clause 3(2).

Justification for the power

140. There are a number of references to EU directives in domestic legislation, and so this power enables HM Treasury to modify legislation in order to replace or remove references to them, as this cannot be done through the power to repeal under clause 1. The power in this clause is needed in order to remove the residual references to EU directives.

Justification for the procedure

141. Where regulations under this power modify primary legislation, then the affirmative procedure must be used; in all other cases the negative procedure is applies. While this power can modify legislation for the same set of purposes as clause 3(2), it is naturally a narrower power than clause 4, as it can only operate on references to EU directives, and so it is not necessary to use the affirmative procedure except where it amends primary legislation.

Clause 6: Restatement in rules: exemption from consultation requirements etc

- New provision to enable HM Treasury to make regulations that provide for a relevant requirement does not apply to the making of rules by a regulator.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure

Context and Purpose

142. When retained EU law is repealed, the FCA, the PRA, the PSR and the Bank ("the regulators") will, in many cases replace the firm-facing regulatory requirements contained in retained EU law with appropriate rules. HM Treasury expects this to take a number of years and a significant programme of work for the financial services regulators.

143. When deciding what rules to make, the FCA and the PRA will need to follow their usual process for making rules including considering any additional "have regards" specified by HM Treasury.

144. As part of the usual rule-making processes for the FCA and the PRA sections 138I and 138J of FSMA 2000 require the regulators to consult publicly on rule changes, and to conduct a cost benefit analysis ("CBA") on the impact the rules will have. Similarly, as part of the PSR's processes for giving general directions or imposing requirements, subsections (2) and (3) of section 104 of the Financial Services (Banking Reform) Act 2013[16] ("FSBRA") requires the PSR to consult publicly and to conduct a CBA. And for the Bank, such rule making processes apply to the Bank under paragraph 10 of Schedule 17A to FSMA which applies section 138J with modification.

[16] Financial Services (Banking Reform) Act 2013 c.33.

145. These requirements are referred to as a “relevant requirement” and are specified in subsection (3) of this clause.

146. In some areas, the regulators may conclude that the most appropriate course of action is to replace the retained EU law with rules that are materially the same, with rules that do make material changes but the effect is to reduce a regulatory burden or to just revoke the rules without explaining them

147. Clause 6 operates to exclude a regulator from a relevant requirement when making, amending or revoking rules in the following circumstances:
   a. the regulators make new rules that reproduce a specified retained EU law provision without any changes that are material, or with changes that are material, but the effect is to reduce a regulatory burden (see subsections (1) and (2B);
   b. the regulators change existing rules that contain a retained EU obligation and the effect of the change is to reduce a regulatory burden and the changes have no other effects that are material (see subsections (2) and (2C);
   c. the regulator revokes rules containing a retained EU obligation and the rules are not replaced by other rules (see subsection (2A))..

148. “Regulatory burden” is defined in subsection (2D). “Retained EU obligation” is defined in Schedule 1 to the Interpretation Act 1978[17].

149. In relation to the circumstances described in (a) and (b), above, the regulator can only make or amend rules where a provision or EU obligation is specified, or falls within a description of provisions, in regulations made by the Treasury.

150. Where the regulator revokes rules in the circumstances described in (c), above, the retained EU obligation in the relevant rules will not be specified in regulations made by the Treasury.

151. The regulations made by the Treasury under this clause are subject to the affirmative procedure.

Justification for taking the power

152. The effect of the power to specify in regulations retained EU law or an EU obligation will enable HM Treasury to create targeted exemptions from the requirements that the regulators consult on rules and undertake CBA where it is disproportionate to require the regulators to consult on rules which do not materially change the status quo or which reduce a regulatory burden.

153. This will give the regulators discretion as to whether to consult, and to take a proportionate approach to consulting when they chose to do so. For example, there may be some cases where, even when the conditions set out in this clause are satisfied, it is nonetheless appropriate for the regulators to consult on the rules they intend to make (for

[17] Interpretation Act 1978 c.30.

example, where the regulator is of the opinion that there remains a common law duty to consult on a particular set of rules because a legitimate expectation to consult may have arisen).

Justification for the procedure

154. The purpose of the exemption in clause 6 is to expedite the process of transferring regulations from retained EU law to the regulators' rulebooks if no material changes are to be made or where the rules reduce a regulatory burden. However, the power in subsections (1)(b) and (2)(b) to specify in regulations retained EU law or an EU obligation operates as part of the mechanism in clause 6 to disapply parts of primary legislation specified in subsection (3). Therefore, it is appropriate that the affirmative procedure applies where HM Treasury makes regulations under these subsections of clause 6.

Designated Activities Regime

Clause 8: Designated Activities

New section 71K (Designated activities) and Schedule 6B of FSMA 2000

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure:

- *Affirmative where the effect (or one of the effects) of the proposed regulations would be that an activity which is not a designated activity would become a designated activity, or*
- *Made affirmative where, by reason of urgency, it is necessary to make the regulations without a draft being laid and approved by Parliament (in which case the statutory instrument must be laid after being made and ceases to have effect at the end of the period of 28 days beginning with the day on which the instrument is made unless approved by parliament).*
- *Negative in all other cases.*

Context and Purpose

155. As set out above, clause 1 revokes retained EU law, which will enable the UK to move to a comprehensive FSMA 2000 model of financial services regulation following EU exit.

156. Whilst many aspects of financial services are regulated through the RAO regime, there are many pieces of retained EU law which set the rules for a kind of activity, product, or conduct which are not FSMA 2000 regulated activities, and which apply to a broader range of entities than FSMA 2000 authorised persons. As a result, the general rule-making powers of the PRA and the FCA in relation to authorised persons do not currently apply. Some examples include the Short Selling Regulation[18], which sets out the rules which apply to the activity of short selling, or margin rules that apply to certain types of derivative transactions, which set out how firms engaged in this activity should mitigate the risk posed by these types of contracts.

157. Many of these activities came to be subject to EU law as a response to the global financial crisis, when policy makers sought to introduce standardised rules across a number of different activities, even where those activities may be carried out by some firms which may not consider themselves to be "financial services" firms at all. For example, a large variety of businesses across the economy, including non-financial businesses, enter into derivatives contracts. A car manufacturer may enter into a metal derivative contract in order to protect itself against fluctuations in the price of metals. Under retained EU law, these contracts can require a certain amount of "margin" or collateral in order to reduce the impact if one party is not able to meet its obligations in that contract.

158. The EU legislated to regulate these activities following the global financial crisis as they can have material impact on the proper functioning of financial markets and

[18] EU 236/2012

consumers. These risks continue to operate now that the UK is outside the EU and it is HM Treasury's opinion that they continue to require regulation. However, it would be disproportionate to do so by making them regulated activities under the RAO. Doing so would require any firm wishing to carry out such activities to become an authorised person under FSMA 2000 and comply with all the obligations that entails, including giving the regulators the power to make rules over the firms' wider business unrelated to that activity.

159. Accordingly, the FCA's rule-making powers under the Designated Activities Regime ("the DAR") will only extend to matters relating to the designated activity and will not allow the FCA to make rules relating to the wider, unrelated activities of the person carrying out the designated activity. Anyone wishing to carry out a designated activity will be required to do so in line with conditions or rules made by HM Treasury or by the FCA but will not be required to seek authorisation under FSMA 2000.

160. In order to bring these types of activities within the FSMA 2000 model of regulation, clause 8 of the Bill introduces into FSMA 2000 a new regime, the DAR. The DAR will allow for the proportionate, 'activity-specific' regulation of these activities. New section 71K of FSMA 2000, introduced by clause 8(2) will enable HM Treasury to 'designate' an activity by way of regulations ("designated activity regulations"), which relates or is connected to: (i) the UK's financial markets or exchanges, or (ii) financial instruments, financial products, or financial investments. Section 71K is supplemented by new section 71M, which provides further details about the sort of provision that DAR designation regulations might make, including that the designated activities regulations can confer powers on HM Treasury or the FCA.

161. The purpose of the power in new section 71K is to enable HM Treasury to make regulations to provide for an activity of a specified description to be a designated activity for the purposes of FSMA 2000. This follows the model of section 22 of and Schedule 2 to FSMA 2000. Schedule 3 of the Bill inserts a new Schedule 6B into FSMA 2000, which gives examples of the areas of regulation that HM Treasury expect the powers to be initially used. This supplements section 71K, and, as with Schedule 2 of FSMA 2000, nothing in new Schedule 6B limits the powers conferred by section 71K.

162. The effect of this power is that a person who carries on an activity that has been designated in designated activities regulations can only carry on that activity to the extent, and subject to the conditions, which are imposed under the designated activities regulations. This might mean that the activity cannot be carried on at all, or that it can only be carried on in accordance with conditions imposed in the designated activities regulations or it can only be carried on in accordance with rules made by the FCA in relation to the conduct of that activity. For instance, the wider regulation of cryptoassets, as allowed for by section 71K(7) of FSMA 2000 may be a future such use of the DAR.

Justification for taking the power

163. The government has committed to repealing all retained EU law governing financial services. The powers under the DAR framework will enable HM Treasury to bring

activities currently regulated by retained EU law within the FSMA 2000 model of financial services regulation via secondary legislation. This will allow for the proportionate regulation of these activities by secondary legislation and the independent FCA. HM Treasury's power to confer supervision and enforcement powers on the FCA on an activity-by-activity basis will ensure effective regulation and protect consumers and UK markets. The creation of the DAR will allow for a regulatory framework capable of regulating future, as yet unknown, activities within the UK's financial markets, in a similar way to the way that the RAO allows HM Treasury to include new activities within the regulated and authorised persons regime.

Justification for the procedure

164. New section 71K is designed to bring activities within the regulatory perimeter pursuant to a FSMA 2000 model where HM Treasury controls the perimeter of regulation and the regulators make detailed rules. Where HM Treasury designates an activity for the first time, and so that activity will be regulated pursuant to the rules set out in the DAR, then parliament should have the opportunity to debate the appropriateness of this extension of regulatory reach, and the affirmative procedure is appropriate.

165. This is consistent with section 429 of FSMA 2000 and paragraph 26 of Schedule 2 to FSMA 2000, which governs regulated activities. These provisions state that regulations should be subject to the affirmative procedure where, in the opinion of HM Treasury, the effect (or one of the effects) of the proposed order would be that an activity which is not a regulated activity would become a regulated activity. However, paragraph 26 of Schedule 2 to FSMA 2000 provides that where, in the opinion of HM Treasury, by reason of urgency, it is necessary to make the order without a draft being laid and approved by parliament, the statutory instrument must be laid after being made and ceases to have effect at the end of the period of 28 days beginning with the day on which the instrument is made unless approved by parliament. In all other cases the negative procedure applies. The procedure for the designated activity regulations under new section 71K therefore follows the procedure which has been in place for many years for the RAO.

166. Many of the matters which will be subject to a designation regulation are currently regulated pursuant to retained EU law and HM Treasury anticipates that these matters will continue to be regulated, but it is appropriate for parliament to debate the transition from retained EU law to the DAR.

New section 71N (Designated activities: rules) of FSMA 2000

Power conferred on: Financial Conduct Authority
Power exercised by: rules made in accordance with Part 5A of FSMA 2000
Parliamentary Procedure: none

Context and Purpose

167. New section 71N(1) of FSMA 2000 provides for the FCA to make rules relating to activities designated by HM Treasury under new section 71K.

168. The power in section 71N(1) is constrained by section 71N(2) which provides that the power is only exercisable in so far as permitted by designated activity regulations. This means that HM Treasury sets the parameters of those areas of rules that should remain under the policy control of HM Treasury, and which areas it considers are appropriate to delegate to the FCA. For example, some activities HM Treasury intends to designate, are subject to criminal offences and certain definitions set the scope of the FCA's regulatory reach in regard to these activities. It is appropriate that these areas remain in legislation in accordance with the general working of the FSMA 2000 model.

169. The purpose of the power in new section 71N is to enable the FCA to make rules relating to a designated activity, within a framework set by HM Treasury.

Justification for taking the power

170. Under the FSMA 2000 model of regulation, the regulators are given responsibility to make detailed rules over financial services firms within parameters (including statutory objectives) set by Parliament. New section 71N(1) in conjunction with new section 71N(2) will enable HM Treasury to confer appropriate rule-making powers on the FCA in relation to designated activities in a manner consistent with the existing FSMA 2000 model of regulation. HM Treasury's power to scope the FCA's rule-making power under new section 71N(2) will ensure HM Treasury is able to retain, as appropriate, overview of regulations relating to designated activities which should remain in legislation. To do this via primary legislation would be time consuming and weigh heavily on Parliamentary resource and would not fit within the existing FSMA 2000 model.

Justification for the procedure

171. It is considered that no additional parliamentary oversight is required in relation to the exercise of this power by the FCA whilst exercising its rule making powers on the basis of the existing accountability framework set out in the FSMA 2000 (and further enhanced by measures in this Bill). As set out above the power will be constrained by HM Treasury in secondary legislation to set which areas remain under control of HM Treasury and which areas the FCA can make rules in.

New section 71N(3) of FSMA 2000 (Designated activities: power to suspend rules)

Power conferred on: Financial Conduct Authority
Power exercised by: rules made in accordance with Part 5A of FSMA 2000
Parliamentary Procedure: None

Context and Purpose

172. Section 71N(3) provides the FCA with a power to suspend any of its rules for such period as it considers appropriate. The split responsibility of regulation between primary and secondary legislation on the one hand, and regulator rules on the other is a well-established feature in the FSMA 2000 model and allows for regulation to be as agile as possible to respond to market conditions. This sort of arrangement already exists in elements of retained EU law, for example, Article 13 of the Short Selling Regulation describes circumstances in which certain rules can be suspended.

Justification for taking the power

173. The FCA already has the ability to suspend rules in certain circumstances in retained EU law. For example, Article 13 of the Short Selling Regulation describes circumstances in which certain rules can be suspended. This ensures the FCA can respond quickly where it thinks the relevant market is not functioning properly.

174. As short selling is an activity which HM Treasury may designate under the DAR, it is important that the DAR is capable of giving the FCA the appropriate tools including those it already possesses for responding to market changes when regulating short selling or similar activities. HM Treasury will be able to say in secondary legislation when designating each activity when and if it is appropriate for the FCA to use this power.

Justification for the procedure

175. It is considered that no additional Parliamentary oversight is required in relation to the exercise of this power by the FCA on the basis of the existing accountability framework set out in FSMA 2000 (and further enhanced by measures in this Bill). As set out above the power will be constrained by HM Treasury in secondary legislation to set which areas remain under control of HM Treasury and which areas the FCA can make rules in.

New section 71O (Designated activities: directions) of FSMA 2000

Power conferred on: Financial Conduct Authority
Power exercised by: rules made in accordance with Part 5A of FSMA 2000
Parliamentary Procedure: None

Context and Purpose

176. Section 71O of FSMA 2000 provides a power to the FCA to make (and revoke) directions relating to designated activities. Directions are a tool of regulation used by the FCA and the PRA in relation to authorised persons, and typically allow the FCA to tailor regulations to the circumstances of the authorised person. It is appropriate that this tool is also available to the FCA under the DAR, as part of a flexible regime suited to proportionate regulation-making at the level of the FCA as financial regulator. This power allows the FCA to ensure that the DAR operates effectively in relation to all people (and classes of people) engaged in certain activities. Directions may require people undertaking activities to take specified action, or to refrain from taking specified actions, and the requirement

may extend to activities which are not designated activities (though the requirement itself must relate to a designated activity.

177. The purpose of the power in new section 71O is to enable the FCA to make directions which do not rely on the consent of the person concerned. It may also be constrained by HM Treasury through provisions made in designated activity regulations.

Justification for taking the power

178. This power to provide directions is appropriate for regulation set at the level of regulator rules rather than secondary legislation, as, at regulator rule level, it is appropriate to have a flexible process which allows for a quick response to market conditions.

Justification for the procedure

179. It is considered that no additional Parliamentary oversight is required in relation to the exercise of this power by the FCA on the basis of the existing accountability framework set out in FSMA 2000 (and further enhanced by measures in this Bill). As set out above the power will be constrained by HM Treasury in secondary legislation to set which areas remain under control of HM Treasury and for which areas the FCA can make directions.

New section 71Q of FSMA 2000 (Designated activities and rules: enforcement)

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative unless amending FSMA 2000

Context and Purpose

180. Where activities which were previously regulated through retained EU law become regulated through designated activity regulations it will be important to ensure that tools for enforcement are not lost.

181. Currently, where there is retained EU law, existing monitoring and enforcement powers within FSMA 2000 are sometimes applied through FSMA 2000 (Qualifying EU Provisions) Order 2013[19] ("QUEPO"). The QUEPO applies provisions of FSMA 2000 to retained EU law files listed within it. When an area of regulated activity becomes subject to designated activity regulations, the corresponding retained EU law will be revoked, through commencing the revocation of that law under clause 1 of the Bill and the powers applied under the QUEPO will lapse.

182. As an alternative to the QUEPO approach, enforcement provisions of FSMA 2000 have sometimes been applied through statutory instruments made under the ECA and the EUWA, with or without modifications. Examples are regulation 62 of, and Schedule 3 to,

[19] S.I .2013/419

the Electronic Money Regulations 2011[20] and regulation 1 and paragraph 1 of Schedule 1 to the Payments in Euro (Credit Transfers and Direct Debits) Regulations 2012.[21] These enforcement powers will again lapse, when that activity becomes regulated under designated activity regulations and the accompanying provision in clause 1 is commenced.

183. To ensure that the FCA has all the necessary enforcement tools to allow for the effective regulation of designated activities, section 71Q of FSMA 2000 provides that designated activity regulations may make provision about enforcement in relation to activities included in the DAR.

184. Subsection (2) provides a non-exhaustive list of the types of provision which may be made. Whilst this list is wide the powers are not exceptional for financial services regulation. Examples of similar arrangements exist in FSMA 2000, in relation to authorised persons, in Parts 9A, 11, 14 and 25, and they also exist in relation to non-authorised persons to enable the FCA to effectively regulate relevant parts of retained EU law extending to authorised and non-authorised persons, such as in Part 8A.

185. Subsections (3) and (4) confirm that the power in section 71Q includes the power to apply provisions of FSMA 2000 with or without modification. This will allow HM Treasury to follow the well understood framework of the QUEPO that applies sections of FSMA 2000 to financial services regulations on a case-by-case basis.

Justification for taking the power

186. The power allows HM Treasury to confer on the regulators the appropriate and proportionate enforcement powers on an activity-by-activity basis. This will allow the FCA to undertake appropriate and proportionate monitoring and enforcement of activities designated in designated activity regulations.

Justification for the procedure

187. HM Treasury considers that it is appropriate that Parliament is afforded the opportunity to scrutinise the conferment of powers of enforcement on the regulators and for this scrutiny to be exercised in relation to each designated activity.

188. Enforcement powers for many of the activities currently regulated under retained EU law already exist as set out above. HM Treasury, therefore, consider that replacing those powers when an activity is a designated activity should be subject to the negative procedure. However, it is anticipated that, for each designated activity, the initial enforcement powers will be established in the statutory instrument which designates that activity for the first time, and thus will be subject to the affirmative procedure.

New section 71R of FSMA 2000 (Designated activities and rules: connected amendments)

[20] S.I. 2011/99
[21] S.I. 2012/3122

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative when amending primary, otherwise negative

Context and Purpose

189. The DAR will be inserted as a substantial new part of FSMA 2000, and it is HM Treasury's intention that it will be used to adapt existing parts of FSMA 2000 to operate for the purposes of a designated activity, designated activity regulations or designated activity rules.

190. In order to allow for this, and to ensure that the body of law under FSMA 2000, and other Acts which govern financial services and markets regulation, remains consistent and effective, new section 71R of FSMA 2000 gives HM Treasury the power to amend or modify existing provisions within FSMA 2000, and other primary legislation, in a way it considers appropriate for purposes of, or connected with, any designated activity rules or regulations.

191. This includes, under subsection (3), the power to modify (including by widening the scope of) existing criminal offences attached to designated activities under FSMA 2000. The purpose of the power in new section 71R(3) is to ensure that there is a consistent body of legislation in FSMA 2000 and the regulations which sit underneath it after the inclusion of the new Part 5A of FSMA 2000.

Justification for taking the power

192. Where there is a substantial new Part of FSMA 2000, as with the DAR, it is important that HM Treasury can make connected modifications to FSMA 2000, to regulations made under it, and other primary legislation, in order that the body of law under the FSMA 2000 framework works consistently and effectively.

193. Some activities currently regulated by retained EU law (and which HM Treasury intends to designate through designated activities regulations) already have criminal offences attached to them. However, it may be that when HM Treasury designates the activity, the description of that activity does not match the perimeter of the criminal offence as described in FSMA 2000.

194. It would be disproportionate for HM Treasury to take a broad power to make new criminal offences under the DAR. However, where an existing criminal offence is attached to an activity HM Treasury intends to designate, it is necessary to make provision to allow HM Treasury to retain that criminal offence and, where appropriate, tailor that offence to the new designated activity in a flexible way which can take account of current proposals for regulation and future changes to the regulation of activities within the DAR. This will allow HM Treasury to retain these criminal offences following the repeal of retained EU law, and to be able to modify them so that they fit with HM Treasury's proposals for regulating that activity beyond the offence which attached to retained EU law. New section 71R(3) provides that the power to amend FSMA 2000 extends to modifying (including by

widening) criminal sanctions within FSMA 2000. This means HM Treasury will be able to amend existing criminal offences in primary legislation, and criminal offences already attached to activities HM Treasury designates, by way of secondary legislation.

195. HM Treasury is currently aware of only one instance where it expects to use this power. HM Treasury intends to use this power to deliver changes (previously consulted on in July to September 2021) to the criminal offences that currently apply to the prospectus regime, which are set out in section 85 of FSMA 2000.

Justification for the procedure

196. It is considered appropriate that any regulations made using these powers are subject to the affirmative procedure in both Houses of Parliament where amending primary legislation, especially given they can modify offences.

Financial market infrastructure: general rules and requirements

Clause 9: Rules relating to central counterparties and central securities depositories

New section 300F(1) of FSMA 2000 (Rules relating to central counterparties and recognised CSDs) - power to make rules applying to recognised central counterparties, recognised CSDs, third country central counterparties and third country CSDs as appear to the Bank to be necessary or expedient for the purpose of advancing its Financial Stability Objective

> *Power conferred on: Bank of England*
> *Power exercised by: rules to be made in accordance with the provisions of Part 9A of the FSMA 2000 which are applied to the Bank by paragraph 10, Schedule 17A FSMA 2000*
> *Parliamentary Procedure: none*

Context and Purpose

197. The Bank is responsible for supervising and regulating central counterparties ("CCPs") and central securities depositories ("CSDs"), both of which are types of FMI.[22] This is currently done through provisions contained in Part 18 of FSMA 2000, which establishes a recognition mechanism for these bodies, and detailed requirements contained in two EU regulations which have been retained in UK law following the UK's exit from the EU. These are, for CCPs, Regulation (EU) 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (for CCPs) ("EMIR") and, for CSDs, Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories ("the CSDR") (together "the Bank FMI regulations").

198. Clause 1 of this Bill will, once commenced, repeal the Bank FMI regulations. The government intends to use the power in clause 5 to restate the Bank FMI Regulations in domestic law, and in so doing provide for the direct regulatory requirements on firms to be set by the relevant regulator in accordance with the FSMA 2000 model. However, the Bank currently has extremely limited rule-making powers over these entities, and so would not be able to make the necessary rules. The purpose of this general rule-making power in new section 300F of FSMA 2000 is to ensure that the Bank has the necessary rule-making powers to take full responsibility for these entities once retained EU law has been repealed.

199. The Bank's power to make rules over third country central counterparties and third country CSDs is subject to section 300G (which will also be inserted into FSMA 2000 by this clause) and provides for certain limitations and procedures in relation to rules for overseas firms. In particular, section 300G of FSMA 2000 provides that for these overseas firms, the Bank can only apply the corresponding rules that apply to domestic CCPs or

[22] In financial markets, there are various processes that need to be performed to complete each transaction. These processes are performed by several different types of entity collectively referred to as 'financial market infrastructures' (FMIs). Such processes encompass a range of activities underpinning the functioning of financial markets, including trading services (i.e. facilitating parties to enter into financial transactions) provided by trading venues, and post-trade services such as clearing and settlement (giving effect to trades by transferring securities and payment between parties) provided by central counterparties and securities settlement systems.

CSDs (with appropriate modifications). The Bank cannot impose different rules on overseas firms.

Justification for taking the power

200. The general rule-making power for the Bank is a crucial part of re-establishing the FSMA 2000 model in this area. In line with the overall approach to the FRF, it will allow for the Bank, as the responsible regulator, to take greater responsibility for setting detailed requirements for CCPs and CSDs. The power will be balanced by a strengthened accountability and transparency framework and updated statutory objectives for the Bank, provided for in clauses 45, 46 and 47 of this Bill.

Justification for the procedure

201. As with the FCA and the PRA's general rule-making powers under FSMA 2000 and in relation to the new DAR, it is not considered appropriate to provide for formal parliamentary scrutiny of the rules made using this new rule-making power. However, the provisions Part 9A of FSMA 2000 which are applied to the Bank by Schedule 17A to FSMA 2000 impose procedural requirements on the Bank when making rules, which are designed to ensure that the process of rulemaking is proportionate and transparent. These procedural requirements include: (i) requirements to consult and in many cases to conduct cost benefit analyses before making rules, (ii) a requirement to publish rules in the manner best calculated to bring them to the attention of the public, and (iii) a new requirement imposed by clause 36 (and applied to the Bank by subsection (13) of clause 47 to notify and engage with the relevant Parliamentary committee whenever the Bank issues a consultation.

New section 300G(1)(b) of FSMA 2000 (Section 300F: rules in relation to overseas FMI entities) – power to make regulations authorising the making by the Bank of rules applying to third country central counterparties and third country CSDs

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

202. Section 300F(1) of FSMA 2000 provides for a new Bank general rule-making power over recognised CCPs and recognised CSDs, which are both types of domestic firm. This rule-making power also applies to third country central counterparties and third country CSDs, to the extent permitted by new section 300G. Under section 300G(1)(b), HM Treasury is able to make provision authorising the Bank to make rules which apply to third country central counterparties and third country CSDs. With the exception of "systemic third country CCPs" (provision for which is made in s.300G(6) to (13)), the Bank is only permitted to make rules which apply to these third country firms to the extent it is authorised to do so by HM Treasury's regulations.

203. Section 300G(5) allows for HM Treasury to make provision by reference to matters determined by the Bank when making these regulations.

204. Subsection (5) also allows HM Treasury to provide that the Bank's rule making power over these overseas entities is limited (for example to rules made for specified purposes) or subject to conditions.

Justification for taking the power

205. This power is necessary in order to ensure that, if the Government considers it necessary or appropriate in the future, HM Treasury can confer powers on the Bank to ensure that the framework for overseas CCPs and CSDs providing services to the UK is robust. HM Treasury's ability to place limitations or conditions on this power is important to ensure that the Bank's power is proportionate to the policy objective at the time.

Justification for the procedure

206. The negative procedure is considered appropriate because the power is limited to specifying the types of overseas CCP or CSD in relation to which the Bank can make rules, and limiting the purposes for which the Bank's power to make rules over these entities can be used.

New section 300G(9) of FSMA 2000 (Section 300F: rules in relation to overseas FMI entities) – power to make regulations setting criteria of general application to be used by the Bank in determining whether a firm is a systemic third country CCP

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

207. Section 300G provides that the Bank can apply to systemic third country CCPs the rules which apply to UK central counterparties (with appropriate modifications). It is for the Bank to determine whether a firm is a systemic third country CCP. Section 300G(9) provides for HM Treasury to make regulations setting out criteria of general application to be used by the Bank in determining whether a firm is a systemic third country CCP. This can be supplemented in a statement of policy by the Bank, setting out more detailed criteria.

Justification for taking the power

208. This power is necessary in order to ensure that the Government can set out the high level criteria which are to be used by the Bank to determine whether a firm is of systemic importance, and therefore should be subject to the Bank's rules. This will allow HM

Treasury to provide for criteria of a similar nature to those which are currently set out in article 25(2a) of EMIR, and are used to determine whether a firm is a "Tier 2 CCP".

Justification for the procedure

209. The negative procedure is considered appropriate because the power is limited to specifying high level criteria to be used by the Bank.

New section 300G(14) of FSMA 2000 (Section 300G: rules in relation to overseas FMI entities) – power to provide for provisions of FSMA 2000 to apply to relevant third country central counterparties and relevant third country CSDs with such modifications as may be specified

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and purpose

210. This power allows HM Treasury to make regulations applying provisions of FSMA 2000 with modifications to relevant third country CCPs and relevant third country CSDs. These are the overseas firms that the Bank will be able to apply its rules to, subject to the limitations set out in section 300G. This power is needed in order to ensure that provisions of FSMA 2000- for example regarding regulatory investigations - apply to these firms as is appropriate in light of the rules that the Bank is able to make. Schedule 17A already makes some provision for application of provisions in FSMA 2000.

Justification for taking the power

211. A power is needed as it is not clear at this stage exactly which provisions of FSMA 2000 it will be appropriate to apply to different types of overseas entities in future, as that will depend on the extent to which the Bank is permitted to apply its rules to overseas firms, according to provision made under s.300G(1)(b).

Justification for the procedure

212. The negative procedure is considered appropriate as the provision made under this power will be technical and limited to the application of existing provisions of FSMA 2000 to these entities.

Clause 10: Other requirements relating to central counterparties and central securities depositories

- New paragraph 9B of schedule 17A to FSMA 2000 (further provision in relation to exercise of Part 18 functions by Bank of England) confers two powers on the Bank;
    a. Power in sub-paragraph (1) to impose requirements on a relevant FMI entity at the Bank's own initiative; and

b. Power in sub-paragraph (7) to impose requirements on the application of a relevant FMI entity.

Power conferred on: Bank of England
Power exercised by: direction
Parliamentary Procedure: none

Context and Purpose

213. The Bill introduces a general rule-making power for the Bank over CCPs and CSDs in clause 9. It also provides in clause 45 for an updated set of statutory objectives for the Bank to advance when exercising this power. The primary objective for the Bank in this area of regulation will remain its financial stability objective – which is to protect and enhance the stability of the UK financial system.

214. The powers in clause 10 will enable the Bank to impose requirements on an individual recognised CCP, a recognised CSD, or a systemic third country CSD. Paragraph 9B(1) of Schedule 17A to FSMA 2000 enables the Bank to impose requirements where either (i) it is desirable to do so to advance the Bank's financial stability objective, or (ii) a firm has failed, or is likely to fail, to satisfy recognition requirements or has failed to comply with an obligation under FSMA 2000. This aligns with similar powers which the FCA and the PRA have under section 55L and section 55M of FSMA 2000 respectively in relation to firms undertaking regulated activities.

215. Paragraph 9B(7) of Schedule 17A to FSMA 2000 provides for a requirement to be imposed on a firm on the application of that firm (known as a 'voluntary' requirement). Again, this is in line with the approach taken for the FCA and the PRA under section 55L and section 55M of FSMA 2000. In practice, this is the most common way for the PRA and the FCA to impose requirements on firms and will provide additional flexibility to the Bank in relation to the regulation of Bank FMIs. The Bill also applies a number of other aspects of the FCA and the PRA's powers in sections 55L to 55Z3 to the Bank in order to make this power to impose requirements operable, such as the power to refuse an application to impose a requirement and the ability to issue decision notices if an application is refused.

Justification for taking the power

216. The power is necessary to ensure the Bank has the full range of tools available to it to advance its financial stability objective and tackle non-compliance with recognition requirements and legal obligations. It will provide the Bank with equivalent powers to those which the FCA and the PRA already have under FSMA 2000 to impose requirements on their respective sets of regulated firms.

Justification for the procedure

217. It is not considered appropriate to provide for formal parliamentary oversight on the use of this power as it is a supervisory tool that the Bank would employ in relation to individual firms. Paragraph 9B(9) ensures that where appropriate the Bank is required to

follow the same procedure as that which applies to the FCA in the exercise of their powers to impose requirements. This includes requirements to issue warning and decision notices, and, where a requirement is imposed under paragraph 9B(1) (on the Bank's own initiative), or where a request for a voluntary requirement is refused, for an appeal to the First Tier Tribunal.

Clause 11: Rules relating to recognised investment exchanges and data reporting service providers

- New section 300H to FSMA 2000 (General rules: recognised investment exchanges and data reporting service providers)

Power conferred on: Financial Conduct Authority
Power exercised by: rules made under Part 9A of FSMA 2000
Parliamentary Procedure: none

Context and Purpose

218. As set out above, in relation to clause 1 the repeal of retained EU law will enable the UK to have a model of financial services regulation where many of the detailed rules will be written by the UK's financial services regulators. This clause gives the FCA general rule-making powers over Recognised Investment Exchanges ("RIEs") and Data Reporting Service Providers ("DRSPs") via an amendment to FSMA 2000 (insertion of new section 300H – Rules relating to recognised investment exchanges and other bodies).

219. The FCA currently has some powers over RIEs in sections 286 and 293 to 300 of FSMA 2000. However, these are limited for two reasons. First, under Part 18 of FSMA 2000, RIEs are exempt from the requirement of authorisation. Therefore, the general rule-making power that the FCA has under section 137A of FSMA 2000 does not apply to RIEs. Second, because prior to EU exit the regulations relating to RIEs were mainly set at EU level through the "Markets in Financial Instruments Regulation (MiFIR), the Markets in Financial Instruments Directive (MiFID) - together the 'Markets in Financial Instruments (MIFI) framework" - and the Market Abuse Regulation ("MAR") and so the FCA did not need extensive rule-making powers.

220. When retained EU law in relation to financial services is revoked pursuant to clause 1 and without conferring further powers on the FCA that would allow it to replace the rules in the MIFI framework, there will be a gap in the FCA's powers to appropriately regulate RIEs. Giving the FCA a general rule-making power for RIEs will allow the FCA to make rules to replace those revoked and thereby ensure that RIEs will continue to be regulated effectively.

221. Similarly, the rules for DRSPs derive mainly from the EU's MIFI framework. DRSP's are currently regulated under the Data Reporting Services Regulations 2017[23] (DRSRs), which formed part of the transposition of MiFID II into UK legislation. Other relevant

[23] S.I. 2017/699.

components include MAR 9 of the FCA Handbook and Chapter 6 of the MiFID Org Regulation in addition to transaction reporting obligations in Article 26 of onshored MiFIR and related technical standards. DRSPs are not 'relevant persons' under FSMA 2000, and so the FCA's general rule-making power does not apply to them.

222. When retained EU law in relation to financial services is revoked pursuant to clause 1, there will be a gap in the FCA's powers to appropriately regulate DRSPs. Giving the FCA a general rule-making power for DRSPs will allow the FCA to make rules to replace those revoked and thereby ensure they can continue to be regulated effectively.

223. The approach set out under this power is consistent with the powers that regulators are being given for other Financial Market Infrastructure firms (FMIs) as part of this Bill.

Justification for taking the power

224. The government considers that a general rule-making power is the most appropriate way to ensure that the regulation of UK RIEs and DRSPs continues to be effective once retained EU law is revoked. The exercise of this power will be subject to the enhanced accountability framework that this Bill introduces. This will ensure appropriate accountability, democratic input and stakeholder engagement in the FCA's rule-making process. A delegated power will provide the flexibility required to enable the regulator to respond to changing market conditions, emerging risks and innovation.

225. This power will also align the regulation of RIEs and DRSPs with the regulation of other FMIs such as Central Counterparties (CCPs), where delegated powers are being given to the Bank of England pursuant to clause 9. It will also align the FCA's ability to set requirements for trading venues operated by a UK RIE and those operated by MTFs and OTFs, as the power will ensure that all trading venues are subject to similar FCA rule-making powers.

Justification for taking the procedure

226. There is no parliamentary procedure. The FCA's general rule-making powers in Part 9A of FSMA 2000 do not have formal parliamentary oversight. These powers are specific rule-making powers, which replicate the procedures that apply to the FCA's general rule-making powers, and as such HM Treasury do not consider it appropriate to provide for any additional, formal parliamentary oversight. Instead, safeguards provided in Part 9A of FSMA 2000 will apply, in particular, sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA).

Financial market infrastructure: Piloting powers

Clause 13: Testing of FMI technologies or practices

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

227. A new power for HM Treasury to make regulations for the purpose of (1) testing, for a limited period, the efficiency or effectiveness of the carrying on of FMI activities in a particular way using developing technology (such as distributed ledger technology) or adopting new or different practices (such as new forms of trading venue) and (2) assessing whether or how relevant enactments should apply in relation to the FMI activities carried on in that way. This provision is referred to as an 'FMI Sandbox'.

228. In financial markets, there are various processes that need to be performed to complete each transaction. These processes are performed by several different types of FMIs. Some FMIs are considered systemically important, meaning that the failure of an FMI could lead to material instability across the financial services sector, with subsequent negative impacts on the real economy due to the disruption this would cause to the proper functioning of the financial markets, on which many economic activities rely. It is therefore important that there is a robust regulatory framework to manage any risks associated with the use of new technology and adoption of new practices by FMIs.

229. It is however also important that FMIs can innovate and adopt new technologies or practices. These could allow firms to reduce their operating costs and perform in new and better ways and allow markets to operate more effectively. Effective competition and innovation enable agile companies to meet customer needs and challenge incumbents by providing better services, which, in turn, helps to maintain the UK financial services system at the forefront of innovation. However, it is not yet clear what legislative changes will most effectively support FMIs in their safe use of new technology or practices.

230. A particular example of this is distributed ledger technology ("DLT"), which enables the sharing and updating of information records in a distributed and decentralised way. Since some of the key functions that FMIs perform relate to the accurate maintenance of, and access to, records of financial transactions, DLT could potentially make FMI services more efficient, more resilient and more transparent.

231. In 2021, HM Treasury conducted a Call for Evidence to examine the application of DLT to FMIs. A key issue identified in responses to the Call for Evidence was that the UK legislative framework has not been built to support the use of DLT in FMIs, and that a reconsideration of the legislative framework would be needed to enable the use of DLT and to realise the potential benefits while ensuring regulatory objectives around their safety and robustness were met.

232. A further example is where existing regulatory requirements represent a barrier for firms that want to access capital through public markets. As set out in the response to the Wholesale Markets Review ("WMR") consultation – which was published in March 2022 – respondents identified that regulatory burdens and costs associated with having their securities admitted on a public market can represent a barrier for SMEs financing on public markets. Most respondents asked the government to therefore consider a more proportionate disclosure regime without lowering regulatory standards. The testing and introduction of bespoke requirements could therefore potentially facilitate greater access to public markets sooner for SMEs, private companies and other businesses.

233. An FMI sandbox is designed to test in a controlled environment for a limited period of time whether and how FMI's can use developing technology or new practices to perform specific activities and to test its compatibility within the existing legislative framework in an effective, efficient and safe way. It can be used to remove existing regulatory barriers and put in place more appropriate temporary rules. There is no legislative precedent in the UK for a pilot scheme known as a "Sandbox", and this is an expression which is more often used in the technology field, but the FCA operate a regulatory Sandbox24 in this area and there are plenty of examples of legislative pilot schemes.

234. Clause 13 and Schedule 4 provide that HM Treasury may make regulations that will identify the descriptions of FMI entities and other persons (e.g. users of FMI's) who are eligible to participate in an FMI Sandbox, the FMI activities to which the Sandbox relates, and period for which the Sandbox arrangements apply. Modifications will be made to relevant enactments for the purposes of the Sandbox.

Justification for taking the power

235. The taking of a regulation making power is important for the implementation of a Sandbox, because the UK needs to be able to respond swiftly to developments in technology and the emergence of new practices in the carrying out of FMI activities. New technology or practices could take many forms in the coming years and legislative flexibility is important. If provision for the testing were to be made wholly in primary legislation this would delay, or potentially prevent, testing, creating a significant barrier to innovation and placing the UK at a comparative disadvantage to its competitors. Testing also enables HM Treasury and the regulators to better understand new technologies and practices where the business models are still evolving, enabling legislation to be better tailored and consequently more effective.

Justification for the procedure

236. The power includes powers to modify certain Acts of Parliament and retained EU law regulations, among other relevant enactments. An affirmative procedure is not considered appropriate because the powers will be exercised temporarily for the duration of an FMI Sandbox and would apply to legislation expressly identified on the face of the Bill, or as

[24] https://www.fca.org.uk/firms/innovation/regulatory-sandbox

modified by clause 17(6). Applying the affirmative procedure in this context, would place a considerable burden on Parliament in scrutinising legislation, because more than one Sandbox may operate at any given time (for different sectors) and the modifications of legislation may be technically complex and lengthy.

237. Other relevant features of the power justifying the choice of procedure are as follows. The modifications of legislation which may be made apply only to the FMI entities, and others (such as users of FMI entities), described in the regulations who participate in the FMI Sandbox. The enactments that may be modified by HM Treasury are restricted to those that are listed in the Bill or that are added to the list by regulations using the power in clause 17(6) explained below. During the operation of the Sandbox the general legislation will continue to apply as before to those firms who do not participate in the Sandbox.

238. HM Treasury may impose limits or prohibitions on the type and values of financial instruments tested under the Sandbox. This is an important safeguard for ensuring that the testing in the FMI Sandbox is undertaken safely. Provision may also be made, in the enforcement provisions of the regulations allowing the appropriate regulator to suspend or terminate a person's participation in the FMI Sandbox or impose civil penalties.

239. Clause 16 requires that HM Treasury consults with the regulators, and such other persons as HM Treasury considers appropriate, before it makes regulations pursuant to this power. Through the transparency and reporting provisions of the regulations mentioned in Schedule 4, HM Treasury may impose requirements on the appropriate regulator to publish specified details of the FMI Sandbox arrangements. Under clause 13, HM Treasury must report to Parliament on the outcome of each FMI Sandbox before they may exercise their separate delegated power to make permanent changes to the law (which is subject to a different Parliamentary procedure).

Clause 13 and clause 16: Testing of FMI Technologies/Regulations

- A new power for the FCA and the Bank of England to do anything under, or for the purposes of, the regulations, including making or modifying rules or technical standards.

Power conferred on: the Financial Conduct Authority and the Bank of England
Power exercised by: rules
Parliamentary Procedure: none.

Context and Purpose

Clause 13(5) and clause 16

240. The context is the same as for the other clauses relating to the FMI Sandbox.

241. This power (which may be conferred by regulations made by HM Treasury under clauses 13 and 16(1) would (amongst other things) give the appropriate regulator powers to make or modify rules and technical standards applicable for the purposes of the FMI Sandbox arrangements or to change their existing rules and technical standards for these purposes.

242. To be sufficiently flexible to be workable in practice, the procedural requirements imposed on the regulators by HM Treasury may be different from those currently applying to the making of permanent rules or technical standards of general application.

243. The powers that may be conferred on the regulators also include enforcement powers (see paragraph 9 of Schedule 4). These are necessary to ensure that the regulators have powers that are suitable in the unusual circumstances of a Sandbox, including the powers to suspend or terminate participation in the Sandbox.

Justification for taking the power

244. The appropriate regulator may need to make or modify rules or technical standards for the purposes of an FMI sandbox. For example, new rules or technical standards may need to be made to facilitate, or to address risks posed by, the testing of carrying on FMI activities using developing technologies or new practices, and for assessing how rules or technical standards should apply in relation to FMI activities carried on in this way. It is expected that the regulator will also need, through its rulebook and technical standards, to put in place applications or other procedures for participating in the FMI sandbox arrangements.

245. The consultation procedure that applies to the making of rules of general application under existing powers of the regulators under FSMA 2000 may not be appropriate in such a case, because the FMI Sandbox will have limited application and duration and because the regulators will need to flexibly respond to new issues that may arise in the course of an FMI sandbox. Clause 16(2) requires that HM Treasury consult before making regulations under these sections.

Justification for the procedure

246. The regulators' existing rule making powers are not subject to Parliamentary scrutiny and therefore it is not appropriate for such scrutiny to apply to these new rule making powers. The relevant powers relate to making, modifying or deleting rules or technical standards for purposes of the FMI Sandbox. Furthermore, the making of operational decisions concerning participation in the Sandbox is plainly more properly a matter for the regulators.

Clause 15: Permanent implementation of arrangements tested under an FMI Sandbox

- A new power for HM Treasury to make regulations implementing sandbox arrangements after testing of them in a Sandbox has finished.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative unless subsection (5) does not apply.

Context and Purpose

247. The context for this power is the same as for the related power providing for the testing of FMI technologies and practices.

248. The purpose of this power is to allow permanent and general implementation of the temporary and limited legislative modifications made under clause 13 through amendments of the legislation. The power also permits HM Treasury to make such variations to the temporary amendments as HM Treasury considers appropriate; this arrangement allows HM Treasury to learn from the FMI Sandbox and make improvements where the report to Parliament on a FMI Sandbox shows that it is not as efficient or effective as it could have been.

249. The power permits HM Treasury to make these permanent changes either after the Sandbox has concluded or before it has finished. There may be sufficiently compelling evidence for seeking to enact the modifications prior to the formal termination date, based on how the FMI Sandbox has performed. It also ensures there is no legislative gap between the temporary and permanent arrangements.

Justification for taking the power

250. It is important that modifications can be made quickly and before the end of a FMI Sandbox, because otherwise the participants who have tested new technology and practices would have to revert to old technology and practices again for a period. Making the temporary changes permanent and applying them generally to classes of FMI and others will require further legislation. If this were to be achieved through primary legislation this would inevitably lead to a legislative gap during which firms would have no choice but to revert to using older technology or practices. If the new technology or practices prove to be more efficient or effective during the Sandbox, such a legislative gap could be seen as damaging to services and competitiveness.

Justification for the procedure

251. Pursuant to clause 15(5) and in accordance with ordinary conventions, HM Treasury proposes that the affirmative procedure applies if the regulations amend primary legislation. In other cases, and pursuant to clause 15(6), a negative procedure will apply. HM Treasury must first report to Parliament on the success of the Sandbox and the changes being taken forward, and HM Treasury must consult the appropriate regulators and such other persons as it considers appropriate before making any permanent changes. This will also enable any firms that did not participate in the Sandbox a further opportunity to express their views.

Clause 17: Interpretation

- A new power for HM Treasury to amend the list of relevant enactments in clause 17(3).

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative.

Context and Purpose

252. The context for this power is the same as for the other Sandbox powers (clauses 13 and 15).

253. The purpose is to allow HM Treasury to add to the list of "relevant enactments" which may be the subject of modifications by them under clause 13 or amendments under clause 15.

Justification for taking the power

254. The need to modify further enactments may emerge from the consultation which is required by clause 16. In addition, the categories of FMI entity which may potentially be the subject of an FMI Sandbox may be added to by regulations made under clause 13(11). If such provision is made, it may be appropriate to add to the list of relevant enactments.

255. Over time the legislation applying to FMI's will change. This is particularly true of the retained EU legislation which is to be revoked pursuant to clause 1 and replaced under the future regulatory reform provisions in the Bill. Some of the replacement provisions will not fall within the scope of the FCA's regulatory Sandbox. Consequently, it is appropriate to have a procedure enabling Sandboxes to continue to be created by HM Treasury in the future which modify the latest applicable legislation and subsequently for permanent amendments to be made. Waiting for an opportunity for primary legislation would have a similar detrimental effect to the omission of the powers provided for in clauses 13 and 15. If any legislative obstacles to the use of new technology or practices were to remain in place they could not be tested or permanently adopted.

Justification for the procedure

256. The power may be exercised to amend the list of enactments that may be modified under regulations providing for a FMI sandbox. This list is contained in primary legislation and so an affirmative procedure is considered appropriate.

Powers in relation to critical third parties

Clause 18: Critical third parties: designation and powers

New section 312L of FSMA 2000 (Critical third parties).

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: none

Context and Purpose

257. Financial services firms and FMI firms are, through outsourcing and other arrangements, increasingly relying on third parties outside the finance sector for key functions or services (such as cloud-based computing services). These arrangements can come with many benefits but can also introduce material risks into the provision of financial services. In particular, if many firms rely on the same third party, the failure or disruption of this 'critical' third party could pose financial stability or market confidence risks. These third parties are currently outside the financial services regulatory perimeter and so the financial regulators have no direct powers over them. Further, the regulators' existing powers are insufficient to properly mitigate the risks that these arrangements introduce into the financial services sector.

258. Clause 18 introduces a new chapter, Chapter 3C, into Part 18 of FSMA 2000. New section 312L confers on HM Treasury a power to designate a third-party provider to one or more authorised persons, relevant service provider, or FMI entity as 'critical'. New section 312L(8) defines relevant service provider and FMI entity, which together with the existing definition of authorised person, act as a limitation on the power. Such designation then enables the financial regulators to oversee the services that the designated third party provides to the financial services firms by bringing the third party into scope of the targeted oversight regime set out in clause 18.

Justification for taking the power

259. The list of critical third parties could change frequently and could require amendment at short notice. It would be impractical to pass an Act of Parliament each time a firm meets (or ceases to meet) the criteria for a critical third party. Accordingly, it is considered appropriate to take a power for HM Treasury to set the perimeter of the regulatory regime, which is considered to be in accordance with the principle of the FSMA 2000 model.

260. The critical third parties designation process in new section 312L is modelled on the procedure in the Banking Act 2009 for designating payment systems. Under section 184 of the Banking Act 2009, HM Treasury may, by order, designate payment systems, which then fall under the supervision of the Bank of England as set out in Part 5 of that Act.

Justification for the procedure

261. The power in new section 312L does not bring an entity into full supervision by the financial authorities, but does allow the financial authorities to oversee the services provided to regulated finance sector firms by a designated critical third party. It similarly requires HM Treasury to have regard to fixed criteria when designating third parties as critical. It therefore follows the precedent set by the Banking Act 2009, which is the closest comparable regime in financial services legislation.

New section 312M of FSMA 2000 (Power to make rules).

Power conferred on: the FCA, Bank and the PRA
Power exercised by: rules made in accordance with Part 9A of FSMA 2000, as modified
Parliamentary Procedure: none

Context and Purpose

262. The context for this power is the same as that set out for new section 312L.

263. This power enables the relevant regulator (the FCA, Bank or the PRA) to make rules about the services that critical third parties provide to regulated finance sector firms.

Justification for taking the power

264. This power represents a targeted extension of the financial services regulatory regime to the services provided by critical third parties to the sector. Pursuant to the FSMA 2000 model, the setting of detailed, technical rules for these services is for the regulators rather than for Parliament or HM Treasury.

265. Further, the use of the power is constrained by the usual requirements relating to transparency and acting in accordance with regulators' objectives.

Justification for the procedure

266. It is considered that no Parliamentary oversight is required in relation to the exercise of this power because it represents an extension of the regulators' existing rule-making powers to manage an emerging risk. In that context, the relevant regulator is exercising the rule-making power on the basis of the framework set out in FSMA 2000 and will be subject to the accountability requirements of the Act.

New section 312N of FSMA 2000 (Power of direction).

Power conferred on: the FCA, Bank and the PRA
Power exercised by: direction
Parliamentary Procedure: none

Context and Purpose

267. The context for this power is the same as that set out for new section 312L.

268. This power enables the relevant regulator (the FCA, Bank or the PRA), where it appears to the regulator to be necessary or expedient considering its objectives (as described in the new section 312M), to direct a critical third party to do (or not do) something in relation to the provision of services to regulated financial services firms. Pursuant to new section 312O(3), if the relevant regulator considers it necessary, it may use this power to issue a direction that has immediate effect.

269. A regulator issuing a direction must give notice to the relevant critical third party. This notice is designed to provide key information to the critical third party to whom the direction is made, including information about;

a. the reasons for the direction;
b. the critical third party's rights to make representations to the regulator, and
c. the critical third party's rights to appeal against the direction to the Tribunal.

Justification for taking the power

270. If the action or inaction of a critical third-party provider could lead to systemic financial stability or market confidence risks, it is appropriate for the relevant regulator to be able to direct that critical third party to do (or not do) something in relation to the services it provides to the financial services sector. The intention would be to mitigate the possible risk posed by that provider to the sector.

271. The power to issue directions is subject to the normal procedural protections associated with such powers, including:

a. requiring the regulator to set out the reasons for making the direction (per new section 312O(4)(b));
b. allowing the affected critical third party the right to make representations to the regulator about the appropriateness of the direction, and then requiring the regulator to review the continuation of the direction in light of the representations (per new section 312O(4)(c) and 312(6));
c. creating a right of appeal to the Tribunal for affected critical third parties against the direction (per new section 312O and new section 312S).

Justification for the procedure

272. There is no Parliamentary procedure, as is usual for the exercise of statutory powers by a financial services regulator to take the form of a direction, instruction or prohibition (see, for example, powers to give direction in sections 192C, 257, 261X and elsewhere in FSMA 2000). The FCA, Bank and the PRA are given these powers to exercise as part of their day-to-day supervisory and enforcement activities as regulators. Parliamentary procedure would be inappropriate and would prevent the relevant regulator from making decisions regarding individual entities in a timely manner.

273. The use of this power is subject to the usual requirements in relation to powers to make directions, including:

a. a requirement to set out reasons;

b. a right for an affected critical third-party provider to make representations to the regulator issuing the direction and for the regulator to consider whether, in light of those representations, the direction should either come into effect or continue in effect (if it was made with immediate effect); and
c. a right to appeal against the direction to the Tribunal.

Financial Promotions

Clause 20: Financial promotion

- New section 55NB of FSMA 2000 (Section 55NA: power to provide for exemptions).

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative procedure under s.429 FSMA 2000

Context and Purpose

274. Under section 21 of FSMA 2000, no invitation or inducement to engage in investment activity or claims management activity may be communicated, unless: (i) it is by an authorised person; (ii) the content of the communication has been approved by an authorised person; or (iii) an exemption under FSMA 2000 (Financial Promotion) Order 2005[25] applies. In connection with content of a communication being approved by an authorised person, the aim of clause 20 is to improve the quality of financial promotions communicated by unauthorised persons and to give the FCA greater oversight of the authorised firms approving financial promotions. As a result, consumer protection outcomes will be strengthened.

275. Section 21 of FSMA 2000 will be amended to insert the new subsection (2A), with the effect that FCA authorised persons will be unable to approve financial promotions unless they are either permitted to do so by the FCA (via a financial promotions gateway under the new section 55NA) (following consultation with the PRA or the Gibraltar regulator, where appropriate), or if an applicable gateway exemption applies (under the new section 55NB). The new section 55NA will be inserted into Part 4A of FSMA 2000. This will impose a new, general requirement on all Part 4A-authorised firms not to approve a financial promotion for the purposes of section 21, unless permission to do so has been given by the FCA.

Description of the powers

276. The new section 55NB, which will also be inserted into Part 4A of FSMA 2000, confers a delegated power on HM Treasury to create exemptions to the new section 55NA gateway requirement. The specific gateway exemptions will be set out in regulations made by HM Treasury.

277. This power will enable HM Treasury to make provision for specific gateway exemptions to have effect in respect of:
   a. specified persons;
   b. persons falling within a specified class;
   c. approvals given in relation to activities of a specified description;
   d. in specified circumstances; or
   e. subject to specified conditions.

[25] S.I. 2005/1529.

Justification for taking the power

278. HM Treasury has considered that there are likely to be cases where it would not be reasonable or proportionate for certain persons or circumstances to be subject to this financial promotion gateway process.

279. In light of the FCA's commitment to supervising authorised firms holistically, HM Treasury will seek to create gateway exemptions to take account of the interconnections between authorised persons and their associated unauthorised persons, rather than seeking to impose a blanket obligation on authorised firms to comply with the new section 55NA requirement. In some cases, where appropriate, these interconnections will reduce the need for permission under the gateway and related costs. This power will allow for gateway exemptions for authorised persons and is intended to have sufficient flexibility to allow for future gateway exemptions, as it is expected that further possible candidates for exemption may emerge as the market changes.

280. HM Treasury considers that the power to create exemptions from regulatory requirements is a crucial element in setting the perimeter for the regulator's powers and that this power is a reflection of the distribution of responsibilities under the FSMA 2000 model.

Justification for the procedure

281. It is considered appropriate that any regulations made using these powers are subject to the negative procedure.

282. This power is only exercisable for specific purposes. It does not seek to broaden the scope of the new requirement. Rather, it is intended to be exercised in such a way that narrows the scope of the new requirement (thereby, returning persons to the status quo). In these circumstances, providing for an exemption from the new section 55NA general requirements, the negative procedure is appropriate.

Digital Settlement Assets

Clause 21, Schedule 6 and clause 22: Digital settlement assets

Powers conferred on: HM Treasury
Powers exercised by: order made by statutory instrument
Parliamentary Procedure in each case: affirmative

Context and Purpose

283. The two clauses, 21 (digital settlement assets) and 22 (digital settlement assets: power to make regulations), and the associated Schedule 6 (digital settlement assets) together allow for the creation of a regulatory regime for the use of digital settlement assets (DSAs) as a form of payment.

284. Digital settlement assets are digital representations of value or rights (which may or may not be cryptographically secured) which can be used for the settlement of payment obligations. These clauses and the Schedule will, accordingly, allow for the use of certain cryptoassets (where HM Treasury decides this is appropriate) within the regulatory regimes for the electronic money and payments (which is principally located in secondary legislation) as well as making amendments to certain regulatory regimes within primary legislation.

285. These clauses drive forward the agenda outlined above of ensuring that the United Kingdom is at the forefront of developing new technologies and products in financial services.

Clause 21 and Schedule 6 (Parts 1 and 2)

286. Clause 21 (digital settlement assets) introduces Schedule 6 (digital settlement assets). Part 1 of Schedule 6 makes amendments to Part 5 of the Banking Act 2009, which gives the Bank of England regulatory powers in order to mitigate or manage financial stability risks in payment systems, where the payment system has been recognised as systemic by HM Treasury. Part 2 of Schedule 6 makes amendments to Part 5 of the Financial Services (Banking and Reform) Act 2013 ("FSBRA"), which provides for the regulatory powers of the Payment Systems Regulator in relation to payment systems designated by HM Treasury.

287. The amendments made by Part 1 of Schedule 6 expand the definition of "payment system" within that Part to include those that use DSAs. Other consequential amendments are then made to accommodate the differences between systems using DSAs and more traditional payment systems (those which are currently regulated). This has necessitated the inclusion of new clauses covering those who are service providers connected to a DSA payment system.

288. Further, HM Treasury considers that it would be possible for the service provider using DSAs (such as a wallet) to become systemic, and therefore suitable for regulation by the Bank under Part 5 of the Banking Act 2009, where it is not tied to a particular payment system. Consequently, amendments are included allowing for a category of stand-alone

DSA service providers to be recognised where they could cause financial stability risks to the UK financial system.

289. The scope of the amendments made by Part 1 of Schedule 6 is essentially set by the new section 182(4A) of the Banking Act 2009, which defines "digital settlement asset", and new section 182(5A), which defines a "DSA service provider".

Power to amend and justification

290. Digital settlement assets and DSA service providers are new concepts and a new market which are subject to rapid innovation at a scale. This has the potential to affect financial stability and consumer rights. Because of this HM Treasury considers it appropriate to take a power to amend the definitions should this be necessary in such a swiftly developing market. Accordingly, clause 21 and paragraph 4 of Schedule 6 insert into the Banking Act 2009 a new section 182(5C) which allows HM Treasury to amend, by way of regulations under the affirmative procedure, those two new definitions. A similar provision to amend the new definition of DSAs in FSBRA, in section 41(2C) of FSBRA, is included at paragraph 39(2) of Part 2 of Schedule 6.

291. Together clause 22 and Schedule 6 provide a holistic approach to the regulation of DSAs within payments. Clause 22 allows for the updating and creation of legislation to create a new framework for DSAs used in payments, similar to that for electronic money and existing payment services. Schedule 6 amends key provisions in relation to the management of risks potentially caused by payment systems in Part 5 of the Banking Act 2009 and Parts 5 and 6 of FSBRA, so that these can cover DSAs.

Digital settlement assets: power to make regulations

292. Clause 22 enables HM Treasury to legislate by way of affirmative regulations for the purposes of regulating payments that include DSAs, DSA recognised payment systems and DSA service providers. This includes provision to (i) apply or modify legislation (including primary legislation), (ii) confer powers on HM Treasury to legislate further in this area, (iii) confer powers or impose duties on relevant regulators (including to make appropriate rules, but not including a power to legislate), (iv) make provision on fees payable to a regulator, v) about recognition orders and criteria in Part 5 of the Banking Act 2009 and (vi) cover enforcement and information sharing. Clause 22(4) confirms that this includes provision to create offences, which are in line with similar offences in the existing legislative framework.

293. It is initially envisaged that this power to make regulations would be used for the following matters:

a. To amend, replace or make separate provision to existing payments (Payment Services Regulations 2017 "PSR 2017"[26]) and electronic money (Electronic Money Regulations 2011 "EMR 2011"[27]) legislation to make appropriate provision for

[26] S.I. 2017/752.

[27] 2011/99.

stablecoins that are used for payment. Stablecoins are a type of DSA that aims to maintain a stable value in relation to another asset and in the first instance would be those that are related to a fiat currency (such as the Pound Sterling). However, this could be expanded in the future, if considered appropriate to cover other forms of DSAs as the market evolves.

b. To manage the potential overlap where an existing firm regulated by the FCA under either the EMR 2011 and the PSR 2017 is recognised as systemic – such that it is also regulated by the Bank in relation to financial stability risks under Part 5 of the Banking Act 2009. Certain provisions in either of the EMR 2011 or the PSR 2017 (or other payments related legislation) may limit the ability of the Bank to perform its regulatory role under Part 5 of the Banking Act 2009. The power in clause 22 would allow for the disapplication or modification of existing provisions in the EMR 2011 or PSR 2017 and Banking Act 2009 where such overlaps occur – see clause 22(3)(a) and (5) in particular. This is complemented by clause 22(3)(c) to (e), which confirm that such powers include conferring powers or imposing duties on a relevant regulator. This power is necessary in order to provide a coherent regulatory framework.

c. To amend or modify the Financial Markets Infrastructure Special Administration Regime ("FMI SAR") provisions in Part 6 of FSBRA, so that it can be used effectively to mitigate the risks in an insolvent operator of a recognised DSA payment system or a recognised DSA service provider. Clause 22(1)(c) expressly states that such powers are to include the making of insolvency arrangements with respect to such entities. Subsection (3)(b) of clause 22 capture the power to apply legislation relating to insolvency arrangements and interactions between such arrangements with appropriate amendments. These powers are necessary so that HM Treasury can put in place an appropriate regime and to allow it to be amended as different, and likely novel, forms of market participants emerge.

294. Clause 22, paragraphs (5) and (6), gives HM Treasury the general power to amend the definition of DSAs within that clause. This power is necessary in order to respond to changes in the features, underlying technology and usage of these assets in the future. There are similar powers to amend equivalent definitions to be inserted into the Banking Act 2009 and FSBRA by Schedule 6 of this Bill – mentioned above.

295. Clause 22(3)(c) confers on HM Treasury the power to amend primary legislation as considered necessary to make workable the regulatory regimes envisaged in the above. For instance, this could be used to create a power to put in place detailed insolvency rules by statutory instrument in order to engage necessary amendments to the FMI SAR as considered above.

Justification for taking the powers and the procedure

296. The extent of the regulatory power is required, including the power to amend the definition of DSAs, in order to ensure that regulation in this developing area is agile. HM

Treasury considers it likely that it may need to react urgently to the very new and fast-evolving cryptoasset market, and in the interests of protecting consumers. This could include amending the definition of DSA, in order to keep pace with evolving and innovative technologies, and with market features being introduced rapidly. The power to create offences is needed to bolster an effective enforcement regime, and to encourage compliance with a new regulatory regime for payments which include these novel types of assets. The types of offences that can be created are in line with those in the existing legislation governing payments.

297. HM Treasury also believes that detailed legislative changes would be best delivered through secondary legislation rather than by way of primary legislation, and considers that the allocation of responsibilities between parliament, HM Treasury and the regulators accords with the FSMA 2000 model. However, HM Treasury considers that Parliament is given appropriate oversight through the use of the affirmative procedure for such legislation. Where HM Treasury considers it necessary for the regulations to come into force without delay, regulations are subject to the made affirmative procedure. This ensures that the government is able to respond flexibly given the potential to act urgently to market developments, but within a framework for Parliamentary oversight, consultation requirements and timescales as appropriate.

298. The legislation also includes a duty on HM Treasury to consult the FCA and the Bank before making legislation in all cases under the power in clause 22. Similarly, there is also a duty on HM Treasury to consult the Payment Systems Regulator where proposed regulation affects them. This is to ensure that the views of the financial regulators closest to this market are taken into account appropriately before legislation is made.

Mutual recognition

Clause 23: Implementation of Mutual Recognition Agreements

- New provision conferring powers on HM Treasury for the purpose of, or in connection with, implementing any financial services mutual recognition agreement to which the UK is, or is expected to become a party.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

299. The government is taking forward an ambitious international financial services agenda, which includes agreeing mutual recognition agreements (MRAs) with overseas jurisdictions. When the UK was a member of the European Union, the EU was responsible for recognition with other jurisdictions and setting some parameters for trade. The European Commission conferred this access through its equivalence mechanisms. Outside of the EU, the UK is able to negotiate its own international agreements in areas previously within the competence of the EU, including MRAs.

300. These financial services MRAs are intended to provide recognition of rules and practices in other jurisdictions to allow both the UK and its MRA partners to defer to each other in respect of the regulation and supervision of both UK and overseas firms undertaking cross border financial services activity. MRAs therefore offer a practical way to promote openness and mutual market access between jurisdictions, supported by regulatory and supervisory cooperation. In June 2020, the Chancellor and his Swiss counterpart committed to negotiate a comprehensive MRA to improve cross-border access for financial services. Changes may be required to domestic legislation so that this agreement and future MRAs can be fully implemented.

301. The UK has a dualist legal system. This means that a treaty ratified by the government does not alter the laws of the State unless and until it is incorporated into domestic law by legislation. Consequently, international agreements, such as MRAs, must be implemented into domestic law in order to ensure that the UK can meet its international obligations within such an agreement and to ensure that UK firms can benefit from their terms. This does not mean that all obligations within an MRA will require a change to the law, but it is a convention in the UK that an international treaty is not ratified until it has been properly implemented.

302. The Bill will provide HM Treasury with the power to make the changes to domestic legislation necessary to ensure that MRAs can be fully implemented, including granting any additional powers to, or impose duties on, the financial services regulators to give effect to MRAs as required, in the context of the relevant regulator's obligations in FSMA 2000 with respect to advancement of its statutory objectives. Without this power, the UK may be unable to fully meet its obligations under the MRAs it negotiates. This power also allows for amendments to be made to domestic legislation to take account of any subsequent

changes to MRAs as and when the UK and its MRA partners agree to amend an agreement such as by extending the scope of a MRA to cover additional financial services sectors.

Justification for taking the power

303. As with any treaty which the UK enters into, HM Treasury will need to go through a process of ensuring that our domestic legal framework is in compliance with the obligations which the UK enters into under an MRA and that both HM Treasury and the regulators have the powers needed to give effect to its provisions. To the extent that it is determined that UK law must be amended in order to meet those obligations and deliver the effects envisaged by the treaty, the UK's legislative framework will need to change. As a matter of course, this process must be completed before the UK ratifies such an agreement, so as to ensure that it can fully comply with its obligations when the treaty enters into force.

304. Provision which may be made pursuant to this power is limited to what is appropriate for the purpose of, or in connection with, implementing mutual recognition agreements to which the UK is or is expected to become a Party. This power is separate to the process in section 20 of the Constitutional Reform and Governance (CRaG) Act 2010.[28] Any MRA to which this power relates will also be subjected to the CRaG Act process and the text of the agreement laid in Parliament. Any regulations made pursuant to the power would be subject to the affirmative procedure.

305. In respect of the proposed MRA with Switzerland, the precise nature and scope of the obligations to which the UK may commit remains dependent on final negotiations, although negotiations are progressing, and the Parties have largely reached agreement on a joint understanding of its likely parameters. The power to implement the MRA will need to be in force prior to or as soon as possible following the conclusion of negotiations to allow for any secondary legislation needed to implement the treaty under the power to be prepared and laid before Parliament as soon as possible thereafter. The power has been drafted to be sufficiently broad to implement the UK-Switzerland MRA, and any future MRAs, efficiently.

306. These MRAs are intended to cover a broad range of sub-sectors governed by different and complex regulatory regimes, and so the modifications to domestic law which may be necessary for implementation will vary by sector. They are also intended to be dynamic agreements which will be updated over time to expand or alter their scope and add new sectors, subject to the institutional and governance provisions of the agreements. In this context a broad power is desirable to ensure there is sufficient flexibility to make the necessary changes to domestic law in each sector, and to further update the domestic framework over time.

Justification for the procedure

[28] Constitutional Reform and Governance Act 2010 c.25.

307. As noted above, the MRAs that this power is intended to implement will be subject to parliamentary scrutiny under section 20 of the CRaG Act in addition to parliamentary scrutiny of any implementing legislation.

308. The precise scope of these MRAs is currently uncertain, as negotiations are ongoing with Switzerland in respect of the first such agreement which is likely to set a blueprint for future agreements. Given this, and that the power can be used to amend primary legislation or retained direct principal EU legislation, HM Treasury is of the view that the affirmative procedure is appropriate to ensure adequate opportunity for parliamentary debate and scrutiny.

Accountability of regulators

Clause 27: Review of Rules

- New section 3RC of FSMA 2000 (Review of rules)

Power conferred on: HM Treasury
Power exercised by: direction
Parliamentary Procedure: none

Context and Purpose

309. The Bill extends the regulators' rule-making powers and responsibilities.

310. The government considers that it is important to review policy interventions after implementation, including interventions delivered through regulators making rules which impose obligations on firms. This review process ensures that the intervention remains appropriate and has the desired effect. This can range from monitoring to wider evaluation of the impact of a rule after a certain period. This process of regular and predictable review of rules is important for building confidence amongst stakeholders.

311. The Bill introduces into FSMA 2000 new section 3RA which imposes a general requirement on the regulators to review their rules, other than rules made in order to comply with a recommendation or direction issued by the Financial Policy Committee of the Bank ("FPC"). However, the regulators have discretion as to how and when they review their rules to determine whether they function as intended. As the regulators' take on increased rule-making powers and responsibilities, HM Treasury considers that there may be instances where it is in the public interest to require the regulators to review their rules outside the normal review process in order to assess whether the rules are working as expected. For example, where there has been a significant change in market conditions, or other evidence suggests that the relevant rules are no longer acting as intended, it may be in the public interest to review the related rules earlier or more comprehensively than the regulator would otherwise have intended.

312. Accordingly, clause 27 introduces into FSMA 2000 new section 3RC which provides that if HM Treasury considers it to be in the public interest that certain rules, which have been in force for a period of at least 12 months, are reviewed and either (i) the regulator is not going to otherwise undertake a review of the relevant rules, or (ii) if a regulator is going to undertake a review the proposals are not appropriate for the purposes of carrying out an effective review, then HM Treasury may by direction require a regulator to carry out a review. This power will enable HM Treasury to direct the regulators to review a specific rule or group of rules, but is limited to the same rules that can be reviewed by the regulators under new section 3RA.

313. This power will be exercised only where HM Treasury identifies that it is in the public interest for the regulator to review its rules, for example, a significant change in market conditions or other evidence suggests that the relevant rules are no longer acting as intended. If the regulator has already conducted a review, the power will enable HM

Treasury to direct the regulators to conduct a further review of the same rules if new evidence comes to HM Treasury's attention and it is in the public interest to carry out a further review.

Justification for Taking the Power

314. The Bill will increase the scope of the regulators' rule-making powers and responsibilities in several aspects. It is important for effective regulation that the regulators' rules function effectively and that HM Treasury maintains oversight of this. Whilst the Act requires the regulators to keep their rules under review, the power for HM Treasury to direct the regulators to conduct a review of their rules where a review is in the public interest will ensure that there is an appropriate avenue of challenge to ensure the rules continue to function effectively.

315. The direction will only be used in exceptional circumstances and HM Treasury will consult with the regulator before issuing a direction. In addition, it is HM Treasury's view that this power is not legislative in character: the power does not result in HM Treasury exercising any power to make rules, nor does it require the regulators to make rules as a consequence of the exercise of the power. Where the regulators do decide, as a consequence of the review, to change their rules then this will be done pursuant to an existing rule-making power or one of the new rule-making powers conferred under this Bill and subject to assessment elsewhere in this document. Accordingly, this power does not create a free-standing or new power which is legislative in character.

316. Further, and pursuant to new section 3RC(4) HM Treasury must have regard to the desirability to minimising any adverse effect that the carrying out of a review will have on the exercise of the regulator of any of its other functions.

317. In order to ensure transparency over the exercise of this power of direction, HM Treasury will, pursuant to new section 3RC(7) publish the direction in such manner as it sees fit and also lay a copy of the direction before parliament.

Clause 28: Treasury powers in relation to rules

- New section 3RE of FSMA 2000 (Power to require the making of rules).

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure

Context and Purpose

318. Clause 28 introduces new section 3RE into FSMA 2000 which includes a power that enables HM Treasury to place obligations on the regulators to make rules in relation to specific matters or to specified descriptions of people. This power allows HM Treasury to create obligations on regulators, much as primary legislation has previously done. For instance, section 143C of FSMA 2000 (introduced pursuant to Schedule 2 to the Financial

Services Act 2021), pursuant to which the FCA is obliged to make rules in relation to certain matters.

319. Under the power, HM Treasury may specify the matters that the rules must cover, matters that the regulator may or may not have regard to when making rules and the time period within which the rules must be made. The power is constrained by subsection (4) by preventing HM Treasury from requiring the regulators to make rules in a specified form or to advance a specified outcome.

Justification for taking the power

320. The Financial Services Act 2021, which inserted Part 9C into FSMA 2000, is a recent example of legislation that requires the regulators to make rules covering certain issues, and may specify matters which the relevant regulator should have regard when making rules, in addition to the general requirements in FSMA 2000 which govern all rule-making.

321. This power is based on this model, which will enable the government to ensure that more specific public policy priorities can be reflected in regulator rule-making where appropriate. While the UK was a member of the EU, and a significant amount of legislation was negotiated in Brussels, the government could ensure that the necessary rules were in place. Under the FSMA 2000 model, the regulators must act as they consider appropriate to advance their statutory objectives – limiting the extent to which any wider public policy issues, not covered by their statutory objectives, can be considered. When retained EU law is repealed, this power would enable HM Treasury to create a requirement for a regulator to make similar rules, otherwise it may not be replaced.

322. HM Treasury recognises that section 143C imposes an obligation to make rules in relation to certain matters but does not prescribe the outcomes which those rules must deliver. HM Treasury considers this to be an important protection for the independence of the regulators. It is appropriate that the regulators should be required to make rules to cover certain matters, but the regulators should be free to determine the content of those rules. Accordingly, paragraph(3) expressly prevents HM Treasury from using this power to prescribe the content or form of rules made pursuant to any requirement to make rules imposed under clause 28, or to require a regulator to advance a specified outcome.

Justification for the procedure

323. It is considered appropriate that the power should be subject to affirmative procedure to reflect both the permanence and strength of the power and to provide Parliament with the opportunity for full scrutiny and debate.

Clause 29: Matters to consider when making rules

- New section 138EA of FSMA 2000 (Matters to consider when making rules).

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument

Parliamentary Procedure: affirmative procedure

Context and Purpose

324. The power in clause 29 enables HM Treasury to require the regulators, when they are making their rules, to "have regard" to matters specified by HM Treasury. The purpose of this power is to enable the government to ensure that more specific public policy priorities can be reflected in regulator rulemaking, where it considers that appropriate.

325. Accordingly, section 138EA of FSMA 2000 permits HM Treasury by regulations (made by statutory instrument) to specify matters that the regulators must consider when making rules including by reference to the power under which the rules are made, the persons to whom the rules apply and the activities or subject matter to which the rules relate.

326. The power is constrained in that it does not apply where regulators make rules for the purposes of complying with a direction made by the FPC under section 9H of the Bank of England Act 1998 or acting in accordance with a recommendation made by that committee under section 9Q of that Act.

327. The regulators when consulting on rules under sections 138I and 138J of FSMA 2000 will be required to provide an explanation of the ways the "have regards" specified under section 138EA has affected the proposed rules unless the regulators consider compliance to be prejudicial to their objectives (safety and soundness, interest of consumers and policyholder protection) or where the rules involve change to existing rules to no material effect.

Justification for taking the power

328. While the UK was a member of the EU, and a significant amount of legislation was negotiated in Brussels, the government could ensure that the public policy priorities were in place. Under the FSMA 2000 model, the regulators must act as they consider appropriate to advance their statutory objectives – limiting the extent to which any wider public policy issues, not covered by their statutory objectives, can be considered. This power therefore enables HM Treasury to set public policy priorities which the regulators must consider when making rules in particular areas.

329. The Financial Services Act 2021, which inserted Parts 9C and 9D into FSMA 2000, is a recent example of legislation specifying matters which the relevant regulator should have regard when making rules, in addition to the general requirements in FSMA 2000 which govern all rulemaking. However, section 144C of FSMA 2000 has a limited remit and applies to a closed and specified set of rules. It also provides a limited set of matters to which regulators must have regard when making rules.

330. It is not currently possible to provide a similar closed and specified set of rules to which the "have regards" should apply in relation to other financial services files. This is because the perimeter to which the regulator rule-making powers will apply will be determined by

secondary legislation (made pursuant to other powers prescribed in the Bill) and which will only be set following further consideration by HM Treasury and the regulators. Further, until the secondary legislation which will set the perimeter is drafted, it is not possible to identify the appropriate set of matters to which the regulators must have regard when exercising their rule-making powers. Accordingly, HM Treasury considers that it is appropriate to take a power to allow for HM Treasury to set "have regards" by way of secondary legislation at the same time as it transfers responsibility to the regulators.

Justification for the procedure

331. It is considered appropriate that the power should be subject to affirmative procedure to reflect both the permanence and strength of the power and to provide Parliament with the opportunity for full scrutiny and debate.

Clause 32: Power to disapply or modify rules

- New section 138BA of FSMA 2000 (Disapplication or modification of rules in individual cases).

Power conferred on: HM Treasury
Power exercised by: rules
Parliamentary Procedure: affirmative

Context and Purpose

332. Clause 32 inserts new section 138BA into FSMA 2000. This section of FSMA 2000 creates a power for HM Treasury to provide for specific modification and disapplication regimes to regulator rules.

333. This would enable the PRA and the FCA to identify parts of their rules which can be modified or disapplied upon application or consent. Within this, subsection (1) of new section 138BA of FSMA 2000 states that new section 138BA only applies to rules made by a regulator if, or to the extent that, HM Treasury provides for it to apply. This means that new section 138BA only applies if the power is exercised.

334. Subsection (6) enables HM Treasury, when exercising the power in subsection (1), to also provide for procedural provisions to govern each modification and waiver regime. In particular, this would enable HM Treasury to make provisions about how firms can apply for such waivers, and how to withdraw their consent.

Justification for power

335. Clause 1(1) of the Bill repeals retained EU law in financial services. This means that, where the regulators make rules to replace parts of retained EU law, the modification and disapplication of those rules will be governed by section 138A of FSMA 2000. This section sets out that the regulators can only modify or disapply their rules subject to conditions, in particular to the condition in subsection (4)(a) of that section, which requires compliance

by the person with the rules, or with the rules as unmodified, would be unduly burdensome or would not achieve the purpose for which the rules were made.

336. There are a number of different waiver and modification regimes in retained EU law which are not compatible with section 138A of FSMA 2000. For example, Article 18 of the Prospectus Regulation. It is for this reason that the Financial Services Act 2021 inserted section 144G into FSMA 2000, which created a new modification and waiver regime for certain rules which the PRA makes to replace parts of the Capital Requirements Regulation.

337. The ability for the regulators to enable the modification and disapplication of rules is an important tool, as it enables rules to be properly calibrated to the firms to which they apply. The new power inserted by clause 32 enables HM Treasury to make similar provisions in other areas.

338. This power sits alongside the existing section 137A and enables HM Treasury to create bespoke modification and disapplication regimes in certain areas, including where necessary to replace those in retained EU law. This needs to take the form of a power, as a specific modification and disapplication regime needs to be calibrated to the particular policy area in which it operates, (for example, application processes could be different depending on the different types of firms likely to apply), and so it is necessary for HM Treasury to set out this detail in secondary legislation.

Justification for procedure

339. As this power will have the effect of modifying the effect of section 138A of FSMA 2000, which would otherwise apply, affirmative procedure is appropriate.

Clause 37: Reporting Requirements

New paragraph 11A of Schedule 1ZA to FSMA 2000 (Other reports)

Power conferred on: HM Treasury
Power exercised by: direction
Parliamentary procedure: none

Context and Purpose

340. In order to increase the transparency around the work conducted by the FCA under the regulatory framework, at least once per year, the FCA must make a report to HM Treasury. This report must include information relating to a number of different topic areas which are detailed in paragraph 11 of Schedule 1ZA to FSMA 2000. Alongside the topic areas specified in paragraph 11, paragraph 11 includes a power for HM Treasury to direct the FCA to include information on such other matters as specified by HM Treasury. HM Treasury must lay the report received from the FCA before Parliament.

341. Whilst this report continues to serve its purpose of improving transparency, the expanding nature of the FCA's duties and functions means it may be appropriate to ask them to report more regularly. New paragraph 11A gives HM Treasury the power to direct the FCA to publish a report containing information about any of the matters in paragraphs

(a) to (ia) of paragraph 11(1) of Schedule 1ZA to FSMA 2000 together with such other matters that the direction may specify. Sub-paragraphs (a) to (ia) include matters such as the extent to which the FCA's operational objectives have been advanced, it has acted compatibly with its strategic objective and it has considered its regulatory principles in section 3B of FSMA 2000. New paragraph 11A is designed to give HM Treasury the power to direct the FCA to provide information on an ad hoc or more regular basis such that the public are informed as topic areas develop rather than in the annual report which could be provided to HM Treasury many months after an issue is topical. Such reports may also assist Parliament in holding the FCA to account.

Justification for the power

342. It is HM Treasury's view that the changed environment of financial services, in particular the shift from an EU model where technical requirements on firms are contained in legislation to an approach where the regulators generally set requirements via regulator rules, means that a power of this nature is necessary. HM Treasury expects that it will only be used in exceptional circumstances, in cases where existing forms of engagement have been exhausted. It provides a backstop to ensure that the regulators can be directed to provide further information on their performance where required while respecting their operational independence and expertise. The power is intended to accommodate circumstances where there is a specific need for HM Treasury, and the general public, to be provided with information by the FCA at the point in time when this information is most topical or when data is required more often than annually. This will enable HM Treasury to be agile in its approach to policymaking as it will have up to date information from the FCA. It will also support the FCA's accountability to Parliament and the public.

343. New paragraph 11A will enable HM Treasury to direct the FCA to provide further clarity on how it has discharged its general duties including acting compatibly with its strategic objective, advancing its operational objectives and taking into account the regulatory principles and how the FCA is performing against various service levels, for example, standards and timelines of operational performance.

Justification for the process

344. To facilitate parliamentary scrutiny of the use of the power, HM Treasury will be required to lay the direction before Parliament and publish the direction. It is appropriate that the power is exercised by way of a direction because this will allow HM Treasury to react quickly if information about a topic is required. The power is also limited in nature. It only requires the FCA to publish a report on a particular matter. This approach is consistent with that taken in paragraph 11(1)(j).

New paragraph 21A of Schedule 1ZB to FSMA 2000 (Other reports)

Power conferred on: HM Treasury
Power exercised by: direction
Parliamentary procedure: none

345. New paragraph 21A of Schedule 1ZB replicates the power for HM Treasury to direct the FCA on matters specified by HM Treasury but applies the power to the PRA.

346. The purpose and justification for new paragraph 11A of Schedule 1ZA to FSMA 2000 applies equally to this power for the PRA.

Clause 44: Composition of Panels

New section 1MA of FSMA 2000 (Composition of Panels)

Power conferred on: HM Treasury
Power exercised by: Statutory Instrument
Parliamentary procedure: Negative Procedure

Context and Purpose

347. The FCA is required to make and maintain effective arrangements for consulting practitioners and consumers on the extent to which its general policies and practices are consistent with its general duties. In order to satisfy this requirement, the FCA has a number of statutory panels. These panels are established under sections 1N to 1QA of FSMA 2000 and section 138IA of FSMA 2000.

348. The FCA appoints the members of its statutory panels but HM Treasury must approve the appointment of the Chairs of each of the panels. In general, panel members are external to the FCA though some are paid for their work on a panel. For example, this is the case for members of the FCA's Consumer Panel.

349. New section 1MA(1) of FSMA 2000 has the effect that members of a statutory panel of the FCA must not receive remuneration from the FCA, the PRA, the PSR, the Bank of HM Treasury. This is to enhance the independence of the panels. However, HM Treasury considers that it is appropriate to have certain exemptions from this position to reflect the different memberships of the panel. New section 1MA(2) of FSMA 2000 provides that the disqualification in subsection (1) does not apply where HM Treasury have made regulations under subsection (3).

350. Subsection (3) provides that HM Treasury may make provision to disapply subsection (1) in respect of a panel generally or in relation to such descriptions of persons or cases. In some cases, while remaining external, it is appropriate for panel members to receive remuneration. For example, to ensure that the panels continue to attract a diverse range of experts, it may be appropriate for panel members to received remunerations for their work on the panel or other ad hoc work on specific projects. The power does not allow HM Treasury to specify persons by name in the regulations. The effect of this power will enable HM Treasury to, for example, provide for all members of a panel to be remunerated or for a minority of members of a given panel to be remunerated.

Justification for taking the power

351. It is HM Treasury's view that it is important for the statutory panels of the FCA to be comprised, in some form, of people who are independent from the FCA, the PRA, the PSR, the Bank and HM Treasury. This clarifies the role of the panels as being independent from the FCA and enhances the scrutiny of the FCA's policymaking.

352. The composition of the panels is not fixed or permanent as panel members serve terms. A member can be re-appointed at the end of their term but the number of times the member is re-appointed is limited by Terms of Reference. As such, HM Treasury needs to have the flexibility to re-consider exemptions from the disqualification provision in new section 1MA(1) of FSMA 2000. The power to specify, via statutory instrument, categories of people who are exempt from new section 1MA(1) will mean that the most appropriate people are members of a panel at any particular time to ensure the effectiveness of the panels' work.

Justification for the procedure

353. The statutory instrument will be subject to the negative procedure. The power will not be used to amend legislation; it will only have an effect on the FCA in appointing members to its panels.

New section 2LA of FSMA 2000 (Composition of Panels)

Power conferred on: HM Treasury
Power exercised by: Statutory Instrument
Parliamentary procedure: Negative Procedure

Context and Purpose

354. New section 2LA of FSMA 2000 replicates the power in new section 1M(1) so that it applies to the composition of PRA's statutory panels. HM Treasury can provide, by regulations, for an exemption from the disqualification of panel members from being remunerated by the FCA, the PRA, the PSR, the Bank or HM Treasury.

355. The purpose and justification for new section 1MA(2) of FSMA 2000 applies equally to the power in new section 2LA(2) in relation to the PRA's statutory panels.

Bank of England Regulatory Powers

Clause 46: Bank of England: rule-making powers

New section 300K of FSMA 2000 (Requirement to review specified rules).

Power conferred on: HM Treasury
Power exercised by: direction
Parliamentary Procedure: none

356. Please see the entry for clause 27. Clause inserts section 300K into FSMA 2000 which makes equivalent provision for the Bank of England in relation to its rules governing central counterparties and central securities depositories.

New section 300M of FSMA 2000 (Power of Treasury to require making of rules by regulations)

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure

357. Please see the entry for clause 28. Clause 46 inserts section 300M into FSMA 2000 which makes equivalent provision in respect of the Bank of England's rules governing central counterparties and central securities depositories.

Clause 47: Application of FSMA 2000 to FMI functions

New paragraph 33A of Schedule 17A to FSMA 2000

Power conferred on: HM Treasury
Power exercised by: direction
Parliamentary procedure: none

358. New paragraph 33A of Schedule 17A applies, with modifications of paragraph 21A of Schedule 1ZA to FSMA 2000 to the Bank of England in its regulation of central counterparties and central security depositories.

359. The purpose and justification for new paragraph 33A of Schedule 17A to FSMA 2000 applies to this power for the Bank of England.

Amendment to Schedule 17A to FSMA 2000 (further provision in relation to exercise of Bank of England functions under Part 18 of that Act) to apply the new section 138BA of FSMA 2000 (disapplication or modification of rules in individual cases)

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure

360. Please see the entry for clause 32. Subsection (7)(b) of clause 47 applies section 138BA (which is inserted into FSMA 2000 by clause 32) to the Bank of England in relation to central counterparties and central securities depositories.

Amendment to Schedule 17A to FSMA 2000 (further provision in relation to exercise of Bank of England functions under Part 18 of that Act) to apply the new section 138EA of FSMA 2000 (matters to consider when making rules)

> *Power conferred on: HM Treasury*
> *Power exercised by: regulations made by statutory instrument*
> *Parliamentary Procedure: affirmative procedure*

361. Please see the entry for clause 29. Subsection (7)(d) of clause 47 applies section 138EA (which is inserted into FSMA 2000 by clause 29) to the Bank of England in relation to central counterparties and central securities depositories.

Amendment to Schedule 17A to FSMA 2000 (further provision in relation to exercise of Bank of England functions under Part 18 of that Act) to apply section 141A (power to make consequential amendments of references to rules) and the new section 141B of FSMA 2000 (power to consequentially amend enactments)

> *Powers conferred on: HM Treasury and Secretary of State for s.141A; HM Treasury for s.141B*
> *Powers exercised by: order (for s.141A) and regulations (for s.141B) made by statutory instrument*
> *Parliamentary Procedure: negative procedure for an order under s.141A and affirmative procedure for regulations under s.141B*

362. Please see the entry for clause 32. Subsection (7)(h) of clause 47 applies section 141B (which is inserted into FSMA 2000 by clause 61) in relation to rules made by the Bank of England in relation to central counterparties and central securities depositories.

363. It also applies section 141A of FSMA 2000 in relation to such rules or guidance. Section 141A already applies in relation to rules made by the FCA and the PRA, and provides that where legislation contains a reference to rules made by those regulators, or guidance by the FCA, HM Treasury or Secretary of State can by order amend it in consequence of any exercise by the regulator of its power to make, alter or revoke those rules or guidance. An order made under section 141A is subject to the negative procedure by virtue of section 429 of FSMA 2000. This is considered appropriate as the power is limited and technical, being confined to amending references to rules.

Clause 48 and Schedule 7: Payment Systems Regulator's powers

New section 102B of FSBRA (Matters to consider when imposing generally applicable requirements).

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure

364. Please see the entry for clause 29. New section 102B enables HM Treasury to require the PSR, when proposing to impose a generally applicable requirement, to "have regard" to any matters specified by HM Treasury that are relevant to the imposition of the requirement in question.

365. The purpose and justification for taking this power is described in the entry for clause 29.

New subsections (5A) and (5B) of section 103 of FSBRA (regulator's general duty to consult)

Power conferred on: HM Treasury
Power exercised by: Statutory Instrument
Parliamentary procedure: Negative Procedure

Context and Purpose

366. Under section 103 of FSBRA, the PSR is required to make and maintain effective arrangements for consulting relevant persons on the extent to which its general policies and practices are consistent with its general duties and how its payment systems objectives may best be achieved. In order to satisfy this requirement, the PSR is required to establish and maintain one or more panels of persons to represent the interests of relevant persons. The PSR has established a panel called the Payment Systems Regulator Panel.

367. The PSR appoints the members of its statutory panels, but HM Treasury must approve the appointment of the chair of the panel.

368. New subsection (5A) of section 103 has the effect that members of a statutory panel of the PSR must not receive remuneration from the FCA, the PRA, the PSR, the Bank or HM Treasury. This is to enhance the independence of the panels. However, HM Treasury considers that it is appropriate to have certain exemptions from this position. Therefore, new subsection (5B) of section 103, gives a power to HM Treasury to provide, by statutory instrument, that the disqualification does not apply in relation to a PSR panel. New subsection (5C) provides that the statutory instrument may provide an exemption generally from the disqualification, or in relation to a specific description of persons or cases.

369. The purpose and justification for new section 1MA(2) of FSMA 2000, which is concerned with the FCA's statutory panels, applies equally to the power in new subsections (5B) and (5C) in relation to PRA's statutory panels.

New section 104D of FSBRA (Requirement to review specified requirements).

Power conferred on: the Payment Systems Regulator
Power exercised by: direction
Parliamentary Procedure: none

Context

370. Clause 48 introduces Schedule 7, which makes provision relating to the accountability of the PSR. Schedule 7 inserts these accountability provisions into the appropriate legislation governing the PSR and its functions, the Financial Services (Banking Reform) Act 2013 ("FSBRA"). They replicate, with appropriate adaptations for the PSR context, the accountability arrangements for the other financial regulators in Chapter 3 of the Bill.

371. New section 104D of FSBRA confers on HM Treasury the ability to direct the PSR to carry out a review of certain specified generally applicable requirements. This is in line with the accountability arrangements for the other financial regulators but applies instead to directions made by the PSR that apply generally under section 54 of FSBRA (general directions), and requirements imposed on operators generally under section 55 of FSBRA (generally imposed requirements).

Purpose and justification

372. The purpose and justification for taking this power is described in the entry for clause 27.

New section 104F of FSBRA (Power to require the imposition of generally applicable requirements).

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure

373. Please see the entry for clause 29. New section 104F confers on HM Treasury a power to make regulations to require the PSR to impose a generally applicable requirement in relation to a specified activity or specified description of person.

374. The purpose and justification for taking this power is described in the entry for clause 29.

New paragraph 7A of Schedule 4 to FSBRA 2013 (Other reports)

Power conferred on: HM Treasury
Power exercised by: direction
Parliamentary procedure: none

375. New paragraph 7A of Schedule 4 to FSBRA 2013 gives HM Treasury the power to direct the PSR to make a report about such matters as are specified in the direction. The PSR will therefore be required to provide information on an ad hoc basis such that the public are informed as topic areas develop rather than in the annual report which could be provided to HM Treasury many months after an issue is topical.

376. The purpose and justification for new paragraph 7A of Schedule 4 to FSBRA applies to this power for the PSR.

PART 2 – ACCESS TO CASH

Cash Access Services

Clause 51 and Schedule 8: Cash access services

New subsection 131O(9) in new part 8B of FSMA 2000 (Cash Access Services) to enable HM Treasury to amend the definitions set out in this section and to amend any other provision of Part 8B in consequence of the amended definition.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative procedure under s.429(2) FSMA 2000

Context and Purpose

377. Clause 51 introduces Schedule 8 to the Bill, which relates to the provision of cash deposit and withdrawal services in the UK (or a part of the UK). Schedule 8 inserts a new Part 8B into FSMA 2000.

378. New Part 8B of FSMA 2000 creates a new regulatory regime overseen by the FCA, the purpose of which is to protect access to cash for retail customers. The FCA operates the regime, setting rules for designated relevant current account providers to follow in order to ensure the reasonable provision of cash access services, and having the ability to direct the action of those designated relevant current account providers (see description of sections 131V(1) and 131W(1) of FSMA 2000 below). HM Treasury has the ability to designate the firms in scope of the regime (see description of section 131R(1) below), and to set out in a policy statement (see description of section 131P(1) below) the policies in relation to cash access services which the FCA must have regard to when exercising these functions. As part of the FCA's role to ensure the reasonable provision of cash access services the FCA is required to have regard to the impacts of any local deficiencies in the provision of cash access services which the FCA considers to be significant (see description of section 131U below).

379. Section 131O of FSMA 2000 defines terms used in the new Part 8B that determine the firms that HM Treasury may designate as in scope of the regime. The regime can apply to a "relevant current account provider", meaning a firm with a Part 4A of FSMA 2000 permission to accept deposits, and which provides current accounts in reliance on that permission, though certain firms, namely credit unions and friendly societies are excluded through section 131O(8). A "current account" is defined as an account by means of which one or more named persons are able to place cash, withdraw cash, and execute and receive payment transactions to and from third parties, including the execution of credit transfers. This definition is intended to capture only a subset of payment accounts (for instance, savings accounts will typically not be covered). It is current accounts provided by relevant current account providers by virtue of their Part 4A permission (defined as a "relevant current account") that are within scope of this regime.

380. The power in section 131O(9) allows HM Treasury to amend the definitions of "relevant current account provider", "current account" and related terms also set out in

section 131O, and to make consequential amendments to the other provisions of Part 8B of FSMA 2000.

Justification for taking the power

381. The power to amend the definition of "current account", "relevant current account provider" and related definitions is necessary to ensure that HM Treasury has the ability to update the new regime should the retail cash market change in the future. The UK population's use of cash is expected to change over time; for instance, retail customers may increasingly use other types of accounts as opposed to current accounts to facilitate their day-to-day cash transactions. Similarly, the retail banking market is expected to continually adapt, both in the sense of who is in the market, and the solutions they devise to meet their customers' changing needs. Such changes may require amendment to the definition of "current account" and "relevant current account provider."

382. The power to make consequential amendments to Part 8B as a whole is necessary in order to ensure that the provisions remain consistent and coherent.

Justification for the procedure

383. HM Treasury consider the affirmative procedure is appropriate for amendments to primary legislation.

New section 131P(1) (Cash access policy statement) in new Part 8B of FSMA 2000 (Cash Access Services).

Power conferred on: HM Treasury
Power exercised by: policy statement
Parliamentary Procedure: none

Context and Purpose

384. The purpose of the cash access policy statement is to set out HM Treasury's policies concerning cash access services in the UK, or in any part of the UK. The statement may set out policies in relation to a number of considerations, including expectations of reasonable distances for retail customers to travel for deposit services and withdrawal services, for personal current accounts and non-personal current accounts, and for rural and urban areas. HM Treasury may also set out separate expectations for parts of the UK in the expectation that some firms may need to be designated for either all or parts of the UK (see section 131R(3) of FSMA 2000). Initially, the government intends to set out its expectations on the basis of the overall distribution of existing cash access services. In preparing a cash access policy statement, HM Treasury must consult the FCA and have regard to any report provided by the FCA (subsection 131P(4)).

Justification for taking the power

385. HM Treasury considers it to be appropriate for the government to set out its expectations for cash access in the United Kingdom via a policy statement to which the FCA must "have regard", as opposed to placing legal requirements directly on relevant current account providers.

386. This approach ensures that the FCA is equipped to exercise its functions flexibly and responsively, including to avoid any unintended consequences such as over-provision or gaps in provision, that could result from set legal parameters. It also provides HM Treasury with flexibility to adjust its expectations for cash access services as appropriate over time. This may be, for example, in response to changes in the UK population's use of cash over time.

387. This provision therefore requires that HM Treasury set out its expectations for cash provision in a policy statement. Under section 131U of FSMA 2000 the FCA is then required to have regard to the policy statement, as well as any other matters it thinks appropriate, alongside having regard to the impacts of any local deficiencies in provision of cash access services.

388. The FCA is required to ensure "reasonable provision of cash access services" (subsection 131U(1) of FSMA 2000), and the FCA will be required to exercise its functions, including the ability to make rules, as it appears to be necessary in furtherance of the purpose.

<u>Justification for the procedure</u>

389. HM Treasury considers publication of a cash access policy statement in accordance with section 131(5), as opposed to setting legal requirements on relevant current account providers in legislation, as the appropriate approach. The policy statement is intended to set out HM Treasury's expectations generally on cash access services in the UK, or in any part of the UK, for the FCA to take into account when setting requirements for relevant current account providers. HM Treasury will need to respond to changes in the market and needs of consumers and therefore may need to revise its policy statement over time. The population's use of cash is expected to change over time and the retail banking market is expected to continually adapt, both in the sense of who is in the market, and the solutions they devise to their customers' changing needs.

390. This approach provides HM Treasury and the FCA with flexibility to respond to these possible changes and revise expectations for cash access services whilst ensuring sufficient public visibility of the policy. HM Treasury will be required to keep the policy statement under review and the FCA will be required to take the policy statement into account when exercising its functions and consult on any related regulatory rules before they are implemented.

New section 131R(1) (Designation) and new section 131S (Designation criteria) in new Part 8B of FSMA 2000 (Cash Access Services).

Power conferred on: HM Treasury
Power exercised by: notice
Parliamentary Procedure: none

Context and Purpose

391. The purpose of HM Treasury's designation power in section 131R(1) is to allow HM Treasury to determine which firms involved in the provision of cash access services need to be within scope of the regime ("designated persons"). HM Treasury has the ability to designate both the relevant current account providers (see section on section 131O above), and any entity that plays a coordination role in the provision of cash access services where a designated relevant current account provider is a participant. HM Treasury may also designate firms for the United Kingdom, Northern Ireland or Great Britain.

Justification for taking the power

392. HM Treasury considers it appropriate to designate relevant current account providers on a case-by-case basis, rather than apply the regime to all current account providers. HM Treasury considers it would be disproportionate to require all current account providers authorised by the FCA to ensure the provision of cash access services across the United Kingdom, for example when they may only have a relatively small cohort of customers in terms of market share. HM Treasury also anticipates that the market is likely to continue to change over time, for example with current account providers' market shares rising and falling and with some providers increasingly offering their services digitally only. It is necessary for HM Treasury to be able to update the cohort of designated persons to reflect market conditions and to ensure an adequate proportion of the current account market is captured at any given time.

393. As a result, section 131S of FSMA 2000 sets out the criteria which HM Treasury must take into account when exercising this power, including the location of its cash access services, the location of its current account holders, its share of the current account market and the total value of the deposits held by it. On the basis of these criteria, the government expects to designate only the largest relevant current account providers. Per section 131T, HM Treasury may cancel or vary a designation notice, allowing it to update the cohort of designated persons.

394. There is precedent for a designation order of this type in existing regulation of payments services and systems: section 43 of FSBRA allows HM Treasury to designate a payment system to be regulated by the PSR; section 184 of the Banking Act 2009 which allows HM Treasury to recognise a payment system to be regulated by the Bank; and section 21 of the Payment Accounts Regulations 2015[29] allows HM Treasury to designate certain credit institutions required to offer payment accounts with basic features.

Justification for the procedure

[29] Payment Accounts Regulations 2015/2038.

395. HM Treasury considers that no Parliamentary oversight is required in relation to the exercise of this power, as oversight is afforded through the publication of the designation notice by HM Treasury. There are other procedural safeguards in the designation process, such as consultation with the FCA and notification in relation to the person to be designated. This is consistent with the designation processes in FSBRA and the Banking Act 2009 described above.

New section 131U(1) (Purpose for which FCA must exercise its functions) and new section 131V(1) (FCA rules) in new Part 8B of FSMA 2000 (Cash Access Services)

Power conferred on: the Financial Conduct Authority
Power exercised by: rules made in accordance with new Part 8B of FSMA 2000
Parliamentary Procedure: none

Context and Purpose

396. Section 131U of FSMA 2000 sets out the core purpose of this new Part 8B regime, which is to ensure the reasonable provision of cash access services. The FCA may determine the nature and extent of reasonable access with regard to HM Treasury's cash access policy statement and any other matters it considers appropriate. Subsections 131U(3) to (6) set out more detail as to the purpose of this regime and the FCA's functions in respect of it, namely that the FCA is required to have particular regard to the impact of any local deficiency in the provision of cash access services which the FCA considers to be significant when exercising its functions under this Part. In determining whether there are local deficiencies in the provision of cash access services, and the significance of the impacts of such deficiencies, the FCA must have regard to HM Treasury's policy statement and other considerations it considers appropriate. These may include the number of persons likely to be affected by the deficiency; the characteristics of the persons likely to be affected by the deficiency; and the likely impact on the persons likely to be affected.

397. The purpose of the FCA rule-making power in section 131V(1) is to give the FCA the ability to make rules applying to designated persons in order to ensure the reasonable provision of cash access services in accordance with the purpose described above.

Justification for taking the power

398. HM Treasury considers that the rule-making power is necessary in order to properly empower the FCA in its operation of this regime. It will provide a basis for the FCA to set the requirements on designated entities for cash access, breach of which will trigger the enforcement provisions that apply to Part 8B. The FCA will be appointed as the lead regulator for access to cash on the basis that the appropriate provision of cash withdrawal and depositing facilities are the two most significant factors in maintaining access to cash and the FCA has existing regulatory relationships with relevant current account providers that HM Treasury may designate to be in scope of the regime.

399. The FCA already has a general rule-making power in section 137A of FSMA 2000, enabling it to make rules applying to authorised person(s) with respect to both regulated and non-regulated activities where the rules are necessary or expedient for the purpose of the FCA advancing one of its operational objectives. However, the general rule-making power is not sufficiently wide to allow the FCA to ensure the reasonable provision of access to cash: for instance, this Part 8B regime has been designed to apply to a wide range of firms involved in the provision of access to cash, including coordination bodies that are not "authorised persons" and therefore not in scope of the FCA's general rule-making power. Therefore, HM Treasury has created a distinct rule-making power (section 131V) scoped by a new and distinct FCA purpose (subsection 131U(1)).

Justification for the procedure

400. HM Treasury considers that no Parliamentary oversight is required in relation to the exercise of this power by the FCA. It is intended that this rule-making power is exercised in accordance with safeguards already included in Part 9A of FSMA 2000 for the general rule-making power; in particular, sections 138C (evidential provisions), 138F (notification of rules) and 138I (consultation by the FCA).

New section 131W(1) (Power to direct designated persons) in new Part 8B of FSMA 2000 (Cash Access Services).

Power conferred on: the Financial Conduct Authority
Power exercised by: direction
Parliamentary Procedure: none

Context and Purpose

401. The purpose of this power of direction in section 131W(1) of FSMA 2000 is for the FCA to direct designated persons in accordance with the purpose of this regime (section 131U). This will allow the FCA to direct designated persons to take specified action to remedy potential deficiencies arising in relation to local access which the FCA consider to be significant.

Justification for taking the power

402. HM Treasury considers that this power of direction is necessary in order to properly empower the FCA in its operation of this regime, and to enable it to target its actions proportionately and appropriately. The FCA will be appointed as the lead regulator for access to cash on the basis that the appropriate provision of cash withdrawal and depositing facilities are the two most significant factors in maintaining access to cash and the FCA has existing regulatory relationships with relevant current account providers that HM Treasury may designate to be in scope of the regime.

403. The power of direction allows the FCA to meet its purpose of ensuring the reasonable provision of cash access services in a proportionate and targeted manner. While the rules

set out a general framework for the regime, the power of direction allows the FCA to take action on specific issues by directing one or multiple designated persons, as the FCA considers appropriate, to require or prohibit the taking of specific actions. Breach of a direction triggers the enforcement procedures set out in section 131Z (see below).

Justification for the procedure

404. There is no Parliamentary procedure, as is usual for the exercise of FCA statutory powers in the form of a direction, instruction or prohibition, the FCA are given these powers to exercise as part of their day-to-day obligations. Parliamentary procedure would be inappropriate and would prevent the FCA from making decisions regarding individual entities in a timely manner.

Clause 52 and Schedule 9: Wholesale cash distribution

New section 206C (overview and Purpose) and new section 206D (Policy statement) -Power for the Bank of England to prepare a statement of policy with respect to exercise of its powers

Power conferred on: the Bank of England
Power exercised by: preparing a policy statement (section 206D(1)) and providing the statement to HM Treasury for publishing
Parliamentary Procedure: none

Context and Purpose

405. Clause 52 introduces Schedule 9, which makes provision about persons involved in the wholesale distribution of cash. Schedule 9 inserts a new Part 5A into the Banking Act 2009.

406. At the 2020 budget, the Chancellor announced that the government would bring forward legislation to protect access to cash and ensure that the UK's cash infrastructure is sustainable in the long-term. Inserting this new Part 5A into the Banking Act 2009 provides the Bank of England with the powers it needs to ensure that the UK's wholesale cash infrastructure is sustainable.

407. Under this provision (section 206D(1)), the Bank is required to publish a policy statement before it is able to exercise any of its powers under the new Part 5A. Section 206C(2) sets out that the exercise of the Bank's powers must be for the purposes of managing risks to the effectiveness, resilience and sustainability of the wholesale cash infrastructure throughout the UK or any part of the UK. It is expected that the statement will also deal with the powers conferred on the Bank in furtherance of the financial stability objective. The intention is that the statement will explain how the Bank's powers are being exercised in accordance with its purpose. The statement must be reviewed by the Bank of England from time to time at the Bank's discretion. This recognises the independence of the Bank of England as the regulator responsible for the wholesale cash infrastructure.

Justification for taking the power

408. The power requires the Bank to consult the entities representative of those likely to be affected and to explain in the statement how the Bank will be exercising its powers in order to ensure the efficiency, resilience and sustainability of the wholesale cash infrastructure is maintained and to further the Bank's financial stability objective. The Bank will not be able to exercise its enforcement powers contained under Part 5A until such time as the policy statement is published after this consultation.

Justification for the procedure

409. The statement will be laid in Parliament by HM Treasury in the interests of transparency and accountability. The Bank is unable to exercise any powers under this legislation before it has published the statement. The requirement to consult provides the flexibility for the Bank to engage in targeted engagement with affected firms or a fuller public consultation

as appropriate. HM Treasury considers that no Parliamentary oversight is required in relation to the exercise of this power for the Bank to publish a policy statement. The policy statement is intended to set out how the Bank will exercise its powers under the legislation, giving the wholesale cash market an indication of what general considerations the Bank will take into account. Therefore, HM Treasury considers that publication is an appropriate degree of oversight in this instance.

New section 206G (Wholesale cash oversight orders), new section 206H ("market significance" and "systemic significance"), in new part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: HM Treasury
Power exercised by: order
Parliamentary Procedure: none

Context and Purpose

410. The use of cash is declining across the UK and there is a risk that either a disruption to and/or deficiencies in the operation of the network could over time present a risk to cash supply, undermining the government's access to cash objectives. Uncoordinated consolidation, rationalisation or a market exit from the wholesale cash network could accentuate these risks. Furthermore, the serious disruption or failure of any systemic entity formed in the wholesale cash network could create risks to financial stability and confidence in the UK financial system.

411. HM Treasury has given the Bank appropriate authority to take on the responsibility of overseeing the wholesale cash infrastructure due to its existing role in the issue of Bank banknotes and their subsequent circulation and distribution of notes via the Note Circulation Scheme ("NCS"). The Bank has established relationships and knowledge in relation to the wholesale cash distribution network and it is therefore appropriate for HM Treasury to delegate powers to the Bank for effective oversight in this area. Although the Bank would carry out the oversight functions under both the market and prudential regime, the decision to bring the entities in scope of the Bank's oversight powers under the respective regimes via a designation mechanism rests with HM Treasury under new Part 5A Banking Act 2009 through section 206G.

412. The purpose of the power is to enable HM Treasury to bring into scope (section 206G(1)) any entity which performs a relevant function in relation to a wholesale cash distribution activity and is recognised as having market significance. The relevant functions (section 206G(3)) are undertaking the activity, managing the activity, providing a service in relation to the activity and providing financial support in relation to the activity. Wholesale cash distribution activities are defined under section 206E(1) and these are purchasing cash from issuing authorities, storing cash, transporting cash, undertaking authentication processes and facilitating the return of cash to issuing authorities. Under section 206H, a two tier designation criteria is set out such that HM Treasury may designate an entity for market significance (section 206H(2) if satisfied that any significant deficiency in, or disruption to, the performance of the person's relevant functions in relation to

wholesale cash distribution activities would be likely to undermine the effectiveness or resilience of wholesale cash distribution).

413. Under section 206H(3), HM Treasury can further recognise an entity as systemic if satisfied that any significant deficiency in, or disruption to, the performance of the person's relevant functions in relation to wholesale cash distribution activities would be likely (in addition to the consequences mentioned in section 206H(2)) to threaten the stability of or confidence in the UK financial system, or have serious consequences for business or other interests throughout the UK or any part of the UK.

414. Where different companies within the same group structure are involved in wholesale cash distribution activities, HM Treasury can have regard to the relevant functions of all the companies with the group involved in wholesale cash distribution (section 206H(4)). Where any one company would not be significant on its own, but as an aggregate, multiple companies within a group are considered to be significant to wholesale cash infrastructure, it is HM Treasury's intention to recognise all the companies within the group in the oversight order. Each company will be individually listed within the order in such circumstances.

Justification for taking the power

415. This power is necessary and proportionate as it enables HM Treasury to respond quickly to changes in the market without weighing heavily on Parliamentary resource. HM Treasury is seeking similar powers to those under Part 5 of the Banking Act 2009 in respect of payment systems and other FMIs, and necessary in this case because of the nature and scale of the risks to be managed in the Wholesale Cash Distribution network. To ensure that HM Treasury has the information it requires to be able to exercise powers, there is criteria set under section 206H of market significance and systemic significance which must be followed. Under section 206I(1), HM Treasury is required to consult the Bank of England and notify the person it concerns, and consider any representations made before making an oversight order. There is also a requirement to consult relevant regulators (section 206I(2)).

Justification for the procedure

416. There is a requirement for HM Treasury to consult the regulators and to notify the subject as well as consider any representations under section 206I to help ensure that the process is fair and takes into account all appropriate considerations. To undertake this process via primary legislation would be time consuming and weigh heavily on Parliamentary resource. This is consistent with the precedent set out under Part 5 of the Banking Act 2009.

New section 206J (Amendment or revocation of a wholesale cash oversight order)

Power conferred on: HM Treasury

Power exercised by: amending or revoking a wholesale oversight order under section 206J
Parliamentary Procedure: none

Context and Purpose

417. The purpose of the power is to enable HM Treasury to amend or revoke a wholesale cash oversight order.

418. HM Treasury wants to have the flexibility to amend or revoke oversight orders where circumstances change. An example of this is where the relevant group structure of the entity alters sufficiently such that the designation order is no longer fit for purpose. For example, where a specific entity that has been recognised under an oversight order undergoes a restructuring such that either the company name changes or else the business is transferred to a related company within the same group, the order may require amendment. Similarly, if an entity is already recognised as being market significant for undertaking and managing the activity, and subsequently HM Treasury is satisfied that it should also be designated for providing a service in relation to the activity, HM Treasury would amend the oversight order to reflect this. In certain cases, it may be that HM Treasury will instead revoke a designation order where it is satisfied that the entity no longer meets the criteria for wholesale cash distribution market oversight designation or wholesale cash distribution prudential designation.

Justification for taking the power

419. The power is required to provide flexibility for responding to changing circumstances, so that HM Treasury can respond in an agile manner and amend the oversight order without the need for further primary legislation which would take time and cause delay in the process.

Justification for the procedure

420. The same procedural requirements for making an oversight order also apply to the revocation or amendment of a designation order (section 206J(5)). There is a requirement to consult the Bank of England and regulators where relevant and notify the subject of the order and to consider any representations to ensure that there is fairness in the process. The procedure is considered to be proportionate in achieving the aims of the legislation.

New section 206K Power to publish principles in new part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: the Bank of England
Power exercised by: publishing of principles by the Bank of England under section 206K(1)
Parliamentary Procedure: none

Context and Purpose

421. This provision provides the Bank with the ability to issue principles for recognised entities to have regard to when carrying out their relevant functions. Different principles can be published in relation to different wholesale cash distribution activities, different relevant functions, and for persons recognised as having market significance only or persons recognised as having systemic significance.

422. Such principles would be high level and applicable generally. HM Treasury would have to approve the principles before they are made by the Bank. For systemic entities that are not subject to another prudential regime these could be similar to the Principles for Financial Market Infrastructures ("PFMIs"). Some elements of the PFMIs may well be appropriate for wholesale cash distribution market participants also.

Justification for taking the power

423. The power is necessary to enable the Bank to prevent uncoordinated consolidation, rationalisation or a market exit from the wholesale cash network, as well as mitigate against serious disruption or failure of any systemic entity formed in the wholesale cash network in an efficient and timely manner. They set a baseline and high-level framework for the Bank's expectations regarding how wholesale cash infrastructure market participants should conduct themselves in that market, and mitigate the risks that they identify. This power is similar to section 188 of the Banking Act 2009 which confers on the Bank of England the power to publish principles to which the operators of a payment system are to have regard and principles which service providers to recognised payments are to have regard in the provision of services to such systems.

Justification for the procedure

424. The Bank is required to consult with entities representative of those that are within scope when creating principles that it intends to issue, enabling the parties to engage with the process. The Bank will be carrying out the functions in accordance with public law principles. The procedure is consistent with how the Bank issues principles in relation to other comparable regimes, for instance Part 5 of the Banking Act 2009 in relation to payment systems.

New section 206L Power to publish codes of practice in new part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: the Bank of England
Power exercised by: the Bank issuing codes of practise under section 206L(1)
Parliamentary Procedure: none

Context and Purpose

425. The provision provides the Bank with the power to publish codes of practice for the operation of recognised entities in a similar process to that outlined in section 189 of the

Banking Act 2009. It is envisaged this could include codes of practice on operational resilience or business plans. Different codes of practice can be published in relation to different wholesale cash distribution activities, different relevant functions, and for both persons recognised as having market significance only or persons recognised as having systemic significance. For example, the Bank would be able to impose codes of practice for designated entities to abide by when entering into contractual relationships, e.g. with Cash in Transit providers. The Bank could also issue codes of practice specifically for designated service providers of wholesale cash market participants if it deems necessary to do so.

426. The Bank is required to consult with entities representative of those that are within scope when creating codes of practice that it intends to issue, although it can depart from the views of the industry in setting the codes as appropriate and required.

427. The purpose of this provision is so that the Bank can publish codes of practice about the wholesale cash distribution operations of the market participants that have been recognised for having market or systemic significance. For example, these could focus on operational resilience and an entity's business plans, or could impose codes or rules around significant contractual relationships.

Justification for taking the power

428. The power is necessary to enable the Bank to set out codes of practice to prevent the risk of serious disruption to, or failure in, the market, which could occur as a result of uncoordinated consolidation or rationalisation. It is appropriate for the Bank of England to have the power to publish these codes of practice because the Bank of England has existing expertise acquired through the operation of the NCS and its financial stability mandate. As such, the Bank of England is extremely well placed to draft the codes which will embody detail of best practice and safeguards for the purposes of minimising risks to financial stability.

Justification for the procedure

429. The Bank is required to consult with entities representative of those that are within scope when creating codes of practice that it intends to issue, enabling parties to engage with the process. The Bank will be carrying out the functions in accordance with public law principles, ensuring the Bank can respond in an agile, but appropriate, manner as necessary. The procedure is consistent with how the Bank issues codes of practice in relation to other comparable regimes, for instance Part 5 of the Banking Act 2009 in relation to payment systems.

New section 206M(1) power to give directions.

Power conferred on: the Bank of England
Power exercised by: pursuant to section 206M(1) by the Bank issuing a direction
Parliamentary Procedure: none

Context and Purpose

430. Through section 206M(1),the Bank of England has the power to give directions to recognised persons to prohibit the taking of specified action or setting standards to be met in performance of specified relevant functions related to specified wholesale cash distribution activity.

Justification for taking the power

431. To ensure continued effective, resilient and sustainable provision of cash, direction powers are needed so that, if required, the Bank can direct the entities to take action to ensure the wholesale cash system remains sustainable. This power could be used in the event capacity reductions or rationalisation are proposed to occur in a way that undermines the overall capacity of the market and its ability to service retail access to cash for the public. In this scenario, the Bank would be enabled to direct entities to put in place mitigants.

Justification for the procedure

432. The procedure is considered appropriate as the Bank will be carrying out its functions in accordance with public law principles. The procedure is consistent with how the Bank issues directions in relation to other comparable regimes, for instance Part 5 of the Banking Act 2009 in relation to payment systems.

New section 206M(6) Power to confer immunity in relation to directions

Power conferred on: HM Treasury
Power exercised by: order made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

433. Under section 206M(4) any recognised person (including the recognised person's officers and staff) have immunity from liability in damages in respect of action or inaction in accordance with the Bank's direction under section 206M(2) where the direction was given for the purpose of resolving or reducing a threat to the stability of the UK financial system. This is to reassure recognised industry participants that they will not be liable for any action they have taken pursuant to the Bank direction imposed for financial stability purposes. Under section 206M(6), HM Treasury has a power to make regulations conferring immunity on any person from liability in damages in respect of action or inaction in accordance with a direction under section 206M(2) (including a direction given for the purpose mentioned in subsection (3) for the purpose of resolving or reducing a threat to the stability of the UK financial system).

Justification for taking the power

434. This power anticipates a scenario where, in order to resolve or reduce a threat to financial stability the Bank directs a firm that is a recognised person and/or the directors of a firm to take an action and where there is, or the directors perceive there is or might be, a risk of acting contrary to or in conflict with any one or more alternative duties (for example any duty to their shareholders) or other contractual arrangements to which the firm is subject or otherwise bound to provide. In such circumstances, in particular where fast action is required, the Bank considers that such immunity is important to ensure that necessary action is taken promptly to avert a risk to financial stability. An equivalent provision exists under section 191(3) in part 5 of the Banking Act 2009 in relation to both operators of recognised payment systems or specified service providers to such systems. Likewise, in respect of the resolution regime section 48O(2) in part 1 of the Banking Act 2009 provides for immunity for directors of a firm subject to resolution in relation to any action or inaction in accordance with a direction made in or under a resolution instrument. Such immunity is therefore an integral part of the Bank's toolkit.

Justification for the procedure

435. The statutory instrument will be laid in parliament for approval by resolution of each House of parliament to ensure there is sufficient Parliamentary oversight for its use.

New section 206T(3) Penalty-power to prepare statement of principles which it will apply to determine whether to impose a penalty and the amount of penalty in new part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: the Bank of England
Power exercised by: preparing a statement of principles (section 206T(3)) which will apply in determining whether to impose a penalty and the amount of the penalty
Parliamentary Procedure: none

Context and Purpose

436. A recognised entity will be required to have regard to principles (section 206K) and comply with codes of practice (section 206L) and directions issued by the Bank of England (section 206M). Failure to comply with these measures may result in imposition of a financial penalty.

437. The purpose of this power is to enable the Bank of England to publish a statement of principles to be applied to determine whether to impose a penalty and the amount of the penalty.

Justification for taking the power

438. This power is necessary to provide transparency to entities designated under the regime of how penalties will be calculated.

Justification for the procedure

439. This is an area in which flexibility is required to enable the Bank to respond to changing circumstances. To undertake this process via primary legislation would be time consuming and weigh heavily on Parliamentary resource.

New section 206U(2) Closure-power to issue closure orders under section 206U(2) in new Part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: the Bank of England
Power exercised by: the Bank issuing closure order under section 206U(2)
Parliamentary Procedure: none

Context and Purpose

440. This power applies if the Bank of England thinks that a compliance failure by a person recognised for the purposes of Part 5A of the Banking Act 2009 as having systemic significance threatens the stability or confidence in the UK financial system or has serious consequences for business or other interests throughout the UK.

441. The power enables the Bank to give an order to stop performing specified relevant functions in relation to specified activities for a period of time, until further notice or indefinitely.

Justification for taking the power

442. This is an area in which flexibility is required as the need to issue these orders may require urgency to act to maintain financial stability as it relates to the wholesale cash distribution market. The Bank has the expertise to exercise its judgement under the stability mandate. It is not possible to predict the circumstances under which the power will be required therefore it cannot be put in primary legislation.

Justification for the procedure

443. This is an area in which flexibility is required to enable the bank to respond to changing circumstances. To undertake this process via primary legislation would be time consuming and weigh heavily on Parliamentary resource.

New section 206V Power to issue management disqualification order in new Part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: the Bank of England
Power exercised by: order
Parliamentary Procedure: none

Context and Purpose

444. Under section 206U(1), the Bank of England may prohibit a specified person from holding an office or position involving responsibility for taking decisions about the management of a recognised person for a specified period, until further notice or permanently.

445. This provision gives the Bank the power to address management failures.

Justification for taking the power

446. This is an area in which flexibility is required as the need to issue these orders may require urgency to act to maintain stability in wholesale cash distribution market. The Bank has the expertise to exercise its judgement under the financial stability mandate. It is not possible to predict the circumstances under which the power will be required therefore it cannot be put in primary legislation.

Justification for the procedure

447. This power does not require parliamentary oversight as it is a technical area for which the Bank is better suited to make decisions.

New section 206Z(2) Power to make regulations in relation to fees in new Part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: HM Treasury
Power exercised by: order made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

448. Designated entities would be required to pay fees to the Bank to cover the Bank’s operational costs of the regime. Fees must relate to a scale of fees approved by HM Treasury, and then made by HM Treasury under regulations subject to negative resolution. The intention is that the Bank is required to consult industry on a proposed scale of fees, before making a recommendation to HM Treasury.

449. The Bank envisages that the majority of costs would initially be associated with a small supervisory team at the Bank. Other incidental costs such as travel and relevant professional subscriptions related to running the regime are likely to be small.

Justification for taking the power

450. The power is similar to what HM Treasury has under section 203 of Banking Act 2009. HM Treasury considers it appropriate to maintain control over the level of fees that may be charged, in line with arrangements for similar regimes.

451. It is envisaged that the level of fees would change over time (for example, to take into account inflation, or changing circumstances in the market). Further, as the fee scale is likely to be detailed, it is considered appropriate that provision should be set out in secondary legislation.

Justification for the procedure

452. The process of consulting industry gives an opportunity for industry to have input. The negative resolution procedure provides an appropriate degree of Parliamentary oversight and makes appropriate use of Parliamentary time. Any fees would relate to the activities performed by the Bank of England and would not be expected to exceed a cost recovery basis.

New section 206Z4(3) Power to make regulations to permit disclosure of information in new Part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: HM Treasury
Power exercised by: order made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

453. Section 206Z4(2) confers a power on HM Treasury to make regulations to enable the Bank to disclose information overriding contractual or other requirements to keep information in confidence. HM Treasury is able to permit the Bank to publish information specified in the regulations made under this power in a manner provided for through the regulations.

Justification for taking the power

454. This power enables HM Treasury to make regulations to permit the disclosure of information obtained by the Bank under this clause to a specified person. This provision is needed in order to ensure that the Bank can share information appropriately and subject to statutory limits in relation to recognised entities. The gathering and sharing of information will play a fundamental role in the Bank's oversight of the market. The very decision to recognise an entity - the starting premise of the whole structure - is informed by information that can be obtained by virtue of this power.

Justification for the procedure

455. Secondary legislation provides the necessary flexibility to make and amend legislation as appropriate to reflect any need to share information with other persons. The draft regulations are likely to be uncontroversial and technical in nature, therefore, the negative resolution procedure is considered appropriate and provides Parliament with adequate opportunity to scrutinise the draft regulations, while making good use of Parliamentary

time. This is similar to the powers which the Bank has under section 204(6) of Banking Act 2009 which follows the same negative procedure.

New section 206Z6 (Power to disapply regulation and enforcement provisions) in new Part 5A of the Banking Act 2009 (Wholesale cash distribution).

Power conferred on: HM Treasury
Power exercised by: order made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

456. This power enables HM Treasury to disapply the Bank's powers of regulation and enforcement under sections 206K to 206Z4 in relation to companies wholly owned by the Crown by making regulations to that effect. This power is to be read in light of section 206H(6) which further sets out that companies wholly owned by the Crown may not be recognised for systemic significance, i.e. they can only be recognised under this regime for market significance.

457. The Post Office Limited ("POL") is the only entirely state-owned entity in the wholesale cash distribution market. The Postal Services Act 2011[30] provided for a "Post Office company" to continue to be owned by the Crown or a mutual ownership structure after the privatisation of Royal Mail. Under the Act (Part 1, section 4), the Crown may only dispose of its interest in a "Post Office company" through the issue or transfer of shares or share rights in a Post Office company to a relevant mutual by order of the Secretary of State for Business, Innovation and Skills (now BEIS).

458. If any other entity in the wholesale cash distribution market were to become wholly owned by the Crown, any regulations made by HM Treasury exercising this power would apply to those companies as well. The existing power in section 259 of the Banking Act 2009 which allows HM Treasury to make different provisions for different circumstances may also be utilised if in certain cases, it may not be appropriate for other companies wholly owned by the Crown to be treated in the same manner as the Post Office (for example, if in a bail-out situation, one or more of the other market participants were to become temporarily owned by the Crown, HM Treasury may make regulations under section 259 and 206Z6 to treat the other companies differently to the Post Office, if justified on public law grounds.)

Justification for taking the power

459. The government provides funding directly to POL under an established funding agreement which is designed to cover costs of maintaining a network of post offices as well as the development of POL's operations. There are limitations on borrowing and requirements to obtain consent from the Secretary of State under the Articles of Association. In light of these arrangements alongside the general oversight role by BEIS

[30] Postal Services Act 2011 c.5.

over POL's operations, HM Treasury do not think it would be necessary for the Bank to be given prudential oversight powers over POL, which is why there is the restriction in section 206H(6). The existing oversight over POL's financial and other arrangements should be sufficient to safeguard against any risks that may arise should POL become systemic. HM Treasury wish to retain the flexibility to consider any future changes to the structure or name of POL and taking this power would achieve this objective.

460. Notwithstanding the above, it is still possible for HM Treasury to recognise a company wholly owned by the Crown for "market significance". The Bank's powers set out in sections 206K to 206Z4 could therefore apply to classes of persons wholly owned by the Crown who are recognised for being market-significant. This power allows HM Treasury to disapply some of these powers (for instance, the management disqualification power in section 206V) if it considered at the time it is not appropriate to provide the Bank with all of the current suite of powers over companies wholly owned by the Crown. This could be amended over time as appropriate and necessary.

Justification for the procedure

461. This is subject to an affirmative procedure recognising that the power allows HM Treasury to disapply certain provisions of primary legislation against companies wholly owned by the Crown. The laying of the draft regulations before and approved by a resolution of each House of Parliament will serve in the interest of accountability and transparency. This approach is similar to powers in sections 206A and 251 of the Banking Act 2009. HM Treasury will engage with all parties it deems likely to be affected before making such a statutory instrument.

PART 3 – PERFORMANCE OF ACTIVITIES RELATING TO FINANCIAL MARKET INFRASTRUCTURE

Clause 53 and Schedule 10: FMI bodies: senior managers and certification

New section 309A (Recognised bodies to which this Chapter applies) in Part 18 of FSMA 2000.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

462. The Bill legislates to create a new Senior Managers & Certification Regime ("SM&CR") "gateway", which will enable HM Treasury to make regulations applying the SM&CR provisions in Schedule 10 to the Bill to any of the following entities;
  a. central counterparties (CCPs),
  b. central security depositories (CSDs),
  c. recognised investment exchanges (RIEs), and
  d. credit rating agencies ("CRAs").

463. This new section 309A will provide for the application of the regime to CCPs, CSDs and RIEs, while section 309Z8 provides for the extension of the regime to CRAs by way of HM Treasury regulations.

Justification for taking the power

464. New section 309A provides flexibility for the government to determine to which of the potential in-scope firms the regime applies. Although the government has consulted on creating an SM&CR for CCPs and CSDs and intends to apply the regime to these entities, no detailed consideration has yet been carried out on whether or not to extend the regime to CRAs and RIEs. The approach set out in section 309A gives HM Treasury the option to extend the SM&CR to RIEs in the future, should it decide to do so, and following further specific consultation on that issue.

Justification for the procedure

465. The negative procedure is considered appropriate for this power. It is a limited power, to apply the regime provided for in Schedule 10 to one or more of the three types of body identified in the clause itself and can only be exercised following consultation.

New section 309C (Procedure for making Part 18 prohibition orders), new section 309D (Varying and withdrawing Part 18 prohibition orders), new section 309J (Vetting by relevant recognised bodies), new section 309K (Determining applications: power to grant approval), new section 309P (Procedure for withdrawing approval) in Part 18 of FSMA 2000.

Powers conferred on: HM Treasury
Powers exercised by: regulations made by statutory instrument

Parliamentary Procedure: negative

Context and Purpose

466. These powers, contained in new sections that will be inserted into FSMA 2000, provide that consultation requirements may be prescribed which apply to the appropriate regulator before it takes certain steps. Section 417 of FSMA 2000 provides that "prescribed" (where not otherwise defined) means prescribed in regulations made by HM Treasury. Section 429(8) of FSMA 2000 provides that regulations, such as these, which are not identified in section 429(1) to (7), are subject to the negative procedure.

467. Under these powers, HM Treasury will, for example, be able to specify through secondary legislation if consultation between the regulators should occur:

a. ahead of making a Part 18 prohibition order (section 309C(1));
b. ahead of varying and/or withdrawing a Part 18 prohibition order (section 309D(3));
c. ahead of making rules which relate to the application for approval process for senior managers (section 309J(4));
d. ahead of determining applications for senior managers (section 309K(5));
e. ahead of withdrawing an approval (section 309P(1)).

468. The ability for HM Treasury to specify the circumstances in which consultation is required in regulations allows the regime to retain flexibility. HM Treasury will therefore be able to make appropriate provision depending on what entity the new SM&CR is being applied to, and ensure the regime is tailored in a proportionate manner to each entity. For example, consultation between the Bank and the FCA may be useful ahead of the Bank making rules which relate to the application for approval process for senior managers of CCPs. CCPs are often part of larger groups, which also contain RIEs (regulated by the FCA), so it may be useful for HM Treasury to require the Bank to consult the FCA ahead of making rules, to ensure the SM&CR is applied in a consistent manner across the sector.

Justification for taking the power

469. The appropriate consultation requirements will vary depending on which firm the SM&CR is being applied to. As HM Treasury will apply the regime to different firms, or classes of firm, through secondary legislation, it is appropriate for the accompanying consultation requirements to be specified in secondary as well.

Justification for the procedure

470. The negative procedure is appropriate for regulations made in exercise of these powers, which are restricted to a single procedural matter which is to be satisfied before a regulator takes certain steps under the regime.

New section 309F(3) and (4) (Duty in relation to prohibited individuals) and new section 309T(2) and (3) (Breach of statutory duty by relevant recognised bodies) in Part 18 of FSMA 2000.

Powers conferred on: HM Treasury
Powers exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

471. Under new section 309F, a relevant recognised body must take reasonable care to ensure that individuals who are subject to a Part 18 of FSMA 2000 prohibition order do not carry out functions for which they are prohibited. A contravention of this duty is actionable at the suit of a private person who suffers loss as a result of the contravention. New section 309F(3), read in combination with the definition of "prescribed" in section 417 FSMA 2000, provides that HM Treasury can prescribe cases which are actionable by a person who is not a private person, whilst new section 309F (4) enables HM Treasury to prescribe the meaning of "private person".

472. Under new section 309T, a relevant recognised body must take reasonable care to ensure that individuals do not perform a designated senior management function unless they are acting in accordance with an approval given by the appropriate regulator under section 309G. A contravention of this duty is actionable at the suit of a private person who suffers loss as a result of the contravention. New section 309T(2) provides that HM Treasury can prescribe cases which are actionable by a person who is not a private person, whilst new section 309T(3) enables HM Treasury to prescribe the meaning of "private person".

Justification for taking the powers

473. The appropriate definition of private person, as well as the cases which are actionable by a person who is not a private person, will vary depending on which firm, or class of firms, the SM&CR is being applied to. As HM Treasury will apply the regime to different firms through secondary legislation, it is appropriate for the definitions and circumstances described above to be specified in secondary as well.

Justification for the procedure

474. The negative procedure is appropriate for regulations made in exercise of these powers, which are restricted to a single and specific matter.

New section 309G(3) (Requirement for approval) and new section 309Y(3) (Certification of employees by relevant recognised bodies) in Part 18 of FSMA 2000.

Powers conferred on: the appropriate regulator (Bank/FCA)
Powers exercised by: rules made in accordance with Part 9A of FSMA 2000 (for FCA rules) and in accordance with the provisions of Part 9A that are applied to the Bank by paragraph 10 of Schedule 17A of FSMA 2000 (as it will be amended by this Bill) (for Bank rules).
Parliamentary Procedure: none

Context and Purpose

475. Under new section 309G(3), the appropriate regulator (the Bank or the FCA, as the case may be) has the power to set out in its rules the functions which are a "designated senior manager function". Where a function is a "designated senior manager function", a relevant recognised body must take reasonable care to ensure that a person does not perform it in relation to the carrying on of an activity by the body, unless the person is acting in accordance with an approval given by the appropriate regulator under new section 309G.

476. New section 309H(2) and (3) sets out the transitional provision that can be made by regulators under the power in section 309G(3). This ensures that regulators can provide for a smooth transition when the requirement to obtain approval for a particular function is introduced, or when it is changed.

477. Under new section 309Y(3), the appropriate regulator (the Bank or the FCA, as the case may be) has the power to set out in its rules the functions which are a "specified function" for the purpose of the certification regime provided for in new sections 309Y and 309Z. Where a function is specified as a "specified function", a relevant recognised body must take reasonable care to ensure that none of its employees performs it in relation to the carrying on of an activity by the body, unless the employee has a valid certificate issued by the body under section 309Z.

Justification for taking the powers

478. Which functions should be considered "senior management functions" or "specified functions" will vary by type of body and should be determined by the relevant regulator, as is the case for the existing SM&CR regime in Part V of FSMA 2000, which applies to banks, insurers and other authorised persons.

Justification for the procedure

479. There is no parliamentary procedure. Rules made by the regulators under FSMA 2000 do not have formal Parliamentary oversight, but are subject to various procedural requirements which are set out in Part 9A of FSMA 2000 for the FCA, and which are applied where appropriate to the Bank by paragraph 10 of Schedule 17A to FSMA 2000. These procedural requirements will apply to these powers, and as such it is not considered appropriate to provide for formal parliamentary oversight. This is in accordance with the normal FSMA 2000 model.

New section 309H (Rules under section 309G(3): transitional provision) in Part 18 of FSMA 2000.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument

Parliamentary Procedure: negative, or affirmative if modifying a provision of primary legislation

Context and Purpose

480. New section 309H (2) provides that HM Treasury may make regulations making such incidental, consequential, transitional, supplementary or saving provision that HM Treasury considers appropriate in connection with the making of rules by the appropriate regulator under new section 309G (power of the regulator to specify in rules the functions which are a "designated senior management function"). Paragraph (3) provides that this can include provision conferring functions on the regulator (including the function of making rules), and provision modifying (including amending, repealing and revoking) legislation. Legislation in this context means primary and subordinate legislation (including FSMA 2000), as well as retained direct EU legislation.

Justification for taking the power

481. It is not possible to set out the modifications that may be required to be made to legislation in light of the exercise of the regulator's power in section 309G in advance because this will depend on the rules that are proposed to be made in relation to different functions and for different types of body, and the manner in which it is appropriate for those rules to come into force.

482. Due to the nature of certain provisions under this Chapter, it is anticipated that these would, if enacted, require consequential amendment of other enactments, including primary legislation.

Justification for the procedure

483. Provision made under this power will be technical in nature and made for limited purpose. It is therefore considered appropriate for this power to be subject to the negative procedure, except in cases where primary legislation is being modified (including where it is amended, repealed or revoked) where the affirmative procedure is appropriate.

New section 309I (Applications for approval) in Part 18 of FSMA 2000.

Powers conferred on: the appropriate regulator (Bank / FCA)
Powers exercised by: direction
Parliamentary Procedure: none

Context and Purpose

484. New section 309I sets out the procedure for a relevant recognised body to apply for approval of a person to perform a designated senior management function. It contains powers for the regulator to direct firms on the manner in which the application must be made (section 309I(2)), information that must be contained in the application (section 309I(3)(b)), any further information that is required in order to determine an application

(section 309I(5)), the form of any such information, or the way in which it must be verified (section 309I(6)). Different directions may be given and different requirements imposed in relation to different applications or categories of application (section 309I(7)).

Justification for taking the powers

485. These powers are intended to ensure that a relevant recognised body applying for approval from the appropriate regulator under section 309G provides adequate information about the applicant, in a form which is appropriate for the case in question. The power allows the appropriate regulator to give different directions and impose different requirements, in relation to different applications, in order for the process to be adequately tailored to different categories of firms.

Justification for the procedure

486. The proposed power is not subject to Parliamentary procedure. There is no formal parliamentary oversight over the regulators' powers to give directions under FSMA 2000. HM Treasury believe that this is appropriate for section 309I as well. Parliamentary procedure would be inappropriate and would prevent the regulators from making decisions regarding individual entities in a timely manner.

New section 309J(3) (Vetting by relevant recognised bodies) and new section 309Z(3) (Issuing certificates) in Part 18 of FSMA 2000.

Powers conferred on: the appropriate regulator (Bank / FCA)
Powers exercised by: rules made in accordance with Part 9A of FSMA 2000 (for FCA rules) and in accordance with the provisions of Part 9A that are applied to the Bank by paragraph 10 of Schedule 17A (as it will be amended by this Bill) (for Bank rules).
Parliamentary Procedure: none

Context and Purpose

487. New section 309J provides that, before submitting an application for approval of a person to perform a designated senior management function, a recognised body must satisfy itself that the person is a fit and proper person to perform that role. New section 309Z provides that a recognised body can only issue a certificate to a person in relation to a specific function if satisfied that the person is a fit and proper person to perform that role. In deciding whether it is so satisfied in relation to both these provisions, the recognised body must have regard to whether the person has (i) obtained a specified qualification, (ii) has undergone or is undergoing specified training, (iii) possesses a specified competence or (iv) has specified personal characteristics. Sections 309J(3) and 309Z(3) contain powers for the appropriate regulator (the Bank or the FCA, as the case may be) to specify these matters in its rules.

Justification for taking the power

488. The type and level of qualification, training, level of competence and personal characteristics that a person should be expected to have in order to be considered "fit and proper" will vary depending on which kind of body the SM&CR is being applied to, and may change over time (e.g. as new qualifications and training opportunities are developed). Clause 53 allows the appropriate regulator to make different rules in relation to different functions, activities or types of recognised body, in order to ensure the matters under consideration are proportionate and tailored to different categories of firms.

Justification for the procedure

489. There is no parliamentary procedure. Rules made by the regulators under FSMA 2000 do not have formal Parliamentary oversight, but are subject to various procedural requirements which are set out in Part 9A of FSMA 2000 for the FCA, and which are applied where appropriate to the Bank by paragraph 10 of Schedule 17A to FSMA 2000. These procedural requirements will apply to these powers, and as such it is not considered appropriate to provide for formal parliamentary oversight. This accords with the expectations under a FSMA 2000 model of regulation.

New section 309N (Changes in responsibilities) in Part 18 of FSMA 2000.

Powers conferred on: the appropriate regulator (Bank / FCA)
Powers exercised by: rules made in accordance with Part 9A of FSMA 2000 (for FCA rules) and in accordance with the provisions of Part 9A that are applied to the Bank by paragraph 10 of Schedule 17A (as it will be amended by this Bill) (for Bank rules); direction.
Parliamentary Procedure: none

Context and Purpose

490. New section 309N(3) provides for the appropriate regulator (the Bank or the FCA, as the case may be) to make rules relating to whether a change in the aspects of the relevant recognised body's affairs which a person is responsible for managing is to be considered notifiable to the regulator. The appropriate regulator also has the power in new section 309N(4) to direct the form in which the applicant may be required to submit and verify information, when informing the regulator of a notifiable change.

Justification for taking the powers

491. The type of change in responsibilities which ought to be notified to the regulator will vary by type of firm and function, and therefore should be determined by the relevant regulator. The relevant regulator is also best placed to determine the form in which the applicant should submit information.

Justification for the procedure

492. There is no parliamentary procedure. Rules made by the regulators under FSMA 2000 do not have formal Parliamentary oversight, but are subject to various procedural requirements which are set out in Part 9A of FSMA 2000 for the FCA, and which are applied where appropriate to the Bank by paragraph 10 of Schedule 17A to FSMA 2000. These procedural requirements will apply to these powers, and as such it is not considered appropriate to provide for formal parliamentary oversight.

493. The proposed power of direction is also not subject to Parliamentary procedure. There is no formal parliamentary oversight over the regulators' powers to give directions under FSMA 2000. HM Treasury believe that this is appropriate for section 309N as well. Parliamentary procedure would be inappropriate and would prevent the regulators from making decisions regarding individual entities in a timely manner.

494. These arrangements accord with the expectations under a FSMA 2000 model.

New section 309O(5) (Withdrawing approval) in Part 18 of FSMA 2000.

Powers conferred on: the appropriate regulator (Bank / FCA)
Powers exercised by: rules made in accordance with Part 9A of FSMA 2000 (for FCA rules) and in accordance with the provisions of Part 9A that are applied to the Bank by paragraph 10 of Schedule 17A (as it will be amended by this Bill) (for Bank rules); direction.
Parliamentary Procedure: none

Context and Purpose

495. New section 309O(5) provides for the appropriate regulator (the Bank or the FCA, as the case may be) to specify in its rules the meaning of "specified interval", which determines how often a relevant recognised body must consider whether there are grounds on which the appropriate regulator could withdraw a senior manager's approval under section 309G, and, if relevant, notify the appropriate regulator of those grounds.

Justification for taking the powers

496. The interval at which the regulator must consider whether there are grounds to withdraw approval will vary by type of firm and function, and therefore should be determined by the relevant regulator. The clause allows the appropriate regulator to specify different intervals in relation to different functions, activities or types of recognised body, in order to ensure they are proportionate and tailored to different categories of firms.

Justification for the procedure

497. There is no parliamentary procedure. Rules made by the regulators under FSMA 2000 do not have formal Parliamentary oversight, but are subject to various procedural requirements which are set out in Part 9A of FSMA 2000 for the FCA, and which are applied where appropriate to the Bank by paragraph 10 of Schedule 17A to FSMA 2000.

These procedural requirements will apply to these powers, and as such it is not considered appropriate to provide for formal parliamentary oversight.

498. These arrangements accord with the expectations under a FSMA 2000 model.

New section 309Q(4) (Varying approval at request of relevant recognised body) in Part 18 of FSMA 2000.

Powers conferred on: HM Treasury
Powers exercised by: regulations made by statutory instrument
Parliamentary Procedure: negative

Context and Purpose

499. Under new section 309Q, a relevant recognised body may apply to the appropriate regulator to vary an approval that has been given subject to conditions under section 309G. New section 309Q(3) requires the appropriate regulator to determine whether to grant a condition or give a warning notice before the end of the consultation period. New section 309Q(4)(a) provides that HM Treasury can prescribe the length of the consultation period, and different periods may be prescribed in relation to different types of relevant recognised bodies. If no such period is prescribed, new section 309Q(4)(b) provides that the consultation period is equal to a period of three months beginning with the day on which it receives the application to vary the approval.

Justification for taking the powers

500. It may be appropriate to vary the length of the consultation period for different types of firms. This power enables HM Treasury to provide for a period other than the default three-month period for specified types of firms.

Justification for the procedure

501. The negative procedure is appropriate for regulations made in exercise of these powers, which are restricted to a single and specific matter.

New section 309Z1 (Rules of conduct) in Part 18 of FSMA 2000.

Power conferred on: the appropriate regulator (Bank / FCA)
Power exercised by: rules made in accordance with Part 9A of FSMA 2000 (for FCA rules) and in accordance with the provisions of Part 9A that are applied to the Bank by paragraph 10 of Schedule 17A (as it will be amended by this Bill) (for Bank rules).
Parliamentary Procedure: none

Context and Purpose

502. Under new section 309Z1, the appropriate regulator (the Bank or the FCA, as the case may be) may make rules about the conduct of approved senior managers, employees and directors of relevant recognised bodies.

503. Rules under this section may include provision requiring a relevant recognised body to notify its employees of the rules that apply to them, and to take specified steps to secure that such persons understand how those rules apply in relation to them. They can also include provision requiring a relevant recognised body to notify the appropriate regulator if the body takes disciplinary action in relation to a person.

Justification for taking the power

504. The conduct rules that are appropriate to impose may vary by type of body and should be determined by the relevant regulator, as is the case for the existing SM&CR in Part V of FSMA 2000 for banks, insurers and other authorised persons. They will also need to be changed over time, for example to take account of developments in the financial services industry or changes in the law and regulation which apply to firms.

Justification for the procedure

505. There is no parliamentary procedure. Rules made by the regulators under FSMA 2000 do not have formal Parliamentary oversight, but are subject to various procedural requirements which are set out in Part 9A of FSMA 2000 for the FCA, and which are applied where appropriate to the Bank by paragraph 10 of Schedule 17A FSMA 2000. These procedural requirements will apply to these powers, and as such it is not considered appropriate to provide for formal parliamentary oversight.

506. These arrangements accord with the expectations under a FSMA 2000 model.

New section 309Z8 (Power to apply this Chapter to credit rating agencies) in Part 18 of FSMA 2000.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

507. New section 309Z8(1) gives HM Treasury power to provide by regulations for the provisions of this Chapter 2A to apply to registered CRAs as it applies to a type of relevant recognised body specified in regulations under section 309A. Regulations made under this provision must provide for the FCA to be the "appropriate regulator" for CRAs (section 309Z8(2)). The power may modify legislation, including any provision of FSMA 2000 (section 309Z8(3)).

508. As with the power in section 309A (the power to apply this SM&CR to certain types of recognised body), this power will enable HM Treasury to apply the regime to a particular type of body – in this case CRAs. A separate power is needed for CRAs, as – unlike the other bodies to which this regime can be applied - they are not recognised bodies under Part 18 FSMA 2000.

Justification for taking the power

509. The approach set out in section 309Z8 gives HM Treasury the option to extend this SM&CR to CRAs in the future, should it decide to do so, and following further specific consultation on that issue. This separate power to apply the regime to CRAs reflects the fact that (unlike CCPs, CSDs and RIEs) CRAs are not "recognised bodies" for the purpose of Part 18 of FSMA 2000, and instead are regulated for the most part under Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, as that regulation has been retained in UK law following EU Exit (the "CRAR").

510. In applying the regime to CRAs, it is likely to be necessary to modify the provisions of this Chapter, and it may be necessary to modify or amend provisions of other legislation – in particular, FSMA 2000 and the CRAR.

Justification for the procedure

511. The affirmative procedure is considered to be appropriate. This is an extensive power to apply the regime to CRAs, and in so doing, to modify, amend, repeal or revoke primary and subordinate legislation, or retained direct EU law.

PART 4 – CENTRAL COUNTERPARTIES IN FINANCIAL DIFFICULTIES

Paragraph 2 of Schedule 11: Removal of impediments to the exercise of stabilisation powers

- Sub-paragraph 1 of paragraph 2 of Schedule 11: Power to give directions to a CCP to remove impediments to the exercise of stabilisation powers

  Power conferred on: the Bank of England
  Power exercised by: direction made by the Bank of England
  Parliamentary Procedure: None

Context and Purpose of Schedule 11

512. Central counterparties (CCPs) are an integral and essential part of the financial services sector. They are designed to reduce risks in the financial services sector. However, they are also a source of systemic risk. Although the risk of a CCP failure is very low, the consequences of any CCP failure are significant, and would have far ranging consequences for the entire financial services system. A CCP failure scenario is also unpredictable given the limited number of CCPs globally that have failed. It is therefore appropriate and proportionate to have a regime to ensure that any CCP failure is managed effectively and efficiently.

513. For the reasons given above, the UK has an existing resolution regime for CCPs, which confers a limited set of powers on the Bank of England to manage a CCP failure. However, these powers are not considered sufficient for the Bank of England to either resolve a CCP efficiently or effectively mitigate the possible risks of a CCPs failure, including risks to financial stability and public funds, and the substantial risk of market contagion. The Bill contains, in Schedule 11, an expanded resolution regime for CCPs including a number of new tools that the Bank of England may use to resolve a CCP. This regime brings the CCP resolution and recovery regime more fully into line with that which is available in relation to banks under the Banking Act 2009. In particular, the regime allows for eight stabilisation options:

a. Transfer to a private sector purchaser;
b. Transfer to a bridge CCP;
c. Transfer of ownership;
d. Terminating clearing member's contracts (otherwise known as "tear up");
e. Making a cash call;
f. Reducing variation margin gain payments;
g. Writing down liabilities;
h. Taking control of the CCP.

514. These are achieved through the use of stabilisation powers – being the power for the Bank of England to make share transfer instruments, property transfer instruments, and other resolution instruments in respect of the CCP.

515. As part of its existing resolution powers with regard to CCPs the Bank of England only has limited transfer powers (to transfer ownership to a person or bridge institution, or to sell all or part of a CCP to a private sector purchaser). The new suite of stabilisation options

compares to five stabilisation options under the banking resolution regime. Where the stabilisation options differ between CCPs and banks, this is to address the differing way in which a CCP operates and conducts business.

Context and Purpose of Paragraph 2 of Schedule 11

516. Paragraph 2 of Schedule 11 allows the Bank of England to give directions to CCPs to address any impediments to the use of the Bank of England's stabilisation powers in respect of the CCP. Sub-paragraph (2) outlines a non-exhaustive list of the different actions the Bank of England may specify in such direction.

517. Sub-paragraphs (4) and (5) outline that the Bank of England must consult the relevant authorities and have regard to the potential impacts of giving the direction before using this power.

518. Sub-paragraph (6) clarifies that directions can be given to a specific CCP, a class of CCPs or with general effect to all CCPs.

519. An equivalent power exists under the resolution regime for banks, at section 3A of the Banking Act 2009. No equivalent power exists however in relation to CCPs at present.

Justification for taking the powers

520. Given the unpredictable nature of CCP resolution, and also developing market structures, it is considered appropriate for the Bank of England to be able to give directions to CCPs to remove impediments to resolvability, given the benefits this will ultimately bring to the use of the new stabilisation powers. The power will give the Bank of England the tools it needs to respond to specific scenarios, and to ensure that the stabilisation powers can be used effectively. The power would enable the Bank of England to require a CCP to make changes to its arrangements that would ultimately ensure the resolution of a CCP would be effective. The absence of such a power to direct the removal of impediments leaves open the possibility that operational factors within the CCP could hamper any subsequent resolution. This is also in line with the precedent set for banks in the Banking Act 2009.

521. It is expected that the Bank of England would utilise this power as needed alongside its day-to-day functions for CCP supervision and crisis management.

522. It is HM Treasury's opinion that this power is not legislative in nature, but rather is properly seen as part of the Bank of England's day-to-day supervisory function in relation to CCPs.

Justification for the procedure

523. It is considered that no Parliamentary oversight is required in relation to the exercise of this power by the Bank of England given the use of the power forms part of the Bank of England's day-to-day functions for CCP supervision and crisis management. Furthermore, this mirrors the existing resolution regime for banks (section 3A Banking Act 2009). Finally, examples of the types of direction the Bank of England may issue are specified in paragraph 2 sub-paragraph (2).

Paragraph 4 of Schedule 11: Resolution plans

- sub-paragraph 1 of paragraph 4 of Schedule 11: Power to impose requirements on the Bank of England to create and maintain a resolution plan for central counterparties ("CCPs")

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

524. This power gives HM Treasury the ability to make regulations in order to set certain requirements on the Bank of England, the UK's resolution authority, in relation to the resolution plans it develops for UK CCPs.

525. Sub-paragraph (2) of paragraph 4 gives examples of what the regulations would provide for, including the information that must be contained within a resolution plan, how frequently the Bank of England should review plans, and with whom the Bank of England should share copies of plans.

526. It is envisaged that any regulations would create provisions that are broadly comparable to Part 5 of the Bank Recovery and Resolution (No2) Order[31], which sets similar requirements on the Bank of England regarding resolution plans it maintains for banks and building societies.

Justification for taking the power

527. The Bank of England is the UK's resolution authority, and creation and maintenance of resolution plans are an essential part of its role to plan and prepare for the failure of financial institutions. This power granted in paragraph 4 of Schedule 11 importantly ensures that the Bank of England has effective and operational strategies to resolve firms. As mentioned at paragraph 523 above, requirements are already imposed on the Bank of England in relation to its role in resolution planning for banks and building societies. The power would enable HM Treasury to set similar resolution planning requirements on the Bank of England in relation to the resolution of CCPs.

528. The government considers it appropriate to set these requirements in regulations, since resolution planning encompasses the highly detailed aspects of how the Bank of England prepares for a resolution, as opposed to covering the specific use of its resolution powers. In addition, it is possible that the details of resolution planning may need to evolve frequently over time, for example in response to contingency planning carried out by the Bank of England or changes to international standards set in resolution planning guidance provided by the Financial Stability Board ("FSB"). Setting these detailed requirements in regulations also mirrors the approach adopted under the resolution regime for banks, ensuring the statutory frameworks for bank and CCP resolution are broadly comparable

[31] S.I 2014/3348.

and consistent, which will help maintain financial market confidence in the resolution regime overall.

Justification for the procedure

529. It is considered appropriate that regulations made using this power be subject to the negative procedure, since the power is narrow in scope and deals solely with the operational preparedness and planning for CCP failures, and clearly outlines the examples of where the power would be used and why.

Paragraph 7 of Schedule 11: Removal of directors and appointment of temporary managers

- sub-paragraph 6(c) of paragraph 7*:* Power to amend definition of "relevant requirement" in relation to the conditions for use of the Bank of England's power to remove a director/senior manager of a CCP and the power to appoint a temporary manager.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

530. In cases of significant financial deterioration or serious infringement of certain regulatory requirements or the CCP's own rules, it is considered necessary for the Bank of England to have the power to replace the incumbent management as a pre-resolution step to seek to stabilise the CCP without the need to exercise the suite of stabilisation powers. Accordingly, paragraphs 5 and 6 provide the Bank of England with the power to remove a director or senior manager from a CCP and appoint a temporary manager in their place, in circumstances where a CCP is not being placed by the Bank of England into resolution.

531. The use of this power is subject to a number of conditions, which are set out in paragraph 7, which include either a significant deterioration in the financial situation of a CCP or a serious infringement by the CCP of a "relevant requirement". This is to ensure that, in instances where a CCP is in financial difficulty or is found to be non-compliant with statutory requirements and obligations, the Bank of England can act to remove and replace the CCP's management.

532. Sub-paragraph (6) defines a relevant requirement as one imposed by or under FSMA 2000 and the European Market Infrastructure Regulation ("EMIR"), as onshored into UK law. It is of course conceivable that, as markets and legislation develop, there will be other requirements which should be considered "relevant requirements" for this purpose. As such, the power outlined in sub-paragraph (c) of the definition would allow HM Treasury to make regulations specifying other legal enactments that could impose a relevant requirement.

533. The power is analogous to provisions in sections 71D and 204A of FSMA 2000, which set out similar powers in relation to banks.

Justification for taking the power

534. As mentioned at paragraph 528 above, paragraph 7 of Schedule 11 sets out conditions for the Bank of England to be able to take action against a CCP's senior management in cases of a serious infringement by the CCP of a relevant requirement, such as refusal to comply with a requirement or direction or failure to act in line with its statutory obligations.

535. Currently it is envisaged that any relevant requirements will be set out predominantly in FSMA 2000 and onshored EMIR, since these are the pieces of legislation that underpin CCP regulation. However, taking a power will enable HM Treasury to respond to unforeseen changes in the legislative landscape and potential new relevant requirements being introduced under different legislation, including in relation to the outcome of the application of the powers in Part 1 of this Bill to EMIR. This will in turn ensure that the Bank of England's powers continue to work effectively. This is particularly pertinent given the significant changes to financial services legislation to be enacted by Part 1 of this Bill.

536. Moreover, there are a number of safeguards built into the legislation to provide further restrictions over the Bank of England and Treasury's powers to remove a director or senior manager. These include, for example, the provisions in paragraph 10 of Schedule 11 permitting a CCP aggrieved by the removal of a director or senior manager to refer the matter to the Tribunal.

Justification for the procedure

537. It is considered appropriate that regulations made using this power be subject to the negative procedure, since the power is likely to be used in a limited and targeted way to provide for amendments to ensure the Bank of England's power to replace incumbent management of CCPs pre-resolution remains effective. Furthermore, it is noted that the power at section 204A of FSMA 2000 is subject to the negative procedure (by virtue of section 429 of FSMA 2000).

Paragraph 22 of Schedule 11: Pre-resolution valuation

- sub-paragraph 10 of paragraph 22: Power to set out further details regarding the methodology for carrying out an independent valuation prior to exercise of stabilisation powers.

Power conferred on: Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

538. This power forms part of an overall framework set out at paragraph 22 requiring the Bank of England to ensure a valuation is carried out before it exercises the stabilisation powers. The purpose of a valuation is to ensure that the assets and liabilities of the CCP are valued and to inform the decision as to which stabilisation options should be used.

539. The power set out at sub-paragraph (10) confers a power on HM Treasury to set out in regulations further details of the methodology to be used by any independent valuer for

assessing the value of the assets and liabilities of a CCP, and the methodology for calculating and including a buffer for additional losses in a provisional valuation. This will ensure that any valuation is required to be carried out against a specified methodology, minimising the risk of challenge on a subjective basis. As set out at sub-paragraph (11), HM Treasury must consult the Bank of England before making regulations.

540. The power mirrors a similar provision in section 6E of the Banking Act 2009, which grants the Bank of England the ability to make technical standards in relation to a valuation it performs before exercising the stabilisation powers under the resolution regime for banks.

Justification for taking the power

541. Paragraph 22 sets out in some detail when a valuation should be carried out and on what grounds. However, it is considered appropriate that HM Treasury (in consultation with the Bank of England) is given discretion to determine the methodology for undertaking this valuation.

542. Consideration was given to the appropriate form of power, given that section 6E of the Banking Act 2009 uses technical standards (being a holdover from EU legislation). Given the aim to move away from Bank technical standards in legislation moving forward, it seems appropriate that the methodology should be housed in regulations, to minimise the risk of challenge to any valuation by way of judicial review (by limiting the grounds for judicial review that would be available). Given that this is a highly technical matter (and aligns with the Bank of England's broader remit as Resolution Authority and its role making equivalent technical standards for bank resolution) it is considered appropriate that regulations should be drafted in consultation with the Bank of England.

Justification for the procedure

543. It is considered appropriate that regulations made using this power be subject to the negative procedure, since the scope of the power is clearly and narrowly defined. It is intended to be used to deal with a highly technical issue, and Bank consultation will be required. It is noted that the equivalent provision in the Banking Act 2009 is not subject to parliamentary oversight.

Paragraph 25 of Schedule 11: Supplemental provisions for independent valuation

- sub-paragraph 2 of paragraph 25: Powers to confer specific functions on independent valuers carrying out a valuation before use of the power to write-down unsecured liabilities owed by a CCP

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

544. As mentioned in the section above, in order to ensure that assets and liabilities of the CCP are appropriately valued before resolution action is taken, paragraphs 22 to 26 of Schedule 11 set out a framework for a valuation to be carried out before the stabilisation

options are exercised. The valuation will inform the choice of stabilisation power, as well as ensuring powers are used effectively and appropriate value is ascribed in the case of a transfer of property or shares or a write-down.

545. As part of this framework, paragraph 24 requires that the Bank of England must appoint an independent valuer to conduct this valuation. Paragraph 25 follows on from this and provides HM Treasury with powers to make regulations to support the independent valuer in exercising their functions.

546. Paragraph 25(2) gives HM Treasury the power to make regulations conferring specific functions on independent valuers, including duties on an independent valuer regarding publication, disclosure and withholding of information. Sub-paragraph (3) provides that this power may also make provision around how this power should be enforced.

547. Sub-paragraph (5) gives HM Treasury the power to make regulations about the procedure to be followed by an independent valuer.

<u>Justification for taking the power</u>

548. As mentioned, these powers for HM Treasury to make regulations are designed to support an independent valuer to exercise their functions effectively and support the orderly use of the stabilisation options. As a CCP failure is highly scenario dependent, and the powers in this clause are intended to be used in response to a specific CCP failure, the government judges that it is appropriate to deliver provisions and requirements related to independent valuation by regulations.

549. The powers themselves are also necessarily tightly defined in scope, since they make provision for specific aspects of the independent valuation process, such as the functions of the valuer, the procedure to be followed by a valuer, and the reconsideration of and/or appeal against an independent valuer’s decision.

<u>Justification for the procedure</u>

550. It is considered appropriate that regulations made using this power be subject to the negative procedure, since the power is tightly defined in scope and intends to deal with a minor operational issue.

Paragraph 32 of Schedule 11: Cash call power

- sub-paragraph 3 of paragraph 32: Power to set the maximum cash amount that can be required from clearing members in exercise of the cash-call power and specify circumstances in which the Bank of England may require a CCP to use specified funds of specified clearing members.

  Power conferred on: HM Treasury
  Power exercised by: regulations made by statutory instrument
  Parliamentary Procedure: Negative

Context and Purpose

551. Paragraph 32 gives the Bank of England the power to require cash contributions from a CCP's clearing members, in order to absorb losses arising from a CCP failure and recapitalise a failing CCP to restore it to viability.

552. Sub-paragraph (3) grants HM Treasury a power to make regulations setting out the specific parameters around how the Bank of England's power can be used. Specifically, it allows HM Treasury to specify the maximum cash amount that the Bank of England can require from clearing members, to give clearing members more certainty and clarity over how they will be treated in a CCP resolution. It also allows the regulations to specify the circumstances in which the Bank of England may require a CCP to use specified funds of specified clearing members to satisfy all or part of that member's obligations under sub-paragraph (2). An example of this could be placing a clearing member into default where it cannot meet its cash call obligations, and using the failing member's initial and variation margin to absorb losses.

Justification for taking the power

553. It is considered that defining the parameters and limits of the Bank of England's cash call power should be delivered by regulations. The Bank of England will seek to use its resolution powers to limit the losses arising from a CCP failure. In support of this, the government must have the flexibility to specify the limits of the power, depending on the scale of loss absorbency required, and give the Bank of England additional flexibility over the use of its power to ensure it can be used to absorb losses effectively. Equally, with regard to the maximum cash call limit, it is important for the government to be able to exercise control over the maximum amounts so as not to give the Bank of England an unlimited power.

554. It is worth noting that, as set out in its February 2021 consultation and March 2022 consultation response, the government has already publicly stated its intention to limit the amount of cash called on members, specifically:
   a. Two times clearing members default fund contributions (for default losses)
   b. Three times clearing member default fund contributions (for non-default losses)

555. This therefore sets out a clear intent over how this regulation-making power would be used in the short-term. The government intends to make the necessary regulations as soon as practicable after Royal Assent of the Bill in order to achieve this policy.

Justification for the procedure

556. It is considered appropriate that regulations made using this power be subject to the negative procedure, since the scope of the power is clearly and narrowly defined. It is intended to be used to deal with a minor operational issue. The government has also set out clear and public intentions over how it intends to use this power in the short-term, as explained above.

Paragraph 34 of Schedule 11: Power to write-down unsecured liabilities

- sub-paragraph 7 of paragraph 34: Power to add to or amend the list of liabilities not affected by the power to write-down liabilities owed by a CCP

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

557. One of the stabilisation powers conferred on the Bank of England by paragraph 34 is the power to write-down unsecured liabilities owed by a failing CCP. The purpose of this stabilisation power is to allow the CCP to absorb losses, and recapitalise and restore it to viability.

558. It is of course necessary in the public interest that certain categories of unsecured liability should be excluded from such write-downs, and these are set out at sub-paragraph (4). They include, amongst other things, liabilities to employees, pension schemes and tax authorities. This is to ensure the write-down power does not have unintended consequences on the wider economy. The power at sub-paragraph (7) gives HM Treasury the power to make regulations to add to this list of excluded liabilities, or amend or omit any liability listed.

559. A comparable provision exists in section 48F of the Banking Act 2009, which relates to the bail-in option in the resolution regime for banks.

Justification for taking the power

560. While a number of categories of unsecured liability are already specified under sub-paragraph (4), it is considered necessary to have the ability to adapt as needed the list of excluded liabilities from the write-down power.

561. CCPs and their business models evolve over time meaning that new forms of liability that a CCP could owe could come into existence that may be appropriately included in the exclusion from write-down. The government and Bank have no way of knowing in advance what these might be.

562. Accordingly, it is deemed necessary for the government to have the power to adapt this list and ensure the write-down power both remains effective and does not have unintended economic consequences.

Justification for the procedure

563. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure. Given the breadth of potential new liabilities which could be excluded from the write-down power in future, it will be appropriate for Parliament to be able to scrutinise any changes or additions and ensure these remain suitable for the policy to remain effective. This is consistent with the precedent set by section 48F of the Banking Act 2009, which requires additions to the list of excluded liabilities in relation to bank bail in to be made by the draft affirmative procedure.

Paragraph 37 of Schedule 11: Priority between creditors

- sub-paragraph 1 of paragraph 37: Power to specify matters or principles which the Bank of England must have regard to in exercising the write-down power

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

564. This power follows from the power for the Bank of England to write-down unsecured liabilities owed by a CCP, the context and purpose of which is set out in relation to paragraph 34 above.

565. It is acknowledged that the power to write-down unsecured liabilities is a substantial power, potentially engaging rights protected pursuant to the Human Rights Act 1998, in particular Article 1 of Protocol 1 of the European Convention on Human Rights. As such, paragraph 37 provides a power for HM Treasury to make regulations specifying matters or principles that the Bank of England should have regard to when exercising its write-down power, for the purpose of ensuring that the treatment of liabilities in a write-down is suitably aligned with the treatment of liabilities in an insolvency.

566. Sub-paragraph (2) sets out examples of where this power can be used, including to specify the insolvency treatment principles in relation to the use of this power. Sub-paragraph (3) also clarifies that the power may amend paragraph 36(4) which sets out the insolvency treatment principles that are to be adhered to under the write-down power.

567. An equivalent power exists in the resolution regime for banks in relation to bail-in, under section 48G of the Banking Act 2009.

Justification for taking the power

568. It is considered that taking this power is appropriate. The proposed regulations would allow HM Treasury to specify matters to which the Bank of England should have regard to when conducting a write-down, including ensuring appropriate alignment with the treatment of liabilities in insolvency.

569. The insolvency treatment principles are the fundamentals of the insolvency creditor hierarchy, and so it is judged appropriate for HM Treasury to specify these in regulations to ensure that these are reflected in the write-down and that developments in insolvency

principles can be reflected. It is also judged necessary for HM Treasury to have the flexibility to allow the Bank of England to depart from these principles where appropriate, since it is not possible to plan in advance for every potential scenario where the authorities might need to clarify the extent of application of these principles.

Justification for the procedure

570. It is considered appropriate for regulations to be made using the draft affirmative procedure. The ability for HM Treasury to specify a departure from normal insolvency principles, whilst potentially necessary for an effective resolution, would necessarily require scrutiny from Parliament, to ensure that the approach is judged appropriate based on the emerging CCP failure scenario. This is consistent with the precedent set by section 48G of the Banking Act 2009, which requires regulations setting out what the Bank of England must have regard to when ordering a bail-in to be made by the draft affirmative procedure.

Paragraphs 75 and 76 of Schedule 11: Restriction and protection of partial property transfers

- paragraphs 75(2) and 76(2) of Schedule 11: Powers to restrict the making of partial property transfers in certain cases

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

571. This power stems from paragraph 54 which specifies what constitutes a property transfer instrument. In particular, paragraph 54 provides that any property transfer instrument made by the Bank of England may transfer part or all of a CCP's property, rights and liabilities in order to facilitate the private sector purchaser and bridge CCP stabilisation options, set out at paragraphs 27 and 29 respectively. Where only some of the CCP's property, rights and/or liabilities are transferred to a commercial purchaser or bridge bank (a partial property transfer), this necessarily means that there will be a rump of property, rights and/or liabilities that are left behind.

572. In the context of paragraph 54 allowing for both full and partial transfers of the property, rights and liabilities of the relevant CCP, paragraph 75 allows HM Treasury to make regulations imposing restrictions and conditions on the application of partial property transfers.

573. Similarly, paragraph 76 allows HM Treasury to make regulations imposing restrictions on the making of partial property transfers in instances where this might involve or affect protected arrangements. Sub-paragraph (1)(e) defines protected arrangements as security interests, title transfer collateral arrangements, set off arrangements and netting arrangements.

574. Equivalent provisions exist for the resolution regime for banks under sections 47 and 48 of the Banking Act 2009.

Justification for taking the power

575. The purpose of these regulation-making powers is to enable restrictions to be imposed by reference to the nature of the property, rights and liabilities which may or may not form part of the transfer. This may be important in order to ensure the success of a sale to a commercial purchaser, or to ensure the transfer of a CCP's property does not have unintended and destabilising consequences. In particular, it will give users of clearing services greater certainty over how a partial property transfer might affect their contractual rights.

576. Given a CCP failure is scenario dependent, it is considered necessary for HM Treasury to have the power to make regulations in order to specify the relevant requirements, restrictions and conditions in response to a specific CCP failure. It is likely that the contents of any regulations would need to be adapted to the situation at the time and the specific nature of the transfer of a CCP's property, and therefore cannot be provided on the face of the Bill.

Justification for the procedure

577. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure. Given the implications a partial property transfer could have on the contractual rights of clearing members, it is considered appropriate for Parliament to be able to provide scrutiny over any regulations made. This is consistent with the precedent set by sections 47 and 48 of the Banking Act 2009, which requires regulations restricting partial property transfers to be made by the draft affirmative procedure.

Paragraph 78 of Schedule 11: Regulations for safeguarding certain financial arrangements

- sub-paragraph 3 of paragraph 78: Powers to restrict the making of a write-down instrument in cases that involve, or where they might affect, protected interests

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

578. This power stems from the Bank of England's power to write-down liabilities of CCPs at paragraph 34 (the context and purpose for which is set out in paragraphs 557-559 of this memorandum above).

579. Paragraph 34 is naturally a wide power, allowing the Bank of England to make write-down instruments. Against this context, the power in paragraph 78 provides HM Treasury with the ability to make regulations to restrict the Bank of England's exercise of its write-down power, where doing so may involve or affect protected arrangements. By extension, the power also permits HM Treasury to impose conditions on the use of this power, require write-down instruments to include specified provision, provide for a write-down instrument

to be void or voidable, and specify principles to which the Bank of England must have regard when using its power.

580. Sub-paragraph (1) defines protected arrangements as security interests, title transfer collateral arrangements, set off arrangements and netting arrangements.

581. An equivalent provision exists for the resolution regime for banks under section 48P of the Banking Act 2009.

Justification for taking the power

582. The purpose of these regulation-making powers is to enable restrictions to prevent the exercise of the write-down power from having unintended consequences on some of the critical functions of financial markets, which could have destabilising effects.

583. Given a CCP failure is scenario dependent, it is considered necessary for HM Treasury to have the power to make regulations in order to specify the restrictions needed in response to a specific CCP failure. It is likely that the contents of any regulations would need to be adapted to the situation at the time and therefore details cannot be provided on the face of the Bill and it is considered appropriate for them to be set out in regulations at the time of a CCP failure.

Justification for the procedure

584. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure. Given the implications a write-down could have on financial markets, it is considered appropriate for Parliament to be able to provide scrutiny over any regulations made. This is consistent with the precedent set by section 48P of the Banking Act 2009.

Paragraph 85 of Schedule 11: Deferment of provisions

- sub-paragraph 1 of paragraph 85: Power to make provision for the suspension or waiver of provisions made when stabilisation powers are exercised

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

585. Paragraph 85 allows HM Treasury to make regulations to permit enforcement of certain obligations imposed on industry participants during a resolution to be "deferred" i.e., suspended or waived.

586. Sub-paragraph (2) sets out examples where this power could be used, including specifying things to which the Bank of England must have regard before deferring enforcement of an obligation, the procedure for deferring enforcement, the maximum time period any deferral may take effect, and ensuring any deferral is reviewed.

587. The power is intended to deliver the government's policy, as set out in its February 2021 consultation, to allow the Bank of England to delay enforcement of a clearing member's obligations in resolution, should such enforcement during the resolution of a CCP present a risk to financial stability.

Justification for taking the power

588. It is considered necessary for HM Treasury to be able to make regulations to set out the detailed parameters of this power. A power to make regulations will allow the authorities to adapt the statutory framework quickly and as necessary to respond to the specifics of a CCP failure.

589. That said, the government does have a clear short-term policy on how it expects the Bank of England to use its ability to defer enforcement, as set out in its February 2021 consultation. For example, it is the government's expectation that the Bank of England should be able to enforce outstanding obligations resulting from any delay at any time up to 18 months after a resolution, if at the relevant time the reasons for refraining from their enforcement no longer exist.

590. The government therefore intends to use this power to make regulations as soon as practicable after Royal Assent of the Bill in order to implement its immediate term policy framework.

Justification for the procedure

591. While deferral could be controversial and attract significant interest at industry level, the significance of any deferral will be case specific. The regulations themselves will not specify or limit the circumstances in which the Bank can make a decision to defer or waive a provision but will instead set out the procedural framework underpinning such a decision. Accordingly, the negative procedure is appropriate for this power.

Paragraph 87 of Schedule 11: Compensation scheme

- sub-paragraph 1 of paragraph 87: Power to make provision for protecting the financial interests of relevant persons in connection with resolution action

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

592. Paragraph 87 provides HM Treasury with powers to provide compensation to relevant persons who are left worse off under resolution action than they would have been if the CCP had been wound up under normal insolvency proceedings. This power delivers the "No Creditor Worse Off" (NCWO) safeguard, and is designed to protect the financial interests of CCP shareholders and clearing participants.

593. Sub-paragraph (2) sets out the provisions that regulations may provide for, including determining whether relevant persons should be paid compensation and ensuring any compensation is paid.

594. Sub-paragraph (3) sets out the specific things to which HM Treasury must have regard when determining whether compensation should be paid.

595. Sub-paragraph (6) provides for compensation to be paid for by HM Treasury or any other specified person.

Justification for taking the power

596. The NCWO safeguard is an important pillar of the resolution regime for CCPs, since it provides clarity to industry participants over how they can expect to be treated in resolution. Since compensation arrangements can only be designed and provided for in direct response to a CCP failure, and would only be required if relevant persons were deemed to be owed compensation, these details cannot be provided on the face of the Bill and it is considered appropriate for them to be set out in regulations at the time of a CCP failure.

Justification for the procedure

597. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure. The contents of any regulations made under the power are highly scenario dependent, and may carry potential risks to public funds being needed to fund compensation owed. It is therefore considered appropriate for Parliament to fully scrutinise the details of any compensation arrangements.

Paragraph 95 of Schedule 11: Consideration and terms of continuity obligations

- sub-paragraph 1 of paragraph 95: Power to make provision for protecting the financial interests of relevant persons in connection with resolution action

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

598. This power stems from paragraphs 89 and 92, which imposes requirements in relation to a CCP that has been subject to the property and share transfer powers.

599. Paragraph 89 states that a residual CCP (meaning a CCP, all or part of whose business has been transferred by a property transfer instrument) must provide such services and facilities to enable a commercial purchaser or bridge CCP to operate the transferred business effectively. Paragraph 92 similarly requires, in cases where a CCP has been transferred by a share transfer instrument (a transferred CCP), that former CCP group companies must provide such services and facilities to enable the transferred CCP to operate effectively. In both cases, this is referred to as the "continuity obligation", and

ensures that provisions are in place to allow a CCP to continue operating.

600. Paragraphs 90 and 93 provide additional special continuity obligations in relation to property and share transfers, including instances where the Bank of England may cancel or modify the terms of a contract between the residual CCP/its transferee and any former group company, or between a transferred CCP and a former group company.

601. In all continuity obligation cases the residual or transferred CCP has a right to receive reasonable consideration. In addition, as set out in paragraphs 90 and 93 in exercising its powers the Bank of England must aim to preserve provisions in contracts and agreements that would be expected in arrangements concluded between parties dealing at arm's length.

602. The power at paragraph 95 permits HM Treasury to make regulations to support effective continuity obligations, in two ways:

a. As per sub-paragraph (1)(a), to determine what amounts to "reasonable consideration"
b. As per sub-paragraph (1)(b), to specify matters which are or not to be considered in determining what provisions would be expected in arrangements concluded between parties dealing at arm's length

603. Equivalent provisions exist in the resolution regime for banks, as set out at section 69 of the Banking Act 2009.

<u>Justification for taking the power</u>

604. This power is required to enable HM Treasury to ensure the ability of the ongoing CCP (whether a transferred CCP, or a CCP owned by a commercial or bridge purchaser) to provide clearing services, by ensuring it is not commercially disadvantaged by the need to reprocure at speed essential services/facilities.

<u>Justification for the procedure</u>

605. It is considered appropriate for this power to be subject to the negative procedure. This power may need to be exercised on an urgent basis to respond to the failure of a CCP and the resolution thereof. The regulations would be limited in scope and of a technical and market-based nature. It should be noted that the equivalent provision for banks is subject to the negative procedure (section 69(2)(b) Banking Act 2009), and therefore this maintains parity between regimes.

Paragraph 105 of Schedule 11: Tax

- sub-paragraph 1 of paragraph 105: Power to make provision about the fiscal consequences of the exercise of a stabilisation power

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

606. Paragraph 105 permits HM Treasury to make regulations in relation to the interplay of the taxation regime with the exercise of stabilisation powers. Sub-paragraph (2) sets out the taxes in scope of this power, including capital gains tax, corporation tax, income tax, inheritance tax, stamp duty, stamp duty land tax, and stamp duty reserve tax.

607. Sub-paragraph (3) specifies that regulations may apply to a range of circumstances, including any action done in connection with the exercise of a stabilisation power, things transferred or affected by use of powers, a transferor or transferee or any persons affected by use of a power.

608. Sub-paragraph (4) sets out the effects that regulations may have, including the ability to modify or disapply an enactment, provide for an action to have or not have specified consequences, withdraw or restrict a tax relief and modify a charge to tax.

609. Sub-paragraph (5) sets out the time period applicable to anything set out under the regulations.

610. Sub-paragraph (7) allows HM Treasury to amend the list of taxes in sub-paragraph (2).

611. Equivalent provisions exist under the resolution regime for banks, at section 74 of the Banking Act 2009.

Justification for taking the power

612. It is considered necessary for HM Treasury to be able to make regulations to modify or disapply the effects of taxes in relation to a CCP resolution, given the range of fiscal and economic consequences that could otherwise arise. As a CCP failure is scenario dependent and unpredictable, it is not known at this stage exactly which taxes would need to be changed or disapplied in response to a CCP failure or in what way. The ability to make regulations therefore gives the government the flexibility needed to respond appropriately to an emerging crisis scenario.

Justification for the procedure

613. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure. The ability to modify or disapply taxes could itself have significant fiscal and economic effects, including impacts on overall government receipts, and it is therefore appropriate for Parliament to fully scrutinise the details of any changes made.

Paragraph 111 of Schedule 11: Public funds

- sub-paragraph 3 of paragraph 111: Power to specify considerations to be taken into account when determining whether resolution action has implications for public funds

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

614. Paragraph 111(1) sets out that the Bank of England cannot take resolution action without HM Treasury's consent if the exercise of that power would likely have implications for public funds.

615. Sub-paragraph (3) gives HM Treasury the power to specify the considerations which are to be, or not to be, taken into account in determining whether action has implications for public funds.

616. The requirement for the Bank of England to obtain Treasury consent where public funds are at risk is an important principle of the resolution regime, and links to the special resolution objective to protect public funds (paragraph 15(6)).

617. An equivalent power exists under the resolution regime for banks, as set out at section 78 of the Banking Act 2009.

Justification for taking the power

618. It is considered appropriate for HM Treasury to have the power to make regulations specifying factors taken into account when determining if there are implications for public funds, given HM Treasury's overall responsibility for the public finances. Whilst sub-paragraph (1) will already prevent the Bank of England from taking action that puts public funds at risk without HM Treasury consent, the power at sub-paragraph (3) ensures the government is able to exercise its duty to protect the public finances to the fullest extent.

Justification for the procedure

619. HM Treasury already has a clear responsibility in protecting the public finances, and this power allows it to perform that already well understood role. Whilst it is appropriate that the government is fully transparent with Parliament over its intentions to ensure public funds are protected, the regulations would simply set out the matters HM Treasury has taken or will take into account when providing its consent to the Bank of England to allow stabilisation options to be exercised. It is considered appropriate that regulations made using this power be subject to the negative procedure.

Paragraph 152 of Schedule 11: Provision of financial assistance

- sub-paragraph 2 of paragraph 152: Power to provide for a specified activity or transaction to be or not be treated as financial assistance

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Negative

Context and Purpose

620. Paragraph 152 permits HM Treasury to make regulations to provide that a specified activity or transaction is to be or not be treated as financial assistance to a CCP (e.g. the

giving of guarantees or indemnities to a failing CCP). Where HM Treasury has given financial assistance to CCPs, additional conditions must be met in order for the Bank of England to exercise certain stabilisation options.

621. This clause supports HM Treasury's wider responsibility for protecting public funds and its role in authorising the use of stabilisation options where there are implications for public funds.

Justification for taking the power

622. It is considered appropriate for HM Treasury to have the power to make regulations specifying the activities and transactions that should or should not be treated as financial assistance, given HM Treasury's overall responsibility for the public finances and the need for appropriate conditions to be met where HM Treasury has provided financial support to a CCP.

Justification for the procedure

623. HM Treasury already has a clear responsibility in protecting the public finances, and this power allows it to perform that already well understood role. It is considered appropriate that regulations made using this power be subject to the negative procedure.

Paragraph 153 of Schedule 11: Modifications to the law

- sub-paragraph 1: Power to modify the law to enable the stabilisation powers to be used effectively

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: Draft/made affirmative

Context and Purpose

624. Paragraph 153 provides HM Treasury with the power to amend the law in order to ensure the stabilisation options can be used effectively, having regard to the special resolution objectives. Sub-paragraph (2) sets out instances where this power can be used. Sub-paragraph (3) provides that regulations may make provision which has retrospective effect.

625. An equivalent power exists in the resolution regime for banks, under section 75 of the Banking Act 2009, which currently applies to CCPs by virtue of section 75(5)(cb) of that Act.

Justification for taking the power

626. This is a far-reaching power but one that HM Treasury considers necessary in order to implement the resolution regime for CCPs effectively, and to maintain the current legal position.

627. No CCP has failed globally since the international standards for CCP recovery and resolution were developed by the FSB. Resolution powers for CCPs are therefore untested,

and whilst the powers introduced by this Bill are intended to mitigate risks to financial stability and public funds as far as possible, there naturally remains a degree of uncertainty around the effectiveness of the powers in practice.

628. A CCP failure also carries severe risks both to financial stability and public funds, given the criticality of CCPs and clearing services to the operation of financial markets. If a CCP were to fail, there would be high risks of contagion across the financial system, and the impacts would likely be akin to a system wide crisis. A CCP failure would also likely be fast burn in nature, with potential financial stability impacts crystallising within hours.

629. Retrospective provision is necessary as it may not be possible to identify the impediments to a particular resolution action in advance, given the pace at which, for example, transfers could be made and the complexity of the underlying legislation. Additionally, it would create an unacceptable level of legal uncertainty if changes could not take effect simultaneously with the particular transfer.

630. It is therefore considered appropriate that HM Treasury has this power to make regulations, allowing it to respond quickly and flexibly to potential risks to CCPs.

<u>Justification for the procedure</u>

631. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure or, in situations where HM Treasury considers it appropriate for the regulations to come into force without delay, the made affirmative procedure. Given the potential wide-ranging application of such regulations, and the fact this power grants the ability to amend primary legislation by statutory instrument, it will be appropriate for Parliament to be able to scrutinise any use of the power.

Paragraph 156 of Schedule 11: Interpretation of central counterparty group company

- sub-paragraph 1(b) of paragraph 156: Power to specify conditions that must be met to satisfy the definition of a CCP group company

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

<u>Context and Purpose</u>

632. Paragraph 156 sets out how references to a CCP group company in the Bill should be interpreted. There are references throughout Schedule 11 to the Bill where exercising stabilisation powers would have an effect on a CCP group company.

633. Sub-paragraph (1)(a) sets out the definition of a CCP group company. Sub-paragraph (1)(b) gives HM Treasury the power to specify in regulations conditions that, if met, would mean an undertaking would qualify as a CCP group company.

634. An equivalent power exists under the resolution regime for banks, at section 81D of the Banking Act 2009.

Justification for taking the power

635. It is considered necessary for HM Treasury to have the power to make regulations to define what would fall into the parameters of a CCP group company. This is because the structures of financial institutions are often highly complex, and the typical structures used may vary and develop over time. As such this power will ensure the government is able to respond to changing market norms.

Justification for the procedure

636. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure. Given the fact that these regulations will determine which companies fall within the CCP group company definition, it will be appropriate for Parliament to be able to scrutinise any changes or additions and ensure these remain suitable for the policy to remain effective.

Paragraph 165 of Schedule 11: Modified application of corporate law to CCPs in resolution

- sub-paragraph 1 of paragraph 165: Power to specify provisions of certain enactments which should apply for the purposes of Schedule 11, with or without modifications.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

637. Paragraph 165 provides HM Treasury with a power to set out in regulations modifications and applications of certain enactments to CCPs in resolution (being the Company Directors Disqualification Act 1986, Insolvency Act 1986, FSMA 2000, Companies Act 2006, Banking Act 2009, Bank Recovery and Resolution (No.2) Order 2014 ("BRRO No.2"), Insolvency (Northern Ireland) Order 1989 and Company Directors Disqualification (Northern Ireland) Order 2002) for the purposes of Schedule 11. Such modifications and applications of corporate law may be required in order to facilitate the effective use of the stabilisation powers and remove potential impediments to effective resolution of CCPs.

638. Part 17 of BRRO 2 applies (with modifications as appropriate) certain provisions of corporate law where stabilisation powers have been exercised in respect of banks. It is anticipated that any use of the power taken in paragraph 165 would engage with similar corporate law provisions.

Justification for taking the power

639. It is considered necessary for HM Treasury to have the power to make similar modifications and applications of corporate law for the purpose of ensuring that the stabilisation powers set out in Schedule 11 can be used effectively, and CCPs can be

resolved without impediments or obstacles arising from potentially applicable provisions.

640. It is considered appropriate that such applications and modifications should be set out in regulations, to ensure that HM Treasury can in due course respond to any changes to the enactments specified that might be relevant for the purposes of Schedule 11 going forward.

Justification for the procedure

641. It is considered appropriate that regulations made using this power be subject to the draft affirmative procedure, given that any regulations made pursuant to this power may have the effect of applying and modifying primary legislation for the purpose of Schedule 11, and thus Parliament should have the opportunity to scrutinise any use of this power.

PART 5 – INSURERS IN FINANCIAL DIFFICULTIES

Clause 51 and Schedule 12: Insurers in financial difficulties and write-down orders

- paragraph 3(4) of new Schedule 19B to FSMA 2000:

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

642. The context for the use of this power is the circumstance where the court makes a write-down order in relation to an insurer pursuant to the new section 377A of FSMA 2000. Such an order would reduce the value of one or more of an insurer's liabilities.

643. Part 1 of new Schedule 19B to FSMA 2000 prevents the creditors of an insurer subject to a write-down order from taking steps, without the permission of the court, to, for example, enforce security over the insurer's property.

644. The restrictions are similar to those that currently apply when an insurer is in administration. They are intended to help provide stability for an insurer under write-down by preventing volatility which might arise as a result of an insurer's counterparties, for example, enforcing security over its property.

645. Paragraph 3(3) of new Schedule 19B, prevents the restrictions in Part 1 of the Schedule affecting the operation of certain existing finance-related legislative provisions.

646. Paragraph 3(4) of new Schedule 19B confers a power on HM Treasury to amend the list of exclusions set out in paragraph 3(3).

Justification for taking the power

647. The justification for this power is to enable HM Treasury to address potential future changes to legislation or to financial arrangements into which insurers enter which may give rise to the need to add, vary or remove the exclusions in paragraph 3(3).

648. As it is not possible to anticipate all potential future changes in legislation or market practice, it is appropriate for this power to be broad with respect to the changes that can be made to paragraph 3(3). Equally, the power is inherently relatively narrow in scope as it only affects the exclusions from the restrictions in Part 1 of the Schedule.

Justification for the procedure

649. It is considered appropriate that any regulations made using this power be subject to the draft affirmative procedure in both Houses of Parliament, especially given that the power envisages changes to primary legislation and the amendments may involve policy considerations. As a result, it is appropriate that Parliament should be afforded the opportunity to scrutinise the detail of the changes made to the legislation and to seek

assurances from Treasury Ministers during the debates regarding the effects of the amendments to legislation.

Clause 51 and Schedule 12: Insurers in financial difficulties and write-down orders

- paragraph 9(3) of new Schedule 19B to FSMA 2000: power to modify list of legislative provisions for the purposes of which a determination of the value of an insurer's liabilities is to be carried out as specified.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

650. The context for the use of this power is the circumstance where the court makes a write-down order in relation to an insurer pursuant to the new section 377A FSMA 2000. Such an order would reduce the value of one or more of an insurer's liabilities.

651. Paragraphs 8 and 9 of new Schedule 19B to FSMA 2000 provide that, where an insurer's liabilities have been reduced by a write-down order, in determining the value of the insurer's liabilities for the purpose of certain provisions, no account is to be taken of the contingent or prospective value of the liability, or interest on the liability, arising from any expectation that the write-down order will be varied, further varied or cease to have effect, whether in relation to the liability or generally.

652. Paragraphs 8 and 9 of Schedule 19B address a risk that the effect of the write-down order could be undermined (leaving the insurer vulnerable to entry into insolvency proceedings) as a result of the reduction of the insurer's liabilities not being reflected on the insurer's balance sheet (instead being captured as a contingent liability).

653. Paragraph 9(3) of new Schedule 19B to FSMA 2000 provides HM Treasury with a power to amend the list of provisions in paragraph 9(2).

Justification for taking the power

654. This power allows HM Treasury to keep the list of provisions in paragraph 9(2) up to date. This is intended to ensure HM Treasury can address potential future changes in prudential and insolvency legislation, or the court's interpretation of legislation. This would have the effect of requiring account to be taken of the contingent or prospective value of written-down liabilities, or interest on the liabilities, which would risk undermining the effectiveness of the write-down regime.

655. As it is not possible to anticipate all potential future changes in legislation, or the court's interpretation of legislation, it is appropriate for this power to be broad in terms of the changes that can be made to paragraph 9(2). However, the government considers that the power is inherently relatively narrow in scope as it only affects the treatment of written-down liabilities for the purposes of insolvency provisions.

Justification for the procedure

656. It is considered appropriate that any regulations made using this power be subject to the draft affirmative procedure in both Houses of Parliament, especially given that the power envisages changes to primary legislation and the decision may involve policy considerations, albeit in a narrow area. As a result, it is appropriate that Parliament should scrutinise the detail of any changes made to the legislation and to seek assurances from Treasury Ministers during the debates regarding the effect of the amendments to legislation.

Clause 51 and Schedule 13: Insurers in financial difficulties and enforcement of contracts

- paragraph 12 of new Schedule 19C to FSMA 2000:

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

657. The new Schedule 19C to FSMA 2000 introduces restrictions on certain contractual rights of certain counterparties when an insurer is in financial difficulties, as defined by paragraph 2(1) of that Schedule. Broadly put:
   a. Part 2 of the Schedule prevents a policyholder surrendering more than a certain value of their insurance contract in a 12-month period. Paragraph 3(2) specifies the value.
   b. Part 3 of the Schedule prevents an insurer's contractual counterparty terminating a financial, goods and services or reinsurance contract (each a "relevant contract") because the insurer is in financial difficulties. Paragraph 6 of the Schedule defines "relevant contract".

658. Paragraph 9 prevents the restrictions in the Schedule affecting the operation of certain existing finance-related legislative provisions.

659. The restrictions are intended to help provide stability for an insurer in financial difficulties. For example, the restrictions created by Part 3 of the Schedule are intended to prevent the disruption to an insurer's business that could be caused by the termination of a business-critical services contract.

660. Paragraph 12 of Schedule 19C confers a power on HM Treasury to:

   a. vary or omit the subparagraphs in subparagraph 2(1), which define the meaning of "financial difficulties" (paragraph 12(a));
   b. change the maximum value of a policy that a policyholder can surrender during a 12-month period (paragraph 12(b));
   c. amend paragraph 6 with the effect of changing the meaning of "relevant contract" (paragraph 12(c)); and
   d. amend paragraph 9 to change the exclusions in the Schedule (paragraph 12(d)).

Justification for taking the power

661. A key overall justification for this power is that it will enable HM Treasury to alter aspects of the restrictions in Schedule 19C to account for any practice and precedent that develops around the operation of the restrictions (noting that the restrictions are largely without precedent in the context of insurers). For example, paragraph 10 allows the court to disapply the contractual restrictions created by the Schedule. In this context, a precedent could be established that the court always disapplies the restrictions where a petition for the winding up of an insurer is put to the court. In this scenario, limb 12(a) of the power would enable HM Treasury to omit subparagraph 2(1)(c) of the Schedule, which would reduce the administrative burden on the court in future.

662. In relation to paragraph 12(b) of the power, HM Treasury will be able to adjust the value of a policy that a policyholder can surrender in a 12-month period (the 'surrender limit'). This will allow HM Treasury to continue to provide certainty and stability with respect to an insurer's liabilities, including for example addressing potential changes in legislation, or the court's interpretation of legislation where relevant. In relation to paragraph 12(c) and paragraph 12(d) of the power, HM Treasury will be able to address future changes in the contracts or financial arrangements that insurers enter into which may need to be brought within scope of the restrictions in the Schedule or may give rise to the need to add, vary or remove exclusions from para. 9.

663. As regards the scope of the power, we note, in particular that paragraph 12(a) of the power does not permit HM Treasury to add further cases where an insurer would be considered to be in financial difficulties, which narrows the power's scope.

664. The existing section 233C of the Insolvency Act 1986[32] (inserted by section 14 of the Corporate Insolvency and Governance Act 2020[33]) is an example of an existing power providing for amendments to be made to the circumstances in which restrictions on the termination of contracts apply, including to the types of contracts caught by the restrictions.

Justification for the procedure

665. It is considered appropriate that any regulations made using this power be subject to the draft affirmative procedure in both Houses of Parliament, especially given that the power envisages changes to primary legislation and the amendments may involve policy considerations. As a result, it is appropriate that Parliament should scrutinise the detail of the changes made to the legislation and to seek assurances from Treasury Ministers during the debates regarding the effects of the amendments to legislation.

[32] Insolvency Act 1986 c.60.
[33] Corporate Insolvency and Governance Act 2020 c.12.

PART 6 – MISCELLANEOUS

Amendments to FSMA 2000

Clause 60: Unauthorised Co-ownership AIFs

666. Clause 57 confers a power to HM Treasury to make provision that corresponds or is similar to, or applies with modifications, sections 261MO and section 261P(1) and (2) of FSMA 2000 to a contractual scheme that is a co-ownership scheme, which is not authorised and is an alternative investment fund ("AIF") ("unauthorised co-ownership AIF"). Such a power can be exercised generally with regards to unauthorised co-ownership AIFs, or in relation to such AIFs of a description specified in regulations.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary procedure: negative procedure

Context and Purpose

667. A contractual scheme is a formation of undertakings for collective investment constituted in accordance with contract law, as defined under section 235A FSMA 2000. Per section 235A FSMA 2000, a contractual scheme may be either a co-ownership scheme, which has no legal personality distinct from the persons who take part as investors, or a partnership scheme, which is a limited partnership under the Limited Partnerships Act 1907[34].

668. An authorised contractual scheme ("ACS") is a contractual scheme that benefits from an authorisation order under section 261D(1) of FSMA 2000. Sections 261M-P of FSMA 2000 apply to a co-ownership ACS ("CoACS"). In brief, these provisions afford CoACS with the following:

a. section 261M: makes provision about the contracts in the scheme;

b. section 261N: limits an investor's rights and liabilities - to which they are entitled or subject under, or in connection with, contracts in the scheme - to the period that they are a participant;

c. section 261O: limits an investor's liability for debts incurred under, or in connection with, contracts which the operator is authorised to enter on their behalf; and

d. section 261P: provides for the segregation of liabilities of participants in sub-funds, where a co-ownership scheme is constituted as an umbrella fund.

669. The purpose of this power is therefore to allow HM Treasury to broadly apply sections 261M-O and section 261P(1) and (2) of FSMA 2000 to a contractual scheme, that is a co-ownership scheme, but which does not benefit from an authorisation order. The power is scoped to only apply to AIFs, as defined under section 417(1) of FSMA 2000, to ensure that it is not unnecessarily wide.

[34] Limited Partnerships Act 1907 c.24.

Justification for taking the power

670. Without this measure, an investment vehicle that is structured as an unauthorised co-ownership AIF would be commercially unviable and present inappropriate risk to participants. This is because it would not benefit from the same provisions in relation to the contracts in the scheme, statutory rights and limitation and segregation of liability, as CoACS does. However, such a vehicle would only be commercially viable if, in addition, a future Finance Bill were to provide that such vehicle are treated in the same way as a CoACS for tax purposes.

671. The likely exercise of this power will therefore be to make provision that corresponds or is similar to, sections 261M-O and section 261P(1) and (2) of FSMA 2000, for a new investment vehicle that is structured as an unauthorised co-ownership AIF with a corresponding tax treatment, if such a vehicle was to be introduced in a Finance Bill (noting that of section 261P FSMA of 2000, only sections 261P(1) and (2) of FSMA 2000 would be relevant for an unauthorised co-ownership AIF, in any event).

Justification for the procedure

672. This power is constrained to only be exercisable in relation to a specific form of investment scheme, the unauthorised co-ownership AIF. Such a scheme will need to: be a contractual scheme, that is also a co-ownership scheme (section 235A of FSMA 2000); be without an authorisation order (section 261D(1) of FSMA 2000); and meet the definition of an AIF (section 417(1) of FSMA 2000).

673. In the event that a new investment vehicle, that is structured as an unauthorised co-ownership AIF with a corresponding tax treatment, was to be introduced in a Finance Bill, then this power will merely permit HM Treasury to broadly apply the relevant effects of sections 261M-O and section 261P(1) and (2) of FSMA 2000 to such a scheme – mirroring the same as applied to a CoACS, in this respect. This power will not permit HM Treasury to make textual amendments to primary legislation.

Clause 61: Power to amend enactments in consequence of rules

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

674. Clause 61 inserts new section 141B into FSMA 2000. Within this, subsection (1) of new section 141B enables HM Treasury to amend legislation as a consequence of rules made by a regulator. The types of legislation within scope of the term ‘enactment’ are defined in subsection (2).

675. Subsection (3) omits section 144F of FSMA 2000 which enables HM Treasury to amend an enactment as a consequence of CRR rules made by the PRA. New section 141B

will enable HM Treasury to amend enactments as a consequence of Capital Requirement Regulation rules so section 144F is no longer required.

676. Subsection (4)(b) provides for the deletion of section 144F from section 429(2) of FSMA 2000 because of the omission of section 144F provided for in subsection (3) of this clause.

Justification for the power

677. The power in clause 61 is required to ensure that domestic legislation remains operative and effective as a consequence of the regulators making rules.

Justification for the procedure

678. Subsection (4)(a) inserts new section 141B into section 429(2) of FSMA 2000 which provides that regulations made under this power are subject to the affirmative procedure to reflect the strength and permanence of the power.

Clause 63: Power to amend or repeal certain provisions of FSMA 2000

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

679. Clause 63(1) confers a power on HM Treasury to amend or repeal Parts of Part 9C of FSMA 2000. Part 9C of FSMA 2000 was introduced in order to facilitate the creation of the Investment Firm Prudential Regime ("IFPR") and to make the necessary changes (for the purposes of IFPR) to the Capital Requirements Regulation. As part of this process, Part 9C of FSMA 2000 imposed certain duties on the regulators.

680. It is HM Treasury's opinion that as we come to replace retained EU law in certain areas HM Treasury might need to amend or remove provisions in Part 9C of FSMA 2000, not least because there are overlapping provisions in clauses 28 (Treasury powers in relation to rules) and 29 (matters to consider when making rules) of the Bill. Subsection (1) confers on HM Treasury the power to make the necessary changes to ensure that the regimes continue to operate effective when relevant areas of retained EU law are revoked. Subsection (2) also confers a power on HM Treasury to make consequential amendments to the rest of these Parts of FSMA 2000 as a consequence of exercising the power in subsection (1).

Justification for the power

681. The powers in clause 63 are required to ensure that Part 9C of FSMA 2000 remain operative and effective in the event that HM Treasury exercises the powers in clauses 28 (requirement to make rules) and 29 (matters to consider when making rules) and that there

are no overlapping obligations on regulators in the event of the exercise of powers in clauses 28 and 29.

Justification for the procedure

682. The powers in clause 28 and clause 29 are both subject to the affirmative procedure. HM Treasury considers this to be the appropriate procedure because even though the powers are tightly constrained to certain provisions, they are still available to amend primary legislation (FSMA 2000) and should, therefore, be subject to the affirmative procedure. It is appropriate that any repeals or amendments made to Parts 9C of FSMA 2000 under the powers in subsections (1) and (2) of clause 61 are also subject to the affirmative procedure.

Clause 64: Power under FSMA 2000 to make transitional provisions

- amendment to section 427 of and Schedule 17A to FSMA 2000

Powers conferred on: a Minister of the Crown
Powers exercised by: order
Parliamentary Procedure: negative procedure

Context and purpose

683. Section 426 of FSMA 2000 gives power to a Minister of the Crown to make such incidental, consequential, transitional or supplemental provision as he considers necessary or expedient for the general purposes, or any particular purpose, of FSMA 2000 or in consequence or in order to give full effect to FSMA 2000. Section 427 of FSMA 2000 makes provision about the kind of transitional or savings provision that may be made under section 426. Section 427 makes reference in places to "the Authority", a reference to the Financial Services Authority, whose functions are now performed by the FCA and the PRA.

684. The purpose of the amendments to section 427 in this clause are to ensure that the transitional provision provided for can be made in relation to the FCA and the PRA. This clause also amends Schedule 17A to ensure that where an order is made in relation to provisions in Part 18 of FSMA 2000, they can make provision in relation to the Bank as regulator of central counterparties and central securities depositories.

Justification for the delegated power

685. This clause simply updates an existing delegated power in FSMA 2000, to ensure that it can be used in relation to the current regulators for new provisions that are being inserted into FSMA 2000 by this Bill.

Justification for the procedure

686. Section 429 of FSMA 2000 provides that orders made under section 426 are subject to the negative procedure, and this procedure is considered appropriate for orders which include provision of the kind described in section 427, once amended. The amendments to section 427 do not change the nature of the amendments that can be made, they simply reflect changes to the bodies that regulate the financial services sector.

Clause 65: Cryptoassets

- New section 417(5) of FSMA 2000 as inserted by clause 65(4)(b), enables HM Treasury to amend the definition of "cryptoasset" to be inserted into section 417 of FSMA 2000.

  Power conferred on: HM Treasury
  Power exercised by: Regulations made by statutory instrument
  Parliamentary procedure: affirmative procedure

Context and Purpose

687. Clause 65(2) and (3) amends FSMA 2000 to ensure that HM Treasury can use its existing powers in sections 21 (which allows HM Treasury to prohibit unauthorised persons from issuing financial promotions) and 22 (which allows HM Treasury to make provision as to the classes of regulated activity and types of investment that are regulated under FSMA 2000) of FSMA 2000 to regulate cryptoassets. It does so by amending the definitions of "investment" for the purposes of sections 21 and 22 of FSMA 2000 to make clear that both definitions include assets, rights or interests that are, or comprise or represent, a cryptoasset. These amendments clarify rather than extend the scope of HM Treasury's powers under sections 21 and 22, and therefore no entry is required in this delegated powers memorandum in respect of them.

688. Clause 65(4)(a) inserts a definition of "cryptoasset" into section 417 of FSMA 2000, which applies to the term as used in the amendments described above and across FSMA 2000. Clause 65(4)(b) and (5) give HM Treasury the ability to amend this definition by regulation subject to the affirmative parliamentary procedure. The justification for this amendment power and procedure is set out below.

Justification for taking the power

689. The power to amend the definition of "cryptoasset" is necessary to ensure that HM Treasury has the ability to update it should the cryptoasset market change in the future. The definition of cryptoasset relies on a description of the essential characteristics of cryptoassets and the technology that underpins them. Cryptoassets develop rapidly, such that these essential characteristics and technology may change, with the result that certain cryptoassets unintentionally fall outside of the scope of the powers. This amendment power allows HM Treasury to respond quickly to such developments.

Justification for the procedure

690. HM Treasury considers that the affirmative procedure is appropriate for amendments to primary legislation.

Bank of England Levy

Clause 66: Bank of England levy

New paragraph 2(4) of new schedule 2ZA to the Bank of England Act 1998[35]: Eligible institutions

Power conferred on: HM Treasury
Power exercisable by: regulations made by statutory instrument
Parliamentary procedure: affirmative

Context and purpose

691. Clause 64 repeals section 6 of, and schedule 2 to, the Bank of England Act 1998 ("the 1998 Act") and inserts a new section 6A and schedule 2ZA into the 1998 Act. Paragraph 1 of the new schedule 2ZA will provide that the Bank of England may impose a charge, to be known as the Bank of England levy, on eligible institutions in accordance with the schedule.

692. Paragraph 2(1) will define eligible institutions as authorised deposit-takers. Paragraph 2(2) will define authorised deposit-takers as anyone authorised under Part 4A of FSMA 2000 to accept deposits, with the exception of credit unions, friendly societies and insurers. Paragraph 2(4) will give HM Treasury the power to amend paragraph 2 and amend other paragraphs of schedule 2ZA as a consequence of such an amendment, by regulations.

Justification for the delegated power

693. Institutions eligible to pay the levy are broadly deposit-takers authorised under FSMA 2000. The cohort of payers for the levy may need to change over time, for example in response to a change in the structure of the financial market, such as new entities whose activities pose a financial stability risk. For this reason, the power to amend the definition is considered an appropriate matter for secondary legislation.

694. It is also noted that the levy scheme being introduced by these provisions replaces the 'cash ratio deposit' scheme in section 6 of, and schedule 2 to, the 1998 Act. The definition of eligible institutions in the current paragraph 1 of schedule 2 to the 1998 Act similarly includes a power for it to be amended by regulations. It is considered that similar considerations apply to the definition in the levy scheme and the approach is consistent with this.

695. There are also a number of procedural safeguards. Paragraph 10(1) of new schedule 2ZA will provide that, in exercising the power, HM Treasury must consult the Bank of England and such other persons who are likely to be affected. Paragraph 10(2) will provide that, in making the regulations, HM Treasury must have regard to the financial needs of the Bank of England. The exercise of the power would be subject to general constraints under public law.

[35] Bank of England Act 1998 c.11.

Justification for the procedure

696. It is considered appropriate that any regulations made under this power are subject to the draft affirmative procedure, as it is an amendment of primary legislation. Accordingly, Parliament should have the opportunity to debate and approve any such amendments before they take effect.

New paragraph 5(1) of new schedule 2ZA to the Bank of England Act 1998: Liability to pay the levy

Power conferred on: HM Treasury
Power exercisable by: regulations made by statutory instrument
Parliamentary procedure: affirmative

Context and purpose

697. Paragraph 5 of the new schedule 2ZA concerns an eligible institution's liability to pay the levy. Sub-paragraph 1 provides that the amount of the levy that an eligible institution is liable to pay is to be determined by the Bank of England in accordance with regulations made under this provision.

698. In addition, paragraph 5(4) provides that regulations made under sub-paragraph (1) may include provision conferring a discretion on the Bank of England to determine specified matters.

Justification for the delegated power

699. Regulations made under this provision will set down how the Bank of England must calculate the amount of the levy that an eligible institution is liable to pay. The calculation of the levy is likely to need to be changed over time to adapt to the development and operation of the scheme. In addition, it is considered appropriate for secondary legislation to be used to give sufficient detail of the calculation that will be applied so that eligible institutions have clarity and certainty of these matters, whilst being amendable through a parliamentary process.

700. The power to confer a discretion on the Bank of England to determine specified matters in paragraph 5(4) is needed to operate the scheme. It is anticipated that discretion may need to be conferred to enable the Bank of England to determine an eligible institution's eligible liabilities. For example, the Bank of England may need to use discretion to adapt its methodologies to reflect differences in the ways that individual eligible institutions are structured or difference in how available data is captured by the financial institution.

701. There are also a number of procedural safeguards. Paragraph 10(1) of new schedule 2ZA will provide that, in exercising the power, HM Treasury must consult the Bank of England and such other persons who are likely to be affected. Paragraph 10(2) will provide

that, in making the regulations, HM Treasury must have regard to the financial needs of the Bank of England. The exercise of the power will also be subject to general constraints under public law. In addition, in HM Treasury's Policy Statement titled "Review of the cash ratio deposit scheme" the government committed to undertake a formal review of the Bank's funding model within at least 5 years of this legislation being introduced.

702. For these reasons, this is considered an appropriate matter for secondary legislation.

Justification for the procedure

703. HM Treasury is of the view that regulations providing for how the Bank of England must determine the amount of levy an eligible institution must pay would be of particular interest to Parliament and considers it appropriate that these regulations be subject to the affirmative procedure so that Parliament has the opportunity to debate and approve any such new arrangements before they take effect.

New paragraph 8(5) of new schedule 2ZA to the Bank of England Act 1998: Interest

Power conferred on: HM Treasury
Power exercisable by: regulations made by statutory instrument
Parliamentary procedure: negative

Context and purpose

704. Paragraph 8 of the new schedule 2ZA to the 1998 Act concerns interest payments on unpaid amounts of the levy. Paragraph 8(2) provides that, where an eligible institution has been notified of the levy amount payable and the time by which it must be paid, interest is payable on any amount unpaid. Paragraph 8(3) provides that the interest rate is 4% above the benchmark rate (benchmark rate is defined by sub-paragraph (4)). Paragraph 8(5) provides that HM Treasury may, by regulations, amend paragraph (8) so as to amend the rate of interest payable on an unpaid amount of the levy.

Justification for the delegated power

705. The percentage and the benchmark may in the future need changing, for example in response to a change in market conditions. For this reason, the power to amend the interest rate is considered an appropriate matter for secondary legislation.

Justification for the procedure

706. HM Treasury is of the view that, although the regulations would be amending primary legislation, the purpose of the amendment would be technical in nature with limited scope for policy discretion and therefore the negative procedure affords the appropriate level of scrutiny. In addition, paragraph 10(1) of new schedule 2ZA will provide that, in exercising the power, HM Treasury must consult the Bank of England and such other persons who are likely to be affected.

Other miscellaneous provisions

Clause 68: Liability of payment service providers for fraudulent transactions

- amends the PSRs 2017 to add paragraph (6) and (7) and imposes a duty on the PSR.

> *Power conferred on: the PSR*
> *Power exercised by: regulatory requirements made in accordance with Part 5 of FSBRA, as specified in clause and directions made in accordance with PSRs 2017.*
> *Parliamentary Procedure: none*

Context and Purpose

707. The government and the PSR are committed to tackling fraud within payment systems. While there is no statutory definition of Authorised Push Payment ("APP") fraud or APP scam, it is generally understood to have occurred when a person is tricked into sending money from their bank account to an account controlled by another person that they would not have paid absent the fraud e.g. the payer authorises the payment from their account to a fraudulent payee. With APP fraud, which differs from unauthorised fraud, the payer explicitly authorises the transfer of funds out of their account, quite often because they believe they are paying someone for a legitimate purpose.

708. Over the last few years, the PSR and the payments industry have worked together to prevent payments fraud and develop better mechanisms for reimbursing victims of APP fraud. There is a voluntary Contingent Reimbursement Model ("CRM") Code that covers 90% of relevant transactions and payments service providers have also made independent voluntary commitments to victim reimbursement.

709. However, reimbursement to victims of APP scams remains inconsistent, with many victims continuing to suffer losses without reimbursement. Partly because some firms have not made voluntary commitments to reimburse victims of APP scams, but also because even amongst firms who have made voluntary reimbursement commitments, reimbursement remains inconsistent, with disparities in how firms interpret their obligations.

710. Currently, regulation 90(1) of the PSRs 2017 states that where a payment services provider (for example, a bank) has executed a payment in accordance with the unique identifier (for example, the sort code and account number) provider by the payment system user (for example, the payer), then the payment is deemed to have been correctly executed. There is nothing expressly set out in regulation 90(1) in relation to reimbursement for fraud, however.

711. Regulation 90(2) further sets out that where the unique identifiers provided is incorrect, then the payment services provider is not liable for defective execution or non-execution under regulation 91 – 92 but that they do have to make reasonable efforts to recover the funds, and that they can charge for such recovery. Regulation 90(3) and (4) deals with cooperation between providers and information sharing, while regulation 90(5) states that where a payment service user has provided more information than necessary under the

regulations, the payment services provider is only required to execute the payment in accordance with the unique identifier.

712. The purpose of the amendment to the PSRs 2017 is to clarify that nothing in Regulation 90 prevents the PSR from using its existing regulatory powers, in FSBRA or the PSRs 2017, to require mandatory reimbursement in cases of APP scams in designated payment systems.

713. The relevant powers that the PSR can exercise are:

a. A direction given under regulation 125,
b. A direction given under section 54 of FSBRA,
c. A rule made under section 55 of that Act,
d. An order made under section 56(3) of that Act, or
e. A variation of an agreement under section 57(2) of that Act.

714. It is expected that the PSR will utilise its powers by imposing a requirement either directly on participants of the payment system, or by requiring the operator of the payment system to amend its rules.

715. The clause further places a consultation duty on the PSR to consult with a draft direction or requirement under either section 54 or 55 of FSBRA on reimbursement for payments executed over Faster Payment System ("FPS") subsequent to fraud or dishonesty. The rationale for mentioning FPS in this context is because this is the payment system where the volume and value of APP scams is the highest and is increasing every year.

716. The duty requires the PSR to consult with a draft direction or requirement under section 54 or 55 of FSBRA within two months of provisions coming into force, and to implement the draft direction or requirement on reimbursement within six months of provisions coming into force.

717. It is not HM Treasury's intention that every case of APP fraud conducted over FPS has to be reimbursed. The PSR, as the independent regulator, will exercise its discretion and comply with public law duties when imposing requirements. It is expected that when the requirement is imposed, there will be criteria which sets out the circumstances for when reimbursement is triggered, including criteria on where the customer may have been grossly negligent or reckless.

<u>Justification for taking the power</u>

718. This section does not create or delegate any new powers to the PSR or HM Treasury or amend the existing powers framework (FSBRA). It clarifies that the PSR may use certain FSBRA powers, as set out in the section, as may be relevant in relation to reimbursement of APP scams.

719. This is appropriate as the PSR has the relevant objectives, powers and expertise to provide detailed requirements regarding APP scam reimbursement in designated payment systems.

Justification for the procedure

720. There is no parliamentary procedure, as the PSR is not being given any additional powers. As noted above, the purpose of the measure is to clarify that the PSR's existing powers over designated payment systems can be used in the context of APP scams.

Clause 69 and Schedule 14: Credit Unions

- New section 1ZA (Specified financial activities) and 1ZB (Power to add further permitted activities) to the Credit Unions Act 1979.

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative

Context and Purpose

721. Credit unions have a prescriptive legislative framework, which means that credit unions must have express legislative permission to offer specific products and services and are unable to innovate outside of the services listed in their objects in the Act. This legislation would allow credit unions to choose to offer these new products and services for the first time.

722. Whilst the new optional financial activities appear on the face of the Bill, a power is taken in subsection (2) of section 1ZA of the Credit Unions Act 1979, by HM Treasury to specify requirements or add restrictions in relation to these optional financial activities by regulations.

723. New section 1ZB, further provides HM Treasury with the power, exercised by regulations made under the affirmative procedure, to add additional new financial activities for credit unions and to make consequential amendments to the Act or other enactments.

724. Additionally, the power allows HM Treasury to make provision for fees or charges payable to the credit union for the new financial activity or for activities that are ancillary to the activity.

725. Section 11(7) of the Credit Unions Act 1979 has been amended to specify that orders made by HM Treasury in respect of the interest rate cap on loans, may be specified in relation to loans made to members and loans made to a credit union without a membership link.

726. New section 11E of the Credit Unions Act 1979, sets out the remit of the new elective object of entering into a hire purchase agreement or a conditional sale agreement. It

includes a 10% cap on the amount of hire purchase agreements or conditional sale agreements that a credit union may offer to its corporate members, which HM Treasury may amend later by statutory instrument. It also sets out a 3% cap on interest charged for hire purchase agreements or conditional sale agreements, which HM Treasury may amend later by statutory instrument.

Justification for taking the power

727. The powers to specify more optional financial activities and the power to specify requirements or restrictions in respect of the financial activities will allow the credit union model to adapt to changing demands in product offerings in a prompt fashion. This will support the sector's wider competitiveness with other financial institutions, while still supporting the lighter touch regulatory benefits of the prescriptive legislative regime of credit unions by ensuring there is still scrutiny over which services credit unions may offer.

728. The power to amend the 10% limit on total outstanding balances that credit unions can provide to corporate members for hire purchase agreements or conditional sale agreements must ensure that credit unions are able to adapt their product offering to their membership base promptly, should the need arise. Given HM Treasury sets these rates for the sector in legislation, flexibility is required to allow HM Treasury to change them in a timely fashion to allow credit unions to respond to market and industry needs as they arise, to remain competitive.

729. The power to amend the 3% interest rate cap on hire purchase agreements or conditional sale agreements is necessary to ensure that credit unions have flexibility to amend their product offering in line with market changes in a prompt fashion to remain competitive. The Act has an equivalent interest rate cap and power to amend for loans, which had been raised from 2% to 3% in 2014 in line with market changes.

Justification for the procedure

730. Regulations made by HM Treasury to expand the scope of the optional object will be subject to the affirmative procedure. Prior to exercising the power, to make Regulations, there is a duty on HM Treasury to consult with relevant stakeholders.

731. In respect of the power to increase the interest cap, a 3% per month interest rate cap applies for loans and there is a power to raise this subject to the negative procedure. This cap for loans ensures that credit unions are affordable credit providers. Having a power to raise this cap allows the government to do so if market conditions dictate it necessary or for credit unions to remain competitive. This has been the case previously, with the government raising the cap from 2% to 3% in 2014.

732. An equivalent 10% threshold exists on loans for corporate members and there is an equivalent power to lift the 10% threshold, subject to the negative procedure. This threshold exists to ensure that credit unions primarily serve individual members, not small and medium sized enterprises ("SMEs"), but allows them to diversify their income streams. A

power to raise this threshold for hire purchase agreements or conditional sale agreements therefore mirrors the current provision for loans and will allow credit unions to further diversify their income streams if exercised.

Clause 70: Reinsurance for acts of terrorism

- New section 2A (Directions) of the Reinsurance (Acts of Terrorism) Act 1993[36].

Power conferred on: HM Treasury
Power exercised by: direction
Parliamentary Procedure: none

Context and Purpose

733. The Reinsurance (Acts of Terrorism) Act 1993 (the "1993 Act") provides Parliamentary approval for HM Treasury to act as the insurer of last resort to the British insurance market in relation to terrorism. In accordance with its current practice, the Office for National Statistics (the "ONS") is likely to classify a company that enjoys the benefit of a guarantee under the 1993 Act as a public sector body. Such classifications are likely to be retrospective to the date that the company started to enjoy the benefit of a guarantee under the 1993 Act. The consequences of a company being classified as a public sector body include a requirement that its accounts are consolidated into its sponsor department's departmental accounts (as required by the government Resources and Accounts Act 2000[37]), and it becomes subject to the controls, standards and processes expected of a public sector (which may include central government) body, in line with government policy and the expectations of Parliament on the use of funds on the public account. This could include, for example, Managing Public Money guidance.

734. This clause amends the 1993 Act to provide that a "relevant person" must comply with a direction given to it by HM Treasury.

735. "Relevant person" is defined to mean either:
   a. a person that has entered an arrangement with HM Treasury under the 1993 Act, and has been classified to the public sector by the ONS; or
   b. a group undertaking of such a person.

736. HM Treasury may give a direction if it considers it necessary for the purpose of ensuring compliance with any requirements associated with the classification of a person falling under paragraph 734(a) above.

737. Directions may include provision about compliance with relevant requirements relating to auditing, accounting, budgeting, arm's length bodies or public sector bodies. HM Treasury may also exercise a specific power to direct a "relevant person" to appoint an accounting officer.

[36] Reinsurance (Acts of Terrorism) Act 1993 c.18.
[37] Resources and Accounts Act 2000 c.20.

738. The policy objective is to ensure that any entity classified as a public body that benefits from an arrangement under the 1993 Act, will comply with the necessary controls so that funds on the public accounts are managed appropriately. Ensuring these requirements are met will in turn provide value for money, probity, regularity and propriety in the public sector bodies within scope of this provision.

Justification for taking the power

739. It is HM Treasury's opinion that this measure is not legislative in character. The measure does not give HM Treasury the power to make any legislation, or to confer on any other body the ability to make rules. Without direction-making powers, there is a gap in HM Treasury's ability to ensure that its arms' length bodies ("ALBs") comply with central government governance requirements. To secure compliance with the requirements associated with classification as a public sector body, sponsor government departments generally put in place Framework Documents with entities subject to this classification. However, Framework Documents are not legally enforceable. Commonly, ALBs are wholly owned by the government, therefore giving the responsible department a degree of control over its compliance with their Framework Document.

740. This is not always the case, and clause 70 addresses how to ensure compliance with important controls over public funds in the absence of other legal levers. This measure provides a necessary safeguard power for the government to ensure compliance with the requirements expected of a public sector body, in line with government policy and the expectations of Parliament on the use of funds on the public account.

741. A direction can only be issued if HM Treasury considers it necessary for the purpose of ensuring compliance by a "relevant person" with any requirements associated with classification to the public sector and/or if HM Treasury wishes to direct a "relevant person" to appoint an accounting officer. The requirements associated with classification exist to ensure that public funds are managed appropriately, and so the powers will act as a backstop providing additional protection to the taxpayer from any risks.

742. The provision also provides HM Treasury with the ability to issue a direction to the group undertakings of ALBs enjoying a benefit under the 1993 Act. This is intended to ensure that a direction to an ALB cannot be circumvented by some form of corporate restructuring. The power to direct the appointment of an accounting officer will enable HM Treasury to ensure that any public sector body that benefits from a guarantee has sufficient oversight of its requirements as a public sector body.

743. There are a number of safeguards built into this provision to ensure that any exercise of the power by HM Treasury is properly justified. These include the requirement that a direction can only be issued to a narrow category of "relevant persons" (as set out above) and that HM Treasury must consult with such persons before giving them a direction. Any direction must also be accompanied by a written notice which states when the direction

takes effect and gives reasons for the direction, and the direction must also be published by HM Treasury and laid before Parliament.

Justification for the procedure

744. There is no Parliamentary procedure for a direction to be issued.

745. However, for the purposes of transparency, the clause provides that any direction must be published in a manner HM Treasury considers appropriate and laid before Parliament.

PART 7 – GENERAL

Clause 75: Power to make consequential provision

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative if exercised so as to amend, repeal or revoke primary legislation, otherwise negative.

Context and Purpose

746. The power in subsection (1) of this clause enables provision to be made which is consequential upon other provisions of the Bill.

747. Subsection (2) provides that such regulations may amend, repeal, revoke or modify any provision of primary legislation (including this Bill), retained EU legislation or subordinate legislation.

Justification for taking the power

748. Due to the nature of certain provisions under the Bill, it is anticipated that these would, if enacted, require consequential amendment of other enactments, including primary legislation and retained EU legislation. In respect of other secondary legislation, although not necessary to take a power because the powers under which that legislation is made would still be available, it is considered a better approach and more convenient to make all the consequential provision in one instrument, or series, under one power.

749. Consequential amendment is most likely the case in respect of the operation of powers proposed under the Bill, where the manner of their exercise and therefore the consequential effect on existing legislation is yet to be determined.

Justification for the procedure

750. In respect of primary legislation or retained direct principal EU legislation, it is proposed that the regulations are subject to the draft affirmative procedure, as is usual with amendments to primary effected by secondary. The same principle applies to retained direct principal EU legislation.

751. Although secondary legislation which may be amended by exercise of the power under which it is made might be subject to an affirmative resolution procedure, it is considered that a negative procedure is appropriate given that the nature of any amendments will be consequential upon, and therefore only those which arise naturally from, provisions in the Bill.

Clause 76: Regulations

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: affirmative if exercised so as to amend, repeal or revoke primary legislation, otherwise negative

Context and Purpose

752. Clause 76(1) provides that any power to make regulations under the Bill also includes a power to make provision by reference to rules or other instruments as they have effect from time to time. This allows references to rules to reflect any changes made by regulators so that the references are kept up to date.

753. It also enables HM Treasury to make for different provisions for different purposes in addition to supplementary, incidental, consequential, transitional, transitory or saving provision.

Justification for taking the power

754. Due to the nature of certain provisions under the Bill, it is anticipated that these would, if enacted, require consequential amendment of other enactments, including regulator rules. Furthermore, the precise timing for commencement of some provisions is delegated to a Minister in order to deal with the vicissitudes of implementation.

755. In order to give effect to a smooth adoption of the new legislation, the power to make transitional, transitory or saving provision in connection with the coming into force of a provision of the Bill has been included.

Justification for procedure

756. Regulations made under this power will be subject to the same procedure as set out in the power being exercised under the relevant clause.

Clause 78: Commencement

Power conferred on: HM Treasury
Power exercised by: regulations made by statutory instrument
Parliamentary Procedure: none

Context and Purpose

757. This clause provides a power for provision which is not brought into force on the face of the Bill to be brought into force by regulations made by HM Treasury.

758. Subsection (6) provides that such regulations may make different provision for different purposes.

Justification for taking the power

759. The precise timing for commencement of provisions is delegated to a Minister in order to deal with the vicissitudes of implementation.

760. In order to give effect to a smooth adoption of the new legislation, the power to make transitional or saving provision in connection with the coming into force of a provision of the Bill has been included.

Justification for the procedure

761. As is common with commencement regulations bringing into force an enactment and making no substantive provision, it is considered that in respect of these regulations no Parliamentary procedure is indicated.