EXPLANATORY MEMORANDUM TO

THE BANKING ACT 2009 (RESTRICTION OF PARTIAL PROPERTY TRANSFERS) (RECOGNISED CENTRAL COUNTERPARTIES) ORDER 2014

2014 No. 1828

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 The purpose of the instrument is to make provision regarding the application of the special resolution regime ("SRR") provided for in Part 1 of the Banking Act 2009 ("the Act") to recognised central counterparties ("RCCPs"). In particular, the instrument places restrictions on the making of partial property transfers made in respect of RCCPs.

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 provided for a SRR that can be applied in certain circumstances to banks. Section 102 of the Financial Services Act 2012 ("the 2012 Act") made amendments to Part 1 of the Act so as to allow for the SRR to additionally be applied with modifications to "UK clearing houses" in certain circumstances.

4.2 The term "UK clearing house" was defined by the new section 89G of the Act. Section 89G was amended by regulation 25 of the Financial Services and Markets Act 2000 (Over the Counter Derivatives, Central Counterparties and Trade Repositories) Regulations 2013 (S.I. 2013/504) and the term "recognised central counterparty" was substituted for "UK clearing house". A "recognised central counterparty" is a central counterparty in respect of which a recognition order has been made pursuant to Part 18 of the Financial Services and Markets Act 2000.

4.3 Under the SRR, in certain circumstances the Bank of England has the power to make property transfer instruments in respect of a RCCP. Such instruments may provide for the transfer of the property, rights and liabilities of a RCCP. A "partial property transfer" is a property transfer instrument which provides for the transfer of some, but not all, of the property, rights and liabilities of a RCCP (see section

47 of the Act). Sections 47(2) and 48(2) of the Act allow for the Treasury to make orders restricting the making of partial property transfers. The purpose of this instrument is to set out those restrictions.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

The Economic Secretary to the Treasury has made the following statement regarding Human Rights:

In my view the provisions of the Banking Act 2009 (Restriction of Partial Property Transfers) (Recognised Central Counterparties) Order 2014 are compatible with the Convention rights.

7. Policy background

- What is being done and why

7.1 This instrument provides legislative safeguards for the benefit of direct and indirect users of clearing services provided by RCCPs. These safeguards will provide them with greater certainty as to how a partial property transfer might affect their contractual rights and to ensure that there are appropriate restrictions and limitations on the making of a partial property transfer.

7.2 If such persons do not have legal certainty as to how a partial property transfer will affect their contractual interests, negative market reactions are likely. There needs to be certainty with respect to the use of partial property transfers in order to ensure that risk reducing arrangements, including set-off and netting arrangements, are effective.

7.3 To that end, this instrument provides for the following safeguards to apply to partial property transfers made in respect of RCCPs:

- Protection for set – off and netting arrangements to the extent that all positions within a RCCP which are netted within a segregated business line must be transferred together or not at all. A "segregated business line" in this context is defined as a product set cleared by a RCCP that is covered by distinct default protections. A number of RCCPs currently operate more than one segregated business line;
- Partial property transfers cannot be made that would result in the contravention of EU law. In particular, care will have to be taken when making partial property transfers in respect of a RCCP so as to ensure

that the requirements of Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements are not infringed;
- Protection for secured liabilities;
- Protection for market contracts;
- Protection for trust arrangements;
- Restrictions on reverse partial property transfers (i.e. transfers of property, rights and liabilities back to the original transferor);
- Restrictions on the use of partial property transfers made in respect of companies in the same group as the failing RCCP.

- Consolidation

7.4 This instrument makes minor amendments to domestic legislation. Since the amendments are limited in scope, consolidation is not merited.

8. Consultation outcome

8.1 The Government consulted widely on the safeguards that should be implemented to provide sufficient legal certainty to financial markets participants while allowing the Bank of England sufficient flexibility to enable it to effect partial property transfers in the interests of financial stability and minimising tax-payer exposure. The consultation opened on September 26 September 2013 and closed on the 21 November 2013. The consultation lasted 8 weeks. HM Treasury received 10 written responses from industry including RCCPs, banks, law firms and trade associations. The reason for the shorter consultation period of 8 weeks rather than 12 is that having consulted on these policies previously when developing the relevant primary legislation, stakeholders where familiar with the issues. This order reflects the outcome of that consultation process.

9. Guidance

9.1 It is not considered necessary to issue specific guidance in connection with this Order. However, under section 5 of the Act, the Treasury is obliged to issue a code of practice about the use of the stabilisation powers provided for in Part 1 of the Act. The Code of Practice will contain guidance on the approach that will be taken when making a partial property transfer in respect of RCCP.

10. Impact

10.1 The impact on business, charities or voluntary bodies is negligible. This instrument will only have an impact in the event that it necessary to make partial property transfer in respect of a RCCP.

10.2 The impact on the public sector is negligible.

10.3 No specific impact assessment was conducted in respect of this instrument. When Part 1 of the 2009 Act was amended by the 2012 Act in order to allow the SRR provided for in Part 1 of the 2009 Act to be applied to "non – banks" (including RCCPs), an impact assessment was carried out. The purpose of this instrument is to add further detail as to how the SRR would be applied to RCCPs in the event of a crisis, and the impact assessment carried out prior to the amendment of Part 1 of the 2009 Act by the 2012 Act already covers the necessary ground. A copy of that impact assessment is available on the Treasury's website: http://www.hm-treasury.gov.uk/

11. Regulating small business

11.1 The legislation does not apply to small business.

12. Monitoring & review

12.1 The Act requires the Treasury to make arrangements for a panel to advise the Treasury about the effect of the SRR on banks, persons with which banks do business and the financial markets. In particular the panel may advise the Treasury about the exercise of powers to make certain statutory instruments. This panel, the Banking Liaison Panel, will keep this instrument under review and, where appropriate, will provide advice to the Treasury about the operation of this instrument. The Treasury will also keep this instrument under review itself.

13. Contact

Elizabeth Cowell at the HM Treasury Tel: 02072701007 email: Elizabeth.Cowell@HMTreasury.gsi.gov.uk can answer any queries regarding these instruments.