

## EXPLANATORY MEMORANDUM TO

### THE BANKING ACT 2009 (EXCLUSION OF INSURERS) ORDER 2009

#### 2009 No.

1. This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Command of Her Majesty.

This memorandum contains information for the Joint Committee on Statutory Instruments.

2. **Purpose of the instrument**

2.1 This Order excludes insurers from the definition of “bank” in Parts 1 and 2 of the Banking Act 2009 (“the Act”).

2.2 Part 1 of the Act confers powers on the Bank of England and the Treasury to intervene where a bank is failing, or is about to fail, to meet its threshold conditions<sup>1</sup> for authorisation to perform regulated activities. Part 2 of the Act creates a bank insolvency procedure.

2.3 This Order is made in exercise of the powers conferred by sections 2(2)(c) and 91(2)(c) of the Act to exclude insurers from the scope of the definition of “bank”.

3. **Matters of special interest to the Joint Committee on Statutory Instruments**

3.1 None.

4. **Legislative Context**

4.1 Part 1 of the Act confers powers on the Bank of England and the Treasury to intervene where a bank is failing, or is about to fail, to meet its threshold conditions for authorisation to perform regulated activities. In particular, powers are conferred on the Bank of England to transfer the shares, or some or all of the business, of a failing bank to a commercial purchaser (section 11) or some or all of the business to a bridge bank (section 12).<sup>2</sup> Powers are conferred on the Treasury to transfer a failing bank (or its holding company) into temporary public ownership (sections 13 and 82).

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<sup>1</sup> Under section 41 of, and Schedule 6 to, the Financial Services and Markets Act 2000.

<sup>2</sup> Wholly owned and controlled by the Bank of England.

Part 1 of the Act is applied (subject to some modifications) to building societies by virtue of section 84 of the Act and may be applied to credit unions (section 89).

4.2 Part 2 of the Act creates a bank insolvency procedure which is a modified insolvency procedure for deposit-takers that have eligible depositors under the Financial Services Compensation Scheme (“the FSCS”)<sup>3</sup> and is designed to facilitate the fast and orderly pay out of FSCS compensation<sup>4</sup> (where it is not possible to effect a transfer of the deposit liabilities from a failing bank using powers conferred by Part 1).

4.3 Part 3 of the Act creates a bank administration procedure, which is an administration procedure for banks in cases where an institution has been left insolvent as a result of an exercise of the partial property transfer powers under Part 1 of the Act (where some, and not all, of the business of an institution has been transferred). Objective 1 places a duty on the bank administrator to ensure the supply of necessary services and facilities to the transferee, in order to allow the business transferred from the institution to continue to operate effectively, which is likely to be necessary in order to ensure the resolution is effective. A bank may only be placed into bank administration where the partial property transfer powers under Part 1 have been effected and so the definition of “bank” (as defined in section 2) applies in relation to Part 3.

4.4 “Bank” is defined in section 2(1) (for the purposes of Part 1) and section 91(1) (for the purposes of Part 2) as:

“a UK institution which has permission under Part 4 of the Financial Services and Markets Act 2000 to carry on the regulated activities of accepting deposits (within the meaning of section 22 of that Act, taken with Schedule 3 and any order under section 22).”

4.5 “Bank” does not include building societies, credit unions or any other class of institution excluded by an order made by the Treasury under section 2(2)(c) and/or section 91(2)(c).

4.6 Sections 2(2)(c) and 91(2)(c) of the Act confer powers on the Treasury to make Orders, subject to the draft affirmative procedure, excluding any other class of institution from the definition of “bank”. This Order is made in exercise of those powers to exclude insurers from the definition of “bank”.

## **5. Territorial Extent and Application**

5.1 This instrument applies to the United Kingdom.

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<sup>3</sup> The FSCS was established under Part 15 of the Financial Services and Markets Act 2000 and is the UK’s compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation if a firm is unable, or likely to be unable, to pay claims against it. The FSCS is funded by levies imposed on authorised persons.

<sup>4</sup> Currently limited to a maximum of £50,000 per eligible depositor.

## 6. European Convention on Human Rights

6.1 The Financial Services Secretary to the Treasury has made the following statement regarding Human Rights:

‘In my view the provisions of the Banking Act 2009 (Exclusion of Insurers) Order 2009 are compatible with the Convention rights.’

## 7. Policy background

- *What is being done and why*

7.1 The Act establishes a special resolution regime (“SRR”), providing the Authorities (the Bank of England, the Treasury and the Financial Services Authority (“FSA”)) with the tools to deal with banks that are failing, or are about to fail to meet, their threshold conditions.

7.2 The conventional way of defining a ‘bank’ in legislation (for example in tax law) is to refer to a UK institution that has a regulatory permission granted by the FSA to accept deposits, and then to refine the definition to exclude regulated bodies that do not carry out banking business. This is the approach taken in sections 2 and 91 of the Act.

7.3 Under sections 2 and 91 of the Act, credit unions and building societies are explicitly excluded from the definition of “bank”, and consequently from the scope of Parts 1 to 3 of the Act. Provision is made elsewhere in the Act to apply these Parts to these types of institution with appropriate modifications (for example, section 84 applies Part 1 to building societies and section 89 confers a power to apply, by order, Part 1 to credit unions).

7.4 Insurance companies are not explicitly excluded from the definition of “bank”, and consequently an insurer may fall within the scope of Parts 1 and 2 of the Act (and for the reason given in paragraph 4.3, Part 3).

7.5 Under the Financial Services and Markets Act 2000, institutions can apply for multiple permissions to carry on regulated activities such as accepting deposits and dealing in investments. Where institutions meet with the conditions for authorisation, the FSA will issue a permission for each institution that lists all the regulated activities the institution may undertake and any restrictions that apply to those activities. Most institutions that are authorised by the FSA to carry on insurance business also have the permission to accept deposits for the purposes of carrying on insurance business although they are prevented from carrying out banking business by European law.

7.6 As a result of the permission to accept deposits for the purposes of carrying on insurance business, insurance companies fall within the scope of the definition of “bank” in sections 2(1) and 91(1) of the Act. This means that theoretically the Authorities could exercise the SRR powers (referred to in paragraphs 4.1 to 4.3) in relation to such institutions.

7.7 The Government believes that it is appropriate to exclude insurers from the definition of “bank” in sections 2(1) and 91(1) for the reasons set out below.

7.8 First, the powers under Part 1 of the Act are not designed to be used to resolve a failing insurance company. For example, the first three of the special resolution objectives (section 4) refer explicitly to ‘banking services’, ‘banking systems’ and ‘protection of depositors’; none of which are applicable to insurance companies (the other two objectives refer to the Government’s human rights obligations and protection of public funds). Various other provisions of Parts 1 to 3 of the Act would require certain modifications if they were to be applied effectively to insurers, owing to differences in the structure of insurance and banking institutions, and the way in which they carry out their business.

7.9 Second, as implied by its short title, the purpose of the Act is to deal with firms that carry out banking business, not insurance business. The published consultation documents refer to banks and building societies, not insurance companies, and application of the SRR to insurance companies was not substantively debated in the passage of the Banking Bill through Parliament. The published statutory Code of practice (issued under section 5 of the Act), to which the Authorities must have regard in exercising the SRR powers, also refers only to banks and building societies.

7.10 For these reasons, the Government believes that it is appropriate to make this order to explicitly exclude insurers from the definition of “bank” in sections 2(1) and 91(1) of the Act.

## **8. Consultation outcome**

8.1 The Treasury has consulted with the Banking Liaison Panel (“BLP”) established under section 10 of the Act and the Bank of England, the FSA and the Association of British Insurers.

## **9. Guidance**

9.1 It is not considered necessary to issue specific guidance in connection with this Order. However, the Code of Practice issued under section 5 of the Act on 23 February 2009 contains guidance as to how and in what circumstances the Authorities will use the special resolution tools under the Act.

## **10. Impact**

10.1 The impact on business, charities or voluntary bodies is nil.

10.2 The impact on the public sector is nil.

10.3 An Impact Assessment has not been prepared for this instrument.

## **11. Regulating small business**

11.1 The legislation does not apply to small business.

## **12. Monitoring & review**

12.1 The BLP will keep this Order under review and, where appropriate, provide further advice to the Treasury about this Order. The Treasury will also keep this Order under review.

## **13. Contact**

Phelan Hill (tel: 020 7270 6105 or email: [phelan.hill@hmtreasury.gsi.gov.uk](mailto:phelan.hill@hmtreasury.gsi.gov.uk)) can answer any queries regarding the instrument.