

EXPLANATORY MEMORANDUM TO
THE FINANCIAL SERVICES AND MARKETS ACT 2000 (REGULATED
ACTIVITIES) (AMENDMENT) ORDER 2018

2018 No. 831

1. Introduction

- 1.1 This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Command of Her Majesty.
- 1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

- 2.1 This instrument expands the definition of alternative finance investment bonds (AFIBs) to allow these to be admissible for trading on additional types of financial trading venues, known as multilateral trading facilities (MTFs) and organised trading facilities (OTFs). These are markets for the issuing and trading of debt securities which are regulated by the platform's operator, the London Stock Exchange for example.
- 2.2 This ensures equivalent regulatory treatment of AFIBs with conventional bonds, meeting the government's commitment to provide a level-playing field for Islamic Finance instruments in the UK and thereby removing a potential obstacle to the use of UK venues for the issue and trading of AFIBs.
- 2.3 This Order also includes a provision that a person carrying on the regulated activity of administering a benchmark will be seen as carrying on the activity by way of business.

3. Matters of special interest to Parliament

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

- 3.1 This Order is intended to track an amendment made by section 34(2) of the Finance Act 2018 which came into force on 1 April 2018. It is necessary to bring this Order into force with immediate effect rather than after the expiry of 21 days according to the practice which is now recommended so as to reduce the length of time the differing treatment is in effect. The alignment of the tax and regulatory treatment of AFIBs will be to the benefit of business and additional time is not considered to be needed to prepare for this

Other matters of interest to the House of Commons

- 3.2 Disregarding minor or consequential changes, the territorial application of this instrument includes Scotland and Northern Ireland.

4. Legislative Context

- 4.1 This Order is intended to bring the regulatory treatment of AFIBs under the Financial Services and Markets Act 2000 ("FSMA") into line with section 34(2) of the Finance Act 2018 (Debt traded on a multilateral trading facility). The Finance Act 2018

expands the definition of AFIBs (also known as investment bond arrangements) to include those traded on a multilateral trading facility. AFIBs are specified as an investment in article 77A of the RAO, and the definition of an AFIB specifies which trading venues an instrument may be traded on to meet the requirements for qualification as an AFIB. The amendment to article 77A correspondingly amends the definition of AFIBs to include those traded on MTFs and OTFs, and this will ensure that regulatory and tax regimes are harmonised for these products to give certainty to investors and increase the competitiveness of UK markets.

- 4.2 Article 3 amends the Financial Services and Markets Act 2000 (Carrying on Regulated Activities by Way of Business) Order 2001 (S.I. 2001/1177) so that a person administering a benchmark as specified in the RAO will be regarded as carrying on the activity by way of business. This amendment is consequential on the coming into force of the EU Benchmarks Regulation (EU) 2016/1011 which was given effect by the Financial Services and Markets Act 2000 (Benchmarks) Regulations 2018 (S.I. 2018/135).

5. Extent and Territorial Application

- 5.1 The extent of this instrument is the United Kingdom.
- 5.2 The territorial application of this instrument is the United Kingdom.

6. European Convention on Human Rights

- 6.1 The Economic Secretary to the Treasury, John Glen MP, has made the following statement regarding Human Rights:
- “In my view the provisions of the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2018 are compatible with the Convention rights.”

7. Policy background

What is being done and why

- 7.1 The UK is recognised as the leading Western hub for Islamic finance with the UK becoming the first Western nation to issue a sovereign sukuk (Islamic-equivalent bond) in 2014. The government is committed to the development of Islamic finance in the UK to support the international competitiveness of the UK as a financial centre and destination for investment, and to ensure that nobody in the UK is denied access to competitively priced financial products on account of their faith.
- 7.2 Sukuk are one of the most prominent instruments used in Islamic finance and are structured differently to their conventional counterparts in order to adhere to key Islamic principles, such as not giving rise to conventional interest income. In 2010, the UK introduced legislation to ensure that alternative finance investment bonds (AFIBs), such as sukuk, are treated in a similar manner to conventional debt securities for UK regulatory purposes. To date, over \$50 billion USD has been raised by sukuk listed on the UK's primary capital markets.
- 7.3 The Finance Act 2018 widened the definition of AFIBs in tax legislation to allow such instruments to qualify for the Quoted Eurobond Exemption (QEE) which exempts MTFs from withholding tax on interest. This instrument introduces an equivalent

definition change in regulation to allow AFIBs to be admitted to trading on an MTF or OTF.

- 7.4 Conventional bonds are already traded on MTFs and this change would ensure that AFIBs benefit from the same regulatory treatment, thereby removing an obstacle to the use of UK venues for the issue and trading of AFIBs, where the UK has been facing increasing competition from other European venues.

Consolidation

- 7.5 The Treasury does not currently intend to consolidate the legislation amended by this instrument.

8. Consultation outcome

- 8.1 The Treasury has not considered it necessary to consult on the change made by this instrument because it gives effect to an equivalent definition change in tax legislation made as part of the Finance Act 2018.

9. Guidance

- 9.1 It is not considered necessary to issue specific guidance in connection with this change.

10. Impact

- 10.1 The impact on business, charities or voluntary bodies is minimal. As a result of the change made by this instrument, MTF or OTF operators wishing to trade AFIBs on their trading venues would need to apply for a variation of their permission from the Financial Conduct Authority. Currently, there is only one firm with FCA permission to operate an MTF or OTF trading instruments within the existing scope of Article 77A of the Financial Services and Markets Act 2000 (Regulated Activities) Order.
- 10.2 There is no impact on the public sector.
- 10.3 In line with Better Regulation guidance, the Treasury considers that the impact on business will be less than £5 million a year. Due to the limited impact, a business impact assessment was not required.

11. Regulating small business

- 11.1 The legislation applies to activities that are undertaken by small businesses, to the extent that they wish to trade AFIBs on their trading venues.
- 11.2 No specific action is proposed to minimise regulatory burdens on small businesses.

12. Monitoring & review

- 12.1 If the market evolves and new structures emerge that do not fit with the existing regulatory framework or are subject to legislation that is not commensurate with their economic and risk profile, we may review these developments and consider whether any additional legislative action is required.

13. Contact

- 13.1 Ronald Bohlander at HM Treasury Telephone: 0207 270 2831 or email: Ronald.Bohlander@hmtreasury.gov.uk can answer any queries regarding the instrument.