

FINANCIAL SERVICES (IMPLEMENTATION OF LEGISLATION) BILL

Memorandum from HM Treasury to the Delegated Powers and Regulatory Reform Committee

A. INTRODUCTION

1. This memorandum has been prepared for the Delegated Powers and Regulatory Reform Committee following changes made to the Financial Services (Implementation of Legislation) Bill (“the Bill”). The Bill was introduced in the House of Lords on 22 November 2018. The Committee reported on the Bill in its 42nd Report, published on 18th December 2018 and the Government responded on 5 February 2019.

2. This memorandum identifies the provisions of the Bill that confer powers to make delegated legislation, as they have been amended following agreement by the House of Lords to Government amendments tabled at Report, which took place on 29 January 2019.

3. It explains in each case why the power has been taken and explains the nature of, and the reason for, the procedure selected.

B. PURPOSE AND EFFECT OF THE BILL

4. As a member of the European Union, the UK has primarily derived its financial services legislation from the EU. Following withdrawal from the EU in a ‘no deal’ scenario, a legislative framework is needed in order to be able to domesticate certain specified pieces of ongoing EU financial services legislation in the immediate period post-exit. This will ensure the UK can continue meeting core international obligations and remains a competitive and attractive place to do business.

5. The Bill allows for the UK Government to bring into domestic law, via statutory instruments, specified EU financial services legislation that has either been agreed or is in negotiation at the point at which the UK withdraws from the European Union on 29 March 2019, but that are not yet operative.

6. In many cases, the UK has played a leading role in shaping these files since they were proposed, and firms have begun preparing for their implementation. However, the UK would not be able to implement them post-Exit in a ‘no deal’ scenario without primary legislation as they will not be operative before 29 March

2019. This means that the power to domesticate these files will lie outside the scope of the European Union (Withdrawal) Act 2018.

7. The Bill would enable the Treasury, by secondary legislation, to implement Regulations and Directives which are specifically listed in clause 1 and the schedule to the Bill. This power would only be used to implement those key pieces of legislation, without which there would be a risk to the reputation, global competitiveness and efficiency of the UK’s financial markets.

8. For example, if the UK did not domesticate the Prospectus Regulation in a timely way, UK businesses would face higher costs for producing a prospectus in the UK, and EU businesses may also be deterred by the higher costs of accessing UK capital markets. This would concede a competitive advantage to businesses operating in EU-based markets, result in operational and financial disruption to companies currently based in the UK, and impact the UK’s reputation as an attractive destination for capital.

9. Additionally, implementing the Capital Requirements Regulation (CRR) II and Directive (CRD) V will allow the UK to remain compliant with the Basel rules and meet our long-standing G20 commitment to international standards. If we do not implement these in a timely way, it will cause significant disruption to firms who make financial decisions years in advance, and it could call into question the UK’s status as a global leader in financial services.

C. TABLE OF “IN-FLIGHT” FILES

10. The table below sets out all files which are listed on the face of the Bill, with a short summary of their aims.

Markets in Financial Instruments Regulation	This file facilitates the sharing of information on benchmarks, enabling pricing and clearing by Central Counterparties and Trading Venues. It will provide market participants with greater transparency of information.
Bank Recovery and Resolution Directive II	This proposal updates the existing approach to bank resolution. It will provide regulators with an updated resolution framework, and modifies several areas of the first BRRD to ensure flexibility and proportionality for resolution authorities and firms. It is primarily concerned with updating rules on available financial resources in resolution, which are derived from international Financial Stability Board standards.
CCP Recovery and Resolution	The CCP R&R Regulation aims to ensure that both Central Counterparties (CCPs) and national authorities have the means to act decisively in a crisis scenario to maintain financial stability and

	ensure that CCPs can continue to function. It helps ensure that the costs associated with the resolution of failing CCPs do not fall on taxpayers.
Covered Bonds Regulation and Directive	The Covered Bonds file provides principles that ensure the quality of the product and protection for investments in covered bonds. This proposed new framework for covered bonds represents an improvement on the current regime, establishing common rules on the structure and supervision of such bonds.
Capital Requirements Regulation II (CRR II) & Capital Requirements Directive V (CRD V)	CRR II and CRD V are legislative revisions to the existing EU approach to bank capital and bank supervision. They are primarily concerned with updating rules on minimum capital requirements derived from international Basel standards. The files provide regulators with the regulatory framework they must apply, as well as updating their powers where necessary. They are crucial to maintaining a high standard of international financial services regulation.
Cross Border Distribution of Funds Regulation & Directive	This proposal aims to make it easier to market investment funds between EU member states. They will create greater transparency in the fees charged by regulators, make it easier for fund managers to test investor demand for different types of fund products and harmonise rules across the EU for firms that wish to withdraw marketing funds in a particular country. The file creates more transparency of regulatory fees, and makes it easier for fund managers to test investor appetite.
Central Securities Depositories Regulation	This regime was introduced as a measure to improve settlement efficiency and financial stability in the European markets. The proposals set out provisions for mandatory reporting if settlement fails, the imposing of penalties on failed trades and the requirement for failing participants to be subject to compulsory enforcement.
European Market Infrastructure Regulation 2.2	The EMIR 2.2 proposal updates the supervisory framework for third country CCPs, creating a broad set of tools to manage third country CCPs, which can have a significant impact on countries outside their home jurisdiction. The proposed regulation will increase our ability to manage financial stability risks posed by systemic third country CCPs.
EMIR REFIT (Regulatory Fitness and Performance Programme)	This proposal aims to bring in technical changes to EMIR that ensure the Regulation is more proportionate with regards to clearing and reporting. It looks to align EMIR with new international standards and update existing requirements. It also includes a pension scheme clearing exemption that will assist pensions schemes in accessing derivatives markets, allowing them to continue to pay UK pensioners.
European	This proposal makes legislative changes to a number of EU files,

Supervisory Authorities Review	including amendments to the current third country equivalence regimes for benchmarks, prospectuses, and date reporting services.
Investment Firms Review	The Investment Firms Review (IFR) reviews the prudential framework for investment firms and will deliver a new and more proportionate prudential regime tailored to investment firms.
Prospectus Regulation	This file simplifies the requirements of prospectus disclosures, lowering costs for businesses raising capital whilst maintaining a high standard of investor protection. Without it, UK businesses would face higher costs for producing a prospectus and additional regulatory burdens.
Securities Financing Transactions Regulation	This file helps to assess and mitigate risks posed by Securities Financing Transactions (SFTs) by requiring firms to report transactions to trade repositories. This increases market transparency and helps to mitigate risk.
SME Growth Markets Regulation	This proposal is aimed at improving growth in SME Growth Markets, focusing on reducing the administrative burden faced by SMEs in accessing public markets, diversifying financing options for SMEs and encouraging overall growth in SMEs use of public markets.
Sustainable Finance: Low Carbon Benchmarks	This proposal aims to enhance the transparency and comparability of low carbon benchmarks to enable investors to make more informed decisions. These proposals have resulted from targets agreed by the UK at the Paris Climate agreement and through the UN's Sustainable Development Goals.
Sustainable Finance: Disclosures	The EU's Sustainable Finance Action Plan is a response to the targets agreed by the Paris Climate Agreement and the UN Sustainable Development Goals, both of which the UK also supports. This proposal introduces mandatory disclosures obligations for asset managers and institutional investors on how they incorporate Environmental, Social, and Governance (ESG) considerations into their investment decision making and risk processes. It aims to create more transparent disclosures around sustainable investing.
Sustainable Finance: Framework	The Sustainable Finance framework looks to put in place a taxonomy or 'classification system' for what can be considered an environmentally sustainable economic activity. The primary aim of the taxonomy is to reduce 'green washing' (i.e. products labelled as green or sustainable but have little such substance) and help channel investments into sustainable activities.

D. DELEGATED POWERS

Clause 1 Power in respect of EU financial services legislation with pre-exit origins

Power conferred on: the Treasury

Power exercised by: Regulations made by Statutory Instrument

Parliamentary Procedure: Affirmative

Context and Purpose

11. This clause confers a power of the Treasury to make corresponding or similar provision to the EU legislation which is listed in the clause or in the schedule with such adjustments as the Treasury considers appropriate.
12. With respect to the legislation listed in the clause, those adjustments may only be to mitigate or remedy deficiencies in the legislation arising from the withdrawal of the United Kingdom from the EU.
13. With respect to the legislation listed in the schedule, the adjustments are to make changes to reflect, or facilitate the transition to, the United Kingdom's new position outside the EU, but does not include changes that result in provision whose effect is different in a major way from that of the legislation.

Justification for delegation

14. The European Union (Withdrawal) Act 2018 will transfer the existing body of EU law onto the UK statute book on exit day, but it does not include provisions to update that law after exit. This law is complex and highly detailed, with much introduced in the period since the financial crisis. Being unable to make amendments to these provisions in a timely way represents a risk to the reputation, global competitiveness and efficiency of the UK's financial markets. Given the number of files in question, and the potential requirement to implement them to respond to market developments, maintain competitiveness and to meet international obligations, it will not be feasible to rely on primary legislation in each and every instance.
15. Since these files are, in many cases, still under negotiation, it is critical that the UK has the power to implement only those files, or parts of those files, which are necessary and beneficial for the UK. There will also clearly be uncertainty as to how the negotiations around each in-flight file listed in the Schedule will conclude once the UK has exited the EU, and it is possible that the legislation might not accommodate for the specificities or interests of the UK market. A power is therefore needed to reflect the United Kingdom's new position outside of the EU.

16. Of course, the Government recognises that this should only be the case for an interim period while the Government considers a sustainable, longer-term solution that balances the need to ensure appropriate Parliamentary oversight of financial services legislation after we have left the EU, while maintaining the flexibility and competitiveness of our regulatory regime. That is why the model within the Bill would only apply for a temporary (non-extendable) two year period post-exit, specifically in a no deal scenario, and to specified EU files only. The Government will take forward its proposals for a sustainable, long-term model in due course.

Justification for procedure

17. It will clearly be important to ensure there is appropriate parliamentary scrutiny of the files as they are implemented. It is therefore proposed that, in every instance of the power's use, it should be subject to the affirmative procedure.

Safeguards applying to the power

18. The Government acknowledges that this proposal is a broad power, and recognises that it must be temporary and limited. The proposed limitations are:

- a) The power is strictly temporary. It is subject to a sunset provision in subsection (6), and cannot be used more than two years after the UK leaves the EU. This is in line with the sunset applied to the correcting power in the EU Withdrawal Act. There is no power in the Bill to extend the period of its application.
- b) The power can only be exercised in respect of proposals adopted by the European Commission before exit day and to the specified list of files on the face of the Bill. No power to add further files is included.
- c) The power is subject to limitations as in section 8(5) and (7) of the European Union (Withdrawal) Act 2018. The power cannot be used to impose taxation; make retrospective provision; create some criminal offences; establish a public authority; implement a withdrawal agreement; or amend the Human Rights Act or the devolution settlements.
- d) Similarly, any power to introduce fees is subject to the limitations in Schedule 4 to that Act (see subsection (4)).
- e) At least one month before laying the Regulations, the Treasury must publish a document setting out what is proposed as the text of the regulations, detailing which provisions (if any) of the particular EU Directive, or EU Regulation, would not be covered by the regulations, and detailing any

adjustments that would be made by the regulations and giving the reasons for considering those adjustments appropriate.

- f) There are 6 monthly reporting periods, beginning with passing of the Act. No later than 1 month after the end of each reporting period, the Treasury must prepare and publish a report on how the powers have been used in that reporting period, and on how they are intended to be exercised in any future reporting period.

HM Treasury
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