EXPLANATORY MEMORANDUM TO

THE SECURITISATION (AMENDMENT) (EU EXIT) REGULATIONS 2019

2019 No. 660

1. Introduction

1.1 This explanatory memorandum has been prepared by Her Majesty's Treasury and is laid before Parliament by Act.

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

2. Purpose of the instrument

2.1 This instrument is being made to address deficiencies in retained EU law in relation to Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 ("the Securitisation Regulation") which arise from the withdrawal of the United Kingdom (UK) from the European Union (EU). This instrument also amends Regulation (EC) No 1060/2009, (EU) 648/2012, (EU) 575/2013 and (EU) 2017/2401 and Delegated Regulation (EU) 2015/61 as well as making necessary changes to relevant UK law. These changes are made to ensure that the legislation referred to above continues to operate effectively at the point at which the UK leaves the EU.

Explanations

What did any relevant EU law do before exit day?

2.2 Securitisation refers to the process of packaging and converting loans into tradable financial assets (securities), which can then be sold to investors. Through this process, banks can transfer some of the risk attached to these assets to other banks or long-term investors, freeing up capital previously set aside to cover that risk so that it can be used to generate new lending. A typical securitisation involves three key entities: an originator, securitisation special purpose entity (SSPE) and a sponsor. The originator pools income-generating assets and sells them to the SSPE, which is the main investment vehicle in a securitisation. The sponsor is a financial institution that establishes a securitisation programme by purchasing exposures from another entity (for example an original lender of a loan that becomes securitised).

2.3 Prior to the Securitisation Regulation, the EU's framework for all securitisations was relatively complex and covered by a variety of pieces of legislation. The Securitisation Regulation harmonises and reforms existing EU rules on due diligence, risk retention, disclosure and credit granting ("the general requirements") which apply in a uniform way to all securitisations, securitising entities and all types of EU regulated institutional investors.

2.4 The Securitisation Regulation defines a set of criteria for securitisations to qualify as simple, transparent and standardised (STS) securitisations. This is intended to differentiate those products from more complex and opaque products. It creates a framework for the regulation of these STS securities, and asset-backed commercial paper (ABCP) products. ABCP is a type of security that is used by companies to raise short-term financing, and is backed by assets of the company. The Securitisation

Regulation introduces preferential capital treatment for some securitisations that meet the STS standard.

Why is it being changed?

2.5 The Securitisation Regulation is directly applicable EU law. Once the UK leaves the EU the Securitisation Regulation will cease to apply in the UK, but by the operation of the European Union (Withdrawal) Act 2018 (c.16) (EUWA) the Regulation will be transferred to the UK statute book as direct retained EU law.

2.6 For the Securitisation Regulation to remain operable in the UK after the UK leaves the EU, several deficiencies need to be corrected. If these deficiencies were not addressed, then the Securitisation Regulation would not be fully operative in a UK-only context. This could lead to potential uncertainty for the UK securitisation market and risk a lack of adequate regulation of the market, potentially subjecting the financial sector to unnecessary risk.

What will it now do?

2.7 This instrument makes amendments to the Securitisation Regulation to ensure that the UK's regulation of securitisation can operate effectively at the point at which the UK leaves the EU. The amendments include:

- Changes to ensure that there is appropriate treatment of the STS classification of securitisations post-exit. When the UK leaves the EU, without certain adjustments to the geographical scope of the counterparties to securitisations, UK securitisations could no longer be classified as STS.
- Changes that enable UK counterparties to continue to participate in cross-border STS securitisations after exit by allowing some of the parties to a securitisation to be located anywhere in the world. Without this change, the market would be limited to the UK only, effectively preventing UK counterparties from participating in most securitisations. Further changes seek to avoid an immediate impact where EU STS securitisations cease to be recognised in the UK post-exit by putting in place a transitional arrangement that recognises EU STS for a limited time after exit.
- A change to the definition of 'sponsor' in the Securitisation Regulation to ensure that if a sponsor delegates day-to-day portfolio management of a securitisation, the delegated firm may be located anywhere in the world, rather than just within the UK.
- Transfer of functions of the European Supervisory Authorities to the appropriate UK bodies (the Financial Conduct Authority (FCA) or the Prudential Regulation Authority (PRA)).

2.8 Further detail on these changes can be found in Section 7 of this explanatory memorandum.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 This instrument relies on provisions made by other EU exit instruments which have not yet been made. It is therefore conditional on the making of those instruments, which are as follows:

- the proposed Financial Services and Markets Act 2000 (Amendment) (EU Exit) Regulations 2019 (to be laid in due course);
- the laid Alternative Investment Fund Managers (Amendment etc.) (EU Exit) Regulations 2019;
- the laid Collective Investment Schemes (Amendment) (EU Exit) Regulations 2019;
- the laid Financial Conglomerates and other Financial Groups (Amendment) (EU Exit) Regulations 2019;
- the laid Credit Rating Agencies (Amendment, etc.) (EU Exit) Regulations 2019; and
- the laid Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2019.

3.2 This instrument will be made once the above regulations have been made.

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)

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

3.4 The powers under which this instrument is made cover the entire United Kingdom (see section 8(1) and 23(1) and (2) of, and paragraph 21 of Schedule 7 to the EUWA 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 Securitisation (Amendment) (EU Exit) Regulations 2019 are compatible with the Convention rights."

6. Legislative Context

6.1 This instrument amends the Securitisation Regulation, as that Regulation will form part of domestic law by virtue of s.3 of the EUWA. It also amends the Credit Ratings Agencies Regulation (EC) No 1060/2009, the European Market Infrastructure Regulation (EU) No 648/2012, the Capital Requirements Regulation (EU) No 575/2013, the Capital Requirements Amending Regulation (EU) No 2017/2401, the Liquidity Commission Delegated Regulation (EU) No 2015/61, the Financial Services and Markets Act (Regulated Activities) Order 2001 (S.I. 2001/544), and the Securitisation Regulations 2018 (S.I. 2018/1288). These amendments are made to address failures of the retained EU law to operate effectively and other deficiencies arising from the withdrawal of the UK from the EU.

7. Policy background

What is being done and why?

7.1 The UK will leave the EU on 29 March 2019. The UK and EU negotiating teams have agreed the terms of an implementation period that will start on 29 March 2019 and last until 31 December 2020. Therefore, should a deal be approved, the implementation period 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 an 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 must plan for all eventualities, including a 'no deal' scenario. To prepare for this scenario, 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 (c.68) 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 EUWA (https://www.gov.uk/government/publications/financial-services-legislation-under-the-eu-withdrawal-act).

7.9 This instrument makes amendments to aspects of the Securitisation Regulation to ensure that it continues to operate effectively in the UK once the UK has left the EU. These changes include:

STS Recognition

7.10 The Securitisation Regulation creates a new framework for STS and asset-backed commercial paper (ABCP) programmes. Under the Securitisation Regulation, STS is a new designation that is given to securitisations that meet certain eligibility criteria. An STS securitisation needs to meet the general rules of the Securitisation Regulation (such as risk retention, transparency and due diligence requirements) and then meet various criteria to determine the securitisation's simplicity, standardisation and transparency. All three parties involved in the securitisation – the originator, sponsor and SSPE – must be located in the EU. If a securitisation is eligible for STS classification, it may then be granted preferential capital treatment (though this is not guaranteed).

7.11 Given the requirement for all parties in an STS securitisation to be located in the EU, if this deficiency were not fixed when the UK leaves the EU, the scope of this instrument would no longer allow UK parties to be deemed STS. Furthermore, if the scope of the regime was restricted to the UK only, it would cease to capture existing parties, while also putting the status of any existing STS securitisations into question.

7.12 STS status is aimed at reducing risks in the securitisation market as well as providing a boost to the EU's securitisation market as a whole. The UK wishes to maintain this aim in a post-exit scenario. Therefore, to address this deficiency, this SI introduces a transition period during which any securitisations added to the list kept by the European Securities and Markets Authority during a two-year period after exit will be recognised as STS in the UK for the lifetime of the securitisation.

7.13 Specifically for ABCP cross-border securitisations, the SI also ensures that these are eligible for STS recognition in the UK where the sponsor is located in the UK, even where the SSPE and/or originator are located outside the UK. For non-ABCP cross-border securitisations, these would still be eligible for UK STS recognition if the sponsor and originator are located in the UK. This will allow a higher number of potential securitisations to be eligible for STS recognition in the UK post-exit.

7.14 Together, these changes will help to ensure that UK firms are able to benefit from the EU's large market for STS securitisations. By the end of the transitional period, the government intends to have developed a more permanent solution.

The definition of 'sponsor'

7.15 Under the Securitisation Regulation, non-STS securitisations may have the sponsor located anywhere in the world. However, if the sponsor delegates day-to-day portfolio management of a securitisation, the delegated firm must be a regulated asset manager such as an undertaking for the collective investment in transferable securities (UCITS) management company, an alternative investment fund manager (AIFM), or an entity referred to in the Markets in Financial Instruments Directive (Directive 2014/65/EU). This requirement effectively means that the location of the delegated firm must be in the EU.

7.16 This restriction in the geographical location of the delegated firm is an ambiguity in the Securitisation Regulation that arises from cross-references to other EU Directives. The instrument therefore clarifies this ambiguity, as without doing so, post-exit a securitisation could only gain STS recognition in the UK if all three parties were located in the UK.

Exposures to National Promotional Banks

7.17 The Securitisation Regulation exempts exposures to National Promotional Banks located in the EU. These are entities that carry out financial, development and promotional activities with a mandate given to them by a national or regional government. One example is the German state-owned development bank KfW.

7.18 The UK will not continue to provide preferential treatment to EU27 entities post-exit but will treat them in the same way that other third country entities are treated. This instrument therefore restricts the exemption for exposures to National Promotional Banks to those within the UK (e.g. the British Business Bank).

Transfer of functions

7.19 This instrument transfers functions of EU bodies to the PRA and FCA after exit. Reporting responsibilities previously overseen by the European Securities and Markets Authority (ESMA) are transferred to the FCA or PRA, and in some cases to both regulators where this is appropriate.

7.20 The Securitisation Regulation requires originators, sponsors, and SSPEs to report information relating to their public securitisations to repositories located in the EU and authorised and registered with ESMA. ESMA will no longer have jurisdiction in the UK post-exit. The responsibility for authorisation and registration of repositories will therefore be transferred to the FCA as the most appropriate body, given their expertise, to carry out this function post-exit.

7.21 Under this instrument, the responsibility for maintaining a domestic list of securitisations that qualify as STS will be transferred from ESMA to the FCA. Similarly, responsibility for making Binding Technical Standards under this instrument will be transferred to the FCA and PRA as appropriate, in accordance with their objectives and existing functions. The FCA and PRA are also required to consult and coordinate with one another as appropriate under the existing UK financial services framework.

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

8.1 This instrument is being made using the powers in sections 8(1), 23(1) and (2) of, and paragraph 21 of Schedule 7 to, the EUWA in order to address failures of retained EU law to operate effectively or other deficiencies arising from the withdrawal of the UK from the EU. In accordance with the requirements of that 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 extensively with the Bank of England, the PRA and the FCA during the drafting process. HM Treasury has engaged with relevant stakeholders on its approach to Financial Services legislation under the European Union (Withdrawal) Act 2018, including on this instrument, in order familiarise them with the legislation ahead of laying.

10.2 This instrument was also published in draft, along with an explanatory policy note, on 20 December 2018, in order to maximise transparency ahead of laying. (https://www.gov.uk/government/publications/draft-securitisation-amendment-eu-exit-regulations-2019)

10.3 The PRA 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 (c.8). These consultations can be found at:

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

10.5 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 businesses of this instrument is limited. The STS transition period noted above is expected to provide continuity for business wherever possible, with a longer-term solution to be addressed at a later stage. There will be a cost for familiarisation with the text of the SI, however this is expected to be a one-off cost. There is no impact on charities or voluntary bodies.

12.2 In the public sector, the FCA and PRA will be responsible for carrying out functions under this instrument, as detailed above, that are currently carried out by the European Supervisory Authorities. 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, when an opinion from the Regulatory Policy Committee has been received.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses where they engage in the trade of securitisations.

13.2 This instrument addresses deficiencies in the legislation that will exist after the UK leaves the EU, and therefore aims to minimise the impact of these regulatory changes on all firms, including small businesses.

14. Monitoring & review

14.1 As this instrument is made under the EUWA, no review clause is required.

15. Contact

15.1 Luke Miller at HM Treasury Telephone: 02072704399 or email: Luke.Miller@hmtreasury.gsi.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 MP, 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 23(1) or jointly exercising powers in Schedule 2 to create a criminal offence	Set out the 'good reasons' for creating a criminal offence, and the penalty attached.
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	Paragraph 16, Schedule 8	Anybody making an SI after exit day under	Statement setting out: a) the steps which the relevant

where amending regulations under 2(2) ECA 1972		powers outside the European Union (Withdrawal) Act 2018 which modifies subordinate legislation made under s. 2(2) ECA	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 Securitisation (Amendment) (EU Exit) Regulations 2019 do no more than is appropriate".

1.2 This is the case because: the instrument only makes those changes necessary to provide a functioning statute book in relation to the continued regulation of securitisations when the UK leaves 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 the Securitisation (Amendment) (EU Exit) Regulations 2019, 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 the regulation of securitisations in the UK would become legally inoperable when the UK leaves the EU. An unregulated securitisation market would lead to uncertainty for those trading in the market and potentially pose financial risk to the UK and wider financial markets.

3. Equalities

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

"The instrument 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 instrument, 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 the relevant sub-delegated powers in Securitisation (Amendment) (EU Exit) Regulations 2019."

5.2 It is appropriate to delegate the power to make regulatory technical standards to the FCA and the PRA because this will give them the necessary powers to ensure that the technical standards under the Securitisation Regulation for which they are responsible will operate effectively after exit, subject to effective oversight by HM Treasury. The FCA and the PRA have the necessary technical expertise and resources to make technical standards in this area. They are therefore best-placed to take on these functions after the UK leaves the EU.

5.3 This is in line with the approach that the government has set out in which legislative responsibility for Level 2 technical legislation in financial services will be transferred to the financial regulators, while the Treasury will have responsibility for changes to Level 1 legislation which Parliament will approve.