

HOUSE OF LORDS

Secondary Legislation Scrutiny Committee  
(Sub-Committee B)

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3rd Report of Session 2017–19

**Proposed Negative Statutory  
Instruments under the European  
Union (Withdrawal) Act 2018**

**Draft Markets in Financial  
Instruments (Amendment)  
(EU Exit) Regulations 2018**

Includes 4 Information Paragraphs on 4 Instruments

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### *Secondary Legislation Scrutiny Committee (Sub-Committee B)*

The Committee's terms of reference, as amended on 11 July 2018, are set out on the website but are, broadly:

To report on draft instruments and memoranda laid before Parliament under sections 8, 9 and 23(1) of the European Withdrawal Act 2018.

And, to scrutinise –

- (a) every instrument (whether or not a statutory instrument), or draft of an instrument, which is laid before each House of Parliament and upon which proceedings may be, or might have been, taken in either House of Parliament under an Act of Parliament;
- (b) every proposal which is in the form of a draft of such an instrument and is laid before each House of Parliament under an Act of Parliament,

with a view to determining whether or not the special attention of the House should be drawn to it on any of the grounds specified in the terms of reference.

The Committee may also consider such other general matters relating to the effective scrutiny of secondary legislation as the Committee considers appropriate, except matters within the orders of reference of the Joint Committee on Statutory Instruments.

### *Members*

Rt Hon. Lord Cunningham of Felling (Chairman)	Rt Hon. Lord Janvrin	Lord Sherbourne of Didsbury
Baroness Donaghy	Lord Kirkwood of Kirkhope	Rt Hon. Lord Rooker
Lord Goddard of Stockport	Baroness O'Loan	Baroness Watkins of Tavistock
Lord Hodgson of Astley Abbotts	Baroness Redfern	

### *Registered interests*

Information about interests of Committee Members can be found in the last Appendix to this report.

### *Publications*

The Sub-Committee's Reports are published on the internet at <http://www.parliament.uk/seclegbpublications>

The National Archives publish statutory instruments with a plain English explanatory memorandum on the internet at <http://www.legislation.gov.uk/uksi>

### *Committee Staff*

The staff of the Committee are Christine Salmon Percival (Clerk), Paul Bristow (Adviser), Nadine McNally (Adviser), Philipp Mende (Adviser), Jane White (Adviser), Louise Andrews (Committee Assistant) and Ben Dunleavy (Committee Assistant).

### *Information and Contacts*

Any query about the Committee or its work, or opinions on any new item of secondary legislation, should be directed to the Clerk to the Secondary Legislation Scrutiny Committee, Legislation Office, House of Lords, London SW1A 0PW. The telephone number is 020 7219 8821 and the email address is [hlseclegscrutiny@parliament.uk](mailto:hlseclegscrutiny@parliament.uk).

# Third Report

## PROPOSED NEGATIVE STATUTORY INSTRUMENTS UNDER THE EUROPEAN UNION (WITHDRAWAL) ACT 2018

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### Proposed Negative Statutory Instruments about which no recommendation to upgrade is made

- Merchant Shipping and Fishing Vessels (Health and Safety at Work) (Miscellaneous Amendments) (EU Exit) Regulations 2018

## INSTRUMENTS DRAWN TO THE SPECIAL ATTENTION OF THE HOUSE

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### Draft Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018

*Date laid: 17 October 2018*

*Parliamentary procedure: affirmative*

*The Regulations propose to make amendments to the key pieces of EU legislation (“MiFID II”) that govern the buying, selling and organised trading of financial instruments, such as shares, bonds, units in collective investment schemes and derivatives. It is clearly important that the Government should ensure that, if the UK leaves the EU in a “no deal scenario”, the legislation which governs the operation of financial services should continue to work effectively. Given the complexity of such legislation, it seems appropriate to transfer responsibility for applying the detailed requirements to the relevant regulatory bodies in the UK, including the Financial Conduct Authority (FCA), while reserving overall responsibility to HM Treasury (HMT) itself, as this instrument provides.*

*The Regulations propose to give the FCA temporary powers to operate the MiFID II transparency regime with flexibility, during a transitional period. HMT has told us that a statement of policy by the FCA on its use of these temporary powers could not be completed in time to be considered alongside these draft Regulations: while we recognise the timing difficulties, we consider that it would have been helpful to Parliamentary consideration of the Regulations if such a statement had been available.*

*HMT has also pointed out that it might refuse to approve any statement which the FCA proposed to make, if the Department considered that the statement would prejudice any international agreement that the UK hoped to reach. We trust that HMT would make known its reasons for any such refusal, which would no doubt be of interest to Parliament*

*HMT has told us that it is confident that four years beyond the transitional period is an appropriate period of time in which the FCA is able to become operationally ready to carry out its functions relating to transparency. The House may nevertheless wish to ask the Minister about the adequacy of resourcing for the FCA to carry out its new responsibilities.*

**We draw these Regulations to the special attention of the House on the ground that they give rise to issues of public policy likely to be of interest to the House.**

#### *Markets in Financial Instruments Directive*

1. In the Explanatory Memorandum (EM) to these draft Regulations, HM Treasury (HMT) says that the revised Markets in Financial Instruments Directive (MiFID)<sup>1</sup> and the linked Markets in Financial Instruments Regulation (MiFIR) (collectively referred to as MiFID II) are the key pieces of EU legislation that govern the buying, selling, and organised trading of financial instruments, such as shares, bonds, units in collective investment

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<sup>1</sup> Implemented in particular by the Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017 ([SI 2017/701](#)) and the Data Reporting Services Regulations 2017 ([SI 2017/699](#)).

schemes and derivatives. MiFID II took effect in early 2018. HMT summarises its aims as requiring more trades to be conducted through trading venues to promote transparency and financial stability, introducing new safeguards for algorithmic and high frequency trading, and providing a stricter framework for trading commodity derivatives by introducing a position limits and position reporting regime. The draft Regulations make amendments to MiFIR, the tertiary legislation made under MiFID II and the UK legislation which implemented MiFID which would otherwise no longer operate effectively once the UK has left the EU.

2. HMT sets the draft Regulations in the context of its overall approach to financial services regulation. It explains that functions under MiFID II are carried out by EU authorities, principally the European Commission and the European Securities and Markets Authority (ESMA), and that the draft Regulations generally transfer the functions of ESMA to the relevant UK regulator (the Financial Conduct Authority (FCA) or the Bank of England) and the functions of the Commission to HMT itself. They also transfer responsibility for making Binding Technical Standards (BTS) under MiFID II to the relevant UK regulators (the FCA or the Prudential Regulation Authority; in some cases the regulators will have joint responsibility for making BTS). HMT says that this is in line with the approach taken in the Financial Regulators' Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018, which we drew to the attention of the House earlier this year,<sup>2</sup> and which were considered in Grand Committee on 17 October.<sup>3</sup>

#### *Temporary powers for Financial Conduct Authority*

3. In the EM, HMT sets out the detail of the changes being made to address deficiencies in retained EU law in relation to markets in financial instruments. We do not replicate that detail here, but we note in particular that the Regulations propose to grant the FCA a set of temporary powers that will allow it some flexibility over how the MiFID II transparency regime is operated during a transitional period of up to four years in length (which may be ended earlier by HMT). The Department states that powers being granted to the FCA aim to preserve existing outcomes of the transparency regime as far as possible, while providing the FCA with the time required to operate the transparency regime in a standalone UK context (including making any necessary changes to aspects of the transparency regime that are in the BTS) and avoiding any potential for regulatory arbitrage with relevant transparency regimes in third-countries.
4. HMT itemises the temporary powers in the EM, and says that, in exercising them, the FCA will take into account in each instance specified factors (for example, where the use of the relevant power would advance the FCA's integrity objective or where a failure to use the power would unduly harm price formation). It adds that certain transparency conditions (such as the requirement to publish trading carried out under the waivers) will be suspended for the duration of the transitional period, and explains that this is because "the FCA will not have sufficient data or resources during the transitional period to comply with such transparency conditions". Finally, HMT says that the FCA will have a statement of policy on how these temporary powers will be used in place before exit day; and that this

2 [38th Report](#) of Session 2017–19 (HL Paper 179).

3 See: HL Deb, 17 October 2018, [cols 4GC-14GC](#).

statement of policy, and any subsequent changes to it, must be approved by the Treasury before being published.

5. We put questions to HMT about these temporary powers, the policy statement to be made by the FCA, and that body's management of the transparency regime. We are publishing its answers at Appendix 1.

### *Conclusions*

6. It is clearly important that the Government should ensure that, if the UK leaves the EU in a "no deal scenario", the legislation which governs the operation of financial services should continue to work effectively; given the complexity of such legislation, it seems appropriate to transfer responsibility for applying the detailed requirements to the relevant regulatory bodies in the UK, while reserving overall responsibility to HMT itself.
7. The Regulations propose to give the FCA temporary powers to operate the MiFID II transparency regime with flexibility, during a transitional period, which may be justified by the circumstances in which the FCA is taking on these responsibilities. However, HMT has told us that a statement of policy by the FCA on its use of these temporary powers could not be completed in time to be considered alongside these draft Regulations: while we recognise the timing difficulties, we consider that it would have been helpful to Parliamentary consideration of the Regulations if such a statement had been available. HMT has also pointed out that it might refuse to approve any statement which the FCA proposed to make, if the Department considered that the statement would prejudice any international agreement that the UK hoped to reach. We trust that HMT would make known its reasons for any such refusal, which would no doubt be of interest to Parliament.
8. We note that in the EM HMT says that the FCA "will not have sufficient data or resources during the transitional period" to take forward certain transparency conditions. HMT has told us that it is confident that four years beyond the transitional period is an appropriate period of time in which the FCA is able to become operationally ready to carry out its functions relating to transparency. The House may nevertheless wish to ask the Minister about the adequacy of resourcing for the FCA to carry out its new responsibilities.

## **INSTRUMENTS OF INTEREST**

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### **Proceeds of Crime Act 2002 (External Investigations and External Orders and Requests) (Amendment) Order 2018 (SI 2018/1078)**

9. This Order in Council is necessary following amendments made to the Proceeds of Crime Act 2002 (POCA) by the Criminal Finances Act 2017 (the CFA) which provided for the introduction of new powers to investigate, freeze and recover the proceeds of crime. This Order in Council updates the principal Orders in Council made under Part 11 of POCA in light of those amendments, so that equivalent powers are made available to provide assistance to overseas courts and authorities. The consequential changes also include the introduction of two new civil powers to enable the forfeiture of monies stored in bank and building society accounts and the forfeiture of items of personal property, such as precious metals and works of art. For the purposes of external investigations, the Civil Investigation Orders 2013 and 2014 are amended to include Unexplained Wealth Orders and to allow officers of the Serious Fraud Office the requisite investigation powers.

### **Computer Reservation Systems (Amendment) (EU Exit) Regulations 2018 (SI 2018/1080)**

10. An existing EU law provides for a Code of Conduct for businesses using the computerised reservation systems (CRS). The CRS are computer-based systems for airlines to display their flight fares, mostly for use by travel agents to sell to the consumer. The aim is to display on the CRS available flights and fares in an unbiased manner, with no CRS displaying one airline's fares in a preferential way or discriminating against an airline. At present, the monitoring and enforcement body is the European Commission (EC), which has the power to levy fines in case of breach of the rules. Under this instrument, these functions will be transferred from the EC to the UK Civil Aviation Authority (CAA). The Court of Justice of the European Union is currently the route for appeals against fines imposed by the EC. This function will be transferred to the High Court of England and Wales, which will hear appeals against CAA decisions relating to the imposition of fines.

### **Chemical Weapons (Asset-Freezing) and Miscellaneous Amendments Regulations 2018 (SI 2018/1090)**

11. These Regulations, laid by HM Treasury (HMT), put enforcement provisions in place for breaches of the financial sanctions contained in EU Regulation 2018/1542,<sup>4</sup> which introduces new restrictive measures against the proliferation and use of chemical weapons. These include travel restrictions and the freezing of funds of those involved in manufacturing, using or engaging in preparations to use chemical weapons, as well as those who assist or encourage such activities. The EU Regulation came into force on 15 October, and follows from the meeting of the European Council on 22 March of this year, which concluded that the use of chemical weapons was “completely unacceptable, and must be systematically and rigorously

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4 Council Regulation (EU) 2018/1542 of 15 October 2018 concerning restrictive measures against the proliferation and use of chemical weapons:([OJ L259/12](#), 16 October 2018).

condemned”—a conclusion reached in the wake of the use of a chemical nerve agent in Salisbury.<sup>5</sup>

**Special Fissile Materials (Right of Use and Consumption) (EU Exit) Regulations 2018 (SI 2018/1094)**

12. The purpose of these Regulations is to ensure that operators, such as EDF, can exercise their commercial and property rights over special fissile material (enriched uranium and plutonium) without having to comply with obligations under the Euratom Treaty after the UK’s withdrawal from Euratom on 29 March 2019. The Department for Business, Energy and Industrial Strategy (BEIS) explains that, under Article 86 of the Euratom Treaty, all special fissile material in a Euratom Member State is collectively owned by Euratom, with ‘ownership’ referring to a sovereign right of Euratom to ultimately dispose of special fissile materials. This right sits above the normal commercial and property rights that operators have under Article 87 of the Euratom Treaty, which enable them to use and consume special fissile materials subject to certain obligations and safeguards. BEIS explains that while the sovereign Euratom right under Article 86 will cease to apply in the UK following the UK’s withdrawal from Euratom, the Article 87 provisions are directly effective in UK law and need to be revoked to ensure that operators can use special fissile material without having to comply with Euratom Treaty obligations.
13. We asked BEIS what oversight and safeguards arrangements will apply once the UK has left Euratom. The Department explained that special fissile material will continue to be subject to robust safeguards arrangements and that the Nuclear Safeguards Act provides the legal framework for setting up a domestic nuclear safeguards regime, with the Office for Nuclear Regulation as the domestic regulator in place of Euratom. BEIS expects to lay regulations that will set out the details of the new safeguards regime before Parliament under the affirmative procedure in December 2018. According to BEIS, these regulations will offer coverage and effectiveness equivalent to the existing Euratom regime and will exceed international standards.

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5 See: EEAS, ‘Salisbury attack: EU condemns grave challenge to shared security; 17 countries expel Russian diplomats’ (26 March 2018): [https://eeas.europa.eu/headquarters/headquarters-homepage\\_en/42128/Salisbury%20attack:%20EU%20condemns%20grave%20challenge%20to%20shared%20security;%2017%20countries%20expel%20Russian%20diplomats](https://eeas.europa.eu/headquarters/headquarters-homepage_en/42128/Salisbury%20attack:%20EU%20condemns%20grave%20challenge%20to%20shared%20security;%2017%20countries%20expel%20Russian%20diplomats)



## **INSTRUMENTS NOT DRAWN TO THE SPECIAL ATTENTION OF THE HOUSE**

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### **Draft instruments subject to affirmative approval**

Misuse of Drugs Act 1971 (Amendment) Order 2018

### **Draft instruments subject to annulment**

Alterations to the Highway Code Rules 149, 150, 160 and 239 2018

Bath and North East Somerset (Electoral Changes) Order 2018

Hertfordshire (Electoral Changes) (Amendment) Order 2018

### **Instruments subject to annulment**

- SI 2018/1078 Proceeds of Crime Act 2002 (External Investigations and External Orders and Requests) (Amendment) Order 2018
- SI 2018/1080 Computer Reservation Systems (Amendment) (EU Exit) Regulations 2018
- SI 2018/1084 Social Security (Updating of EU References) (Amendment) Regulations 2018
- SI 2018/1085 Social Security (Updating of EU References) (Amendment) (Northern Ireland) Regulations 2018
- SI 2018/1089 Environmental Noise (England) (Amendment) Regulations 2018
- SI 2018/1090 Chemical Weapons (Asset-Freezing) and Miscellaneous Amendments Regulations 2018
- SI 2018/1091 Civil Aviation Act 1982 (Amendment) (EU Exit) Regulations 2018
- SI 2018/1092 Feed-in Tariffs and Contracts for Difference (Amendment) (EU Exit) Regulations 2018
- SI 2018/1094 Special Fissile Materials (Right of Use and Consumption) (EU Exit) Regulations 2018

## APPENDIX 1: DRAFT MARKETS IN FINANCIAL INSTRUMENTS (AMENDMENT) (EU EXIT) REGULATIONS 2018

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### Additional Information from HM Treasury

*Q1: What views have been expressed by stakeholders on the Financial Conduct Authority's (FCA) use of the temporary powers?*

A1: HM Treasury engaged with a wide range of stakeholders, representing large international firms as well as smaller UK businesses, and held detailed discussions on the SI's provisions. Industry participants were supportive of the approach taken in granting the FCA these temporary powers and thought it was a sensible way of dealing with the transparency issues presented by MiFIR as a result of the UK's exit from the EU. HM Treasury received no objections from any of the industry stakeholders on the way these powers would be used by the FCA.

*Q2: Why has the FCA not already made a statement of policy on how these temporary powers will be used, in time for Parliament to consider that statement alongside these draft Regulations?*

A2: The FCA published its first consultation on its approach to dealing with the UK's exit from the EU on 10 October, which will last until the beginning of December. A further consultation is planned dealing in particular with the Binding Technical Standards (BTS) in respect of the MiFID II transparency provisions. A properly considered statement of policy on the use of the temporary powers would need to be informed by these consultations, and as such could not be completed in time to be considered alongside these draft Regulations.

Furthermore, HM Treasury would be required to approve the FCA's statement of policy prior to its finalisation and publication. HM Treasury may refuse to approve the statement of policy if its issuance would prejudice any current or proposed negotiations for an international agreement between the UK and one or more other countries, international organisations (including the EU) or institutions; or under section 410 (international obligations) of FSMA. These provisions are outlined in Regulation 15(5) of the draft Regulations, which inserts a new Regulation 47B on "Statements of Policy" in the Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017.

*Q3: Given that the Explanatory Memorandum states that "the FCA will not have sufficient data or resources during the transitional period to comply with such transparency conditions", how confident is HMT that the FCA can effectively manage the responsibilities which will devolve upon it as a result of these Regulations?*

A3: The temporary powers being granted to the FCA during the transitional period are necessary to enable the FCA to operate the transparency regime in a manner that will uphold market stability during a period of potential market disruption as a result of the UK's exit from the EU. Beyond the transitional period, HM Treasury is confident that four years is an appropriate period of time in which the FCA is able to become operationally ready to carry out its functions relating to transparency under this Regulation and its implementing measures. This is because the FCA estimates that this is the amount of time that it will require in order to complete the following actions before it is operationally ready:

- Manage any immediate post-exit day disruptions; understand how the post-exit day market structure is evolving; and to develop post-exit

day relationships with European authorities, including possible data sharing arrangements

- Develop, publish and conduct consultations and amendments to the relevant BTS
- Analyse consultation responses and publish feedback to the consultations
- Write rules and make necessary IT adjustments to align with the new transparency framework
- Publish final details of the new transparency framework
- Collect data for the new transparency framework
- Publish relevant thresholds under the new transparency framework, allowing sufficient time (approximately six months' notice) before application of the new framework in order to give market participants the opportunity to digest the results and to make any necessary IT adjustments before the final framework is in place

**24 October 2018**

## **APPENDIX 2: INTERESTS AND ATTENDANCE**

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Committee Members' registered interests may be examined in the online Register of Lords' Interests at <http://www.parliament.uk/mps-lords-and-offices/standards-and-interests/register-of-lords-interests>. The Register may also be inspected in the Parliamentary Archives.

For the business taken at the meeting on 30 October 2018, Members declared the following interests:

### **Draft Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018**

Lord Janvrin

*Senior Adviser, HSBC Private Bank (UK) Ltd*

### **Attendance:**

The meeting was attended by Lord Cunningham of Felling, Baroness Donaghy, Lord Goddard of Stockport, Lord Hodgson of Astley Abbots, Lord Janvrin, Lord Kirkwood of Kirkhope, Lord Sherbourne of Didsbury, Baroness Redfern, Lord Rooker and Baroness Watkins of Tavistock.