EXPLANATORY MEMORANDUM TO

THE FINANCIAL CONGLOMERATES AND OTHER FINANCIAL GROUPS (AMENDMENT ETC.) (EU EXIT) REGULATIONS 2019

2019 No. 264

1. Introduction

1.1 This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Act.

2. Purpose of the instrument

2.1 This statutory instrument acts to address deficiencies arising in legislation related to financial conglomerates as a result of the United Kingdom leaving the European Union. This instrument acts to ensure that the UK's regulation of financial conglomerates and other financial groups continues to operate as intended in the UK once the UK has left the EU.

Explanations

What did any relevant EU law do before exit day?

2.2 The EU Financial Conglomerates Directive (FICOD – No. 2002/87/EC) was originally adopted in 2002 and subsequently amended in 2011. It was developed to address the lack of specific prudential treatment for financial conglomerates – groups with activities in more than one of the insurance, banking, or investment services sectors. The directive therefore contributes to greater financial stability and consumer protection.

2.3 FICOD applies specifically to a group with at least one entity in the insurance sector, and at least one entity in the banking or investment services sector. One of these entities, according to the EU definition, must be located in the European Economic Area (EEA), while the other(s) may be located anywhere in the world (including the EEA).

2.4 FICOD sets out specific requirements on solvency to prevent the same capital being used more than once as a buffer against risk in different entities in the same conglomerate. It also sets out requirements related to conglomerates' management, risk management, and requirements for information sharing with relevant regulators.

2.5 The UK subsequently implemented FICOD through the Financial Conglomerates and Other Financial Groups Regulations 2004 (FICOR - 2004 No. 1862). This instrument therefore identifies and amends deficiencies in the EU text to ensure that FICOR will remain operative in a UK-only context post-exit.

Why is it being changed?

2.6 FICOR will contain deficiencies as a result of the UK's withdrawal from the EU. Without an instrument to address these deficiencies, significant aspects of FICOR would become legally inoperable post-exit. For example, if the definition of 'financial conglomerate' were not changed from its current EU-wide scope then it would be unclear which firms would be regulated within the UK. Meanwhile, the jurisdiction of

the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) over financial conglomerates would also not be clear. Without an effective regulatory regime over financial conglomerates there would be extensive uncertainty for firms who are currently regulated under FICOR.

2.7 Failing to have adequate prudential supervision of financial conglomerates would subsequently risk the UK being in a position where it is failing to meet commitments to implement internationally-agreed post-crisis prudential reforms made as part of the UK's membership of the G20.

What will it now do?

2.8 This instrument therefore makes the necessary amendments to FICOR to ensure it continues to operate effectively at the point at which the UK leaves the EU, allowing the UK to continue to meet its G20 commitments. These include necessary changes to the definition of a financial conglomerate, as well as making changes to functions currently allocated to EU bodies, transferring them to UK bodies. More detail on the specific changes being made in these areas can be found in Section 7.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

3.2 The territorial application of this instrument includes Scotland and Northern Ireland.

3.3 The powers under which this instrument is made cover the entire United Kingdom (see section 8(1) of, and paragraph 21 of Schedule 7 to the European Union (Withdrawal) Act 2018) and the territorial application of this instrument is not limited either by the Act or by the instrument.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is to the whole of the United Kingdom.

4.2 The territorial application of this instrument is to the whole of the United Kingdom.

5. European Convention on Human Rights

5.1 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 Conglomerates and Other Financial Groups (Amendment etc.) (EU Exit) Regulations 2019 are compatible with the Convention rights."

6. Legislative Context

6.1 This instrument amends FICOR. Amendments to FICOR have previously been made through the Financial Conglomerates and Other Financial Groups (Amendment) Regulations 2013 (2013 No. 1162).

6.2 FICOR is the UK regulation that implements FICOD. The PRA and FCA are responsible for implementing other parts of FICOD.

6.3 Amendments to FICOR are being made to address failures in the retained law to operative effectively once the UK withdraws from the EU. These amendments are being made using powers in the European Union (Withdrawal) Act 2018 (EUWA).

7. Policy background

What is being done and why?

7.1 The UK will leave the EU on 29 March 2019. The UK and the EU have agreed the terms of an implementation period that will start on 29 March 2019 and last until 31 December 2020. This will provide time to introduce the new arrangements that will underpin the future UK-EU relationship, and provide valuable certainty for businesses and individuals. During the implementation period, common rules will continue to apply. The UK will continue to implement new EU law that comes into effect and the UK will continue to be treated as part of the EU's single market in financial services. This will mean that access to each other's markets will continue on current terms and businesses, including financial services firms, will be able to trade on the same terms as now until 31 December 2020. UK firms will need to comply with any new EU legislation that becomes applicable during the implementation period.

7.2 The government is seeking a deep and special future partnership with the EU, which should be greater in scope and ambition than any such agreement before and encompass financial services. Given the highly regulated nature of financial services, the volume of trade between UK and EU markets, and a shared desire to manage financial stability risks, the UK proposes a new economic and regulatory arrangement that will preserve mutually beneficial cross-border business models and economic integration for the benefit of businesses and consumers. Decisions on market access would be autonomous in our proposed model, but would be underpinned by stable institutional processes in a bilateral agreement and continued close regulatory and supervisory cooperation.

7.3 While the government believes that there will be a deal and an implementation period in place, it has a duty to plan for all eventualities, including a 'no deal' scenario. To prepare for this unlikely eventuality, HM Treasury intends to use powers in the European Union (Withdrawal) Act 2018 (EUWA) to ensure that the UK continues to have a functioning financial services regulatory regime in all scenarios.

7.4 The EUWA repeals the European Communities Act 1972 and converts into UK domestic law the existing body of directly applicable EU law (including EU Regulations). It also preserves UK laws relating to EU membership – e.g. legislation implementing EU Directives. This body of law is referred to as "retained EU law". The EUWA also gives ministers a power to prevent, remedy or mitigate any failure of EU law to operate effectively, or any other deficiency in retained EU law, through SIs. These contingency preparations for financial services legislation are sometimes referred to as 'onshoring'. These SIs are not intended to make policy changes, other than to reflect the UK's new position outside the EU, and to smooth the transition to this situation. The scope of the power is drafted to reflect this purpose and is subject to further restrictions, such as the inability to use the power to impose or increase taxation, or establish a public authority. The power is also time-limited and falls away two years after exit day.

7.5 Wherever practicable, the proposed approach is that the same laws and rules that are currently in place in the UK would continue to apply at the point of exit, providing

continuity and certainty as we leave the EU. However, if the UK does not enter an implementation period, some changes would be required to reflect the UK's new position outside the EU from 29 March 2019.

7.6 If the UK were to leave the EU without a deal, the UK would be outside the EU's framework for financial services. The UK's position in relation to the EU would be determined by the default Member State and EU rules that apply to third countries at the relevant time. The European Commission has confirmed that this would be the case.

7.7 In light of this, the approach in this scenario cannot and does not rely on any new, specific arrangements being in place between the UK and the EU. As a general principle, the UK would also need to default to treating EU Member States largely as it does other third countries, although there are cases where a different approach would be needed including to provide for a smooth transition to the new circumstances.

7.8 HM Treasury published a document on 27 June 2018, which sets out in more detail HM Treasury's approach to financial services legislation under the European Union (Withdrawal) Act. (https://www.gov.uk/government/publications/financial-services-legislation-under-the-eu-withdrawal-act)

7.9 This instrument makes amendments to FICOR to ensure that the UK's regulation of financial conglomerates and other financial groups continues to operate effectively in the UK once the UK has left the EU. These changes include:

The definition of a financial conglomerate

7.10 A financial conglomerate is defined under FICOD as a group with at least one entity in the insurance sector, and at least one entity in the banking or investment services sectors. One of these entities must be located within the EEA while the other(s) may be located anywhere in the world (including the EEA).

7.11 Once the UK leaves the EU it will be necessary to reduce the geographical scope of this provision, as the onshored version of FICOD will only be applicable within the UK. Part 2 of this instrument therefore changes this geographical restriction so that one entity must be located in the UK, rather than the EEA, while the other(s) may be located anywhere in the world. This is in line with how FICOD currently treats third countries, and means that the EEA will be treated as a third country by the UK in the event of no deal.

7.12 In practice this change will not have a material effect on financial conglomerates already operating in the UK. A financial conglomerate with at least one entity operating in the UK before exit met the FICOD requirement by having at least one entity operating in the EEA. Post-exit, the same financial conglomerate will continue to meet the new requirement in the instrument. For example, if a bank located in the UK owned an insurance company in Spain, the group would be classified as a financial conglomerate – both under this instrument and the EU terms of FICOD. Therefore, firms will not experience a change in their status as a financial conglomerate as a result of this change in definition. Furthermore, a financial conglomerate with an entity located in the EU27, and a second elsewhere (e.g. the USA), would still be subject to FICOD requirements.

The definition of a competent authority

7.13 Competent authorities are the organisations nominated by Member States to ensure compliance with EU law. In the current text of FICOR, a competent authority can mean any national regulator within the EEA as there is a joint supervisory framework in place to ensure only one regulator has overall responsibility for a conglomerate's business. However, as the UK will be outside of this supervisory framework post-exit, Part 2 of this instrument amends the definition of a competent authority to mean only UK regulators.

Transfer of functions

7.14 Under FICOR and FICOD, various functions are carried out by the European Supervisory Authorities – in particular, the European Banking Authority, European Securities and Markets Authority, and the European Insurance and Occupational Pensions Authority.

7.15 In line with the Government's cross-cutting approach on the transfer of functions, Part 5 of this instrument ensures that these functions are transferred to the appropriate UK bodies – in this case, the PRA and FCA. The transfer of these functions will not change the existing overarching supervisory responsibilities of the PRA and FCA – the functions that they would adopt through this instrument are broadly in line with their responsibilities today.

7.16 The European Supervisory Authorities are currently required by FICOD to publish and maintain a list of financial conglomerates. In Part 2, this instrument acts to transfer this function jointly to the PRA and FCA and, in Part 4, includes a savings provision to ensure that decisions made by the European Supervisory Authorities before the UK leaves the EU continue to have effect after exit day.

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

8.1 This instrument is being made using the power in section 8 of the European Union (Withdrawal) Act 2018 in order to address failures of retained EU law to operate effectively or other deficiencies arising from the withdrawal of the United Kingdom from the European Union. In accordance with the requirements of the European Union (Withdrawal) Act 2018 Act the Minister has made the relevant statements as detailed in Part 2 of the Annex to this Explanatory Memorandum.

9. Consolidation

9.1 There are currently no plans to consolidate the relevant legislation.

10. Consultation outcome

10.1 HM Treasury has not undertaken a consultation on the instrument, but has engaged with relevant stakeholders on its approach to Financial Services legislation under the European Union (Withdrawal) Act 2018, including on this instrument, to familiarise them with the legislation ahead of laying.

10.2 An explanatory policy note was published on the 22nd October 2018, and the instrument was also published in draft on the 21st December 2018 to maximise transparency ahead of laying. (https://www.gov.uk/government/publications/draft-

financial-conglomerates-and-other-financial-groups-amendment-eu-exit-regulations-2018)

10.3 The Bank of England and the FCA are undertaking public consultation on any changes they propose to make to Binding Technical Standards and rules made under the powers conferred upon them by the Financial Services and Markets Act 2000. These consultations can be found at:

https://www.bankofengland.co.uk/paper/2018/the-boes-approach-to-amending-financial-services-legislation-under-the-eu-withdrawal-act-2018

https://www.fca.org.uk/publications/consultation-papers/cp18-28-brexit-proposed-changes-handbook-bts-first-consultation

11. Guidance

11.1 No further guidance is being published alongside this instrument.

12. Impact

12.1 The impact on business will primarily consist of one off familiarisation costs, particularly for those financial conglomerates that are directly subject to FICOR. There are currently 16 financial conglomerate firms listed by the EU as having the UK as their lead coordinator – all would be subject to the revisions made to FICOR. HM Treasury does not expect there to be any ongoing change in the UK regulatory burden placed on financial conglomerates as a result of this instrument. Furthermore, as the European Supervisory Authorities will have no jurisdiction over the UK post-exit, reporting requirements under FICOR will be transferred to the PRA and FCA. However, this should not lead to a change in the required reporting – just the authority receiving the reports.

12.2 There is no significant impact on charities or voluntary bodies. In the public sector the FCA and PRA will be responsible for carrying out functions under FICOD and FICOR, as detailed above. HM Treasury has been working closely with the FCA and PRA to ensure that they are well prepared for taking on these additional functions.

12.3 A full Impact Assessment will be published alongside the Explanatory Memorandum on the legislation.gov.uk website.

13. Regulating small business

13.1 The legislation does not directly apply to activities that are undertaken by small businesses, as financial conglomerates are groups with activities in more than one of the insurance, banking, or investment services sectors.

14. Monitoring & review

14.1 As this instrument is made under the EU Withdrawal Act 2018, no review clause is required.

15. Contact

15.1 Luke Miller at HM Treasury Telephone: 02072704399 or email: Luke.Miller@hmtreasury.gov.uk and Pawel Wargan at HM Treasury Telephone: 02072706167 or email: Pawel.Wargan@hmtreasury.gov.uk can be contacted with any queries regarding the instrument.

15.2 Clare Bolingford, Deputy Director for Securities Markets and Banking, at HM Treasury can confirm that this Explanatory Memorandum meets the required standard.

15.3 The Economic Secretary to the Treasury John Glen can confirm that this Explanatory Memorandum meets the required standard.

Annex

Statements under the European Union (Withdrawal) Act 2018

Part 1

Table of Statements under the 2018 Act

This table sets out the statements that may be required under the 2018 Act.

Statement	Where the requirement sits	To whom it applies	What it requires
Sifting	Paragraphs 3(3), 3(7) and 17(3) and 17(7) of Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) to make a Negative SI	Explain why the instrument should be subject to the negative procedure and, if applicable, why they disagree with the recommendation(s) of the SLSC/Sifting Committees
Appropriate-ness	Sub-paragraph (2) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	A statement that the SI does no more than is appropriate.
Good Reasons	Sub-paragraph (3) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	Explain the good reasons for making the instrument and that what is being done is a reasonable course of action.
Equalities	Sub-paragraphs (4) and (5) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	Explain what, if any, amendment, repeals or revocations are being made to the Equalities Acts 2006 and 2010 and legislation made under them. State that the Minister has had due regard to the need to eliminate discrimination and other conduct prohibited under the Equality Act 2010.
Explanations	Sub-paragraph (6) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2 In addition to the statutory obligation the Government has made a political commitment to include these statements alongside all EUWA SIs	Explain the instrument, identify the relevant law before exit day, explain the instrument's effect on retained EU law and give information about the purpose of the instrument, e.g., whether minor or technical changes only are intended to the EU retained law.
Criminal offences	Sub-paragraphs (3) and (7) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9, and	Set out the 'good reasons' for creating a criminal offence, and the penalty attached.

		23(1) or jointly exercising powers in Schedule 2 to create a criminal offence	
Sub-delegation	Paragraph 30, Schedule 7	Ministers of the Crown exercising sections 10(1), 12 and part 1 of Schedule 4 to create a legislative power exercisable not by a Minister of the Crown or a Devolved Authority by Statutory Instrument.	State why it is appropriate to create such a sub-delegated power.
Urgency	Paragraph 34, Schedule 7	Ministers of the Crown using the urgent procedure in paragraphs 4 or 14, Schedule 7.	Statement of the reasons for the Minister's opinion that the SI is urgent.
Explanations where amending regulations under 2(2) ECA 1972	Paragraph 13, Schedule 8	Anybody making an SI after exit day under powers outside the European Union (Withdrawal) Act 2018 which modifies subordinate legislation made under s. 2(2) ECA	Statement explaining the good reasons for modifying the instrument made under s. 2(2) ECA, identifying the relevant law before exit day, and explaining the instrument's effect on retained EU law.
Scrutiny statement where amending regulations under 2(2) ECA 1972	Paragraph 16, Schedule 8	Anybody making an SI after exit day under powers outside the European Union (Withdrawal) Act 2018 which modifies subordinate legislation made under s. 2(2) ECA	Statement setting out: a) the steps which the relevant authority has taken to make the draft instrument published in accordance with paragraph 16(2), Schedule 8 available to each House of Parliament, b) containing information about the relevant authority's response to— (i) any recommendations made by a committee of either House of Parliament about the published draft instrument, and (ii) any other representations made to the relevant authority about the published draft instrument, and, c) containing any other information that the relevant authority considers appropriate in relation to the scrutiny of the instrument or draft instrument which is to be laid.

Part 2

Statements required when using enabling powers under the European Union (Withdrawal) 2018 Act

1. Appropriateness statement

1.1 The Economic Secretary to the Treasury, John Glen MP, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In my view the Financial Conglomerates and Other Financial Groups (Amendment etc.) (EU Exit) Regulations 2019 does no more than is appropriate".

1.2 This is the case because: it is in line with the European Union (Withdrawal) Act 2018 in serving to make those changes necessary to provide a functioning statute book in relation to prudential requirements on the day we leave the EU.

2. Good reasons

2.1 The Economic Secretary to the Treasury, John Glen MP, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In my view there are good reasons for the provisions in this instrument, and I have concluded they are a reasonable course of action.

2.2 These are: If this Government were not to proceed with this legislation, then significant aspects of the UK's prudential regulation of financial conglomerates would become legally inoperable. The UK would risk not meeting international commitments made as part of its membership of the G20. This could expose the UK to financial stability risks and could create a period of uncertainty for the UK."

3. Equalities

3.1 The Economic Secretary to the Treasury, John Glen MP, has made the following statement:

"The Financial Conglomerates and Other Financial Groups (Amendment etc.) (EU Exit) Regulations 2019 does not amend, repeal or revoke a provision or provisions in the Equality Act 2006 or the Equality Act 2010 or subordinate legislation made under those Acts."

3.2 The Economic Secretary to the Treasury John Glen MP has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In relation to the Financial Conglomerates and Other Financial Groups (Amendment etc.) (EU Exit) Regulations 2019 I, John Glen MP, have had due regard to the need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010."

4. Explanations

4.1 The explanations statement has been made in section 2 of the main body of this explanatory memorandum.

5. Legislative sub-delegation

5.1 The Economic Secretary to the Treasury, John Glen MP, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In my view it is appropriate to create a relevant sub-delegated power in The Financial Conglomerates and Other Financial Groups (Amendment etc.) (EU Exit) Regulations 2019".

5.2 This is appropriate because: The Financial Conglomerates and Other Financial Groups (Amendment etc) (EU Exit) Regulations 2019 transfers certain functions currently exercised by EU bodies to the appropriate UK regulators. Without transferring these functions, the jurisdiction of the Prudential Regulation Authority and Financial Conduct Authority over financial conglomerates would not be clear and UK regulators would not have appropriate oversight over such conglomerates.