

EXPLANATORY MEMORANDUM TO
THE FINANCIAL SERVICES AND MARKETS ACT 2000 (TRANSPARENCY OF
SECURITIES FINANCING TRANSACTIONS AND OF REUSE) REGULATIONS
2016

2016 No. 715

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 on a matter of interest to the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

- 2.1 These Regulations implement in part Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) 648/2012 (OJ L 337, 23.12.2015, p. 1–34), (more commonly known as the Securities Financing Transactions Regulation or “the SFTR”). These Regulations amend the Financial Services and Markets Act 2000 (c.8) (“FSMA”), the Financial Services and Markets Act 2000 (Qualifying EU Provisions) Order 2013 (S.I. 2013/419) and other secondary legislation to allow certain requirements imposed by or under the SFTR to be enforced using powers conferred by FSMA, and for related purposes. FSMA is amended to ensure that these powers are consistent with the SFTR provisions that relate to such powers. These Regulations also confer powers on the Financial Conduct Authority (“the FCA”) to enforce those requirements in respect of counterparties not regulated under FSMA and to provide powers to the FCA and the Bank of England (“the Bank”) supplementing those in FSMA where necessary. These Regulations ensure that the SFTR is fully effective and enforceable in the United Kingdom.

3. Matters of special interest to Parliament

Matters of interest to the Joint Committee on Statutory Instruments

- 3.1 These Regulations are laid on 8 July and enter into force on 13 July. HM Treasury is therefore in this instance allowing less than the minimum 21 day period applying by convention between the laying of a statutory instrument subject to the negative resolution procedure in Parliament and its coming into force. The Regulations were ready for making and laying before Parliament only very shortly before the 21 day period began. As the economy and role of financial services have been high profile topics in the debate about the UK’s membership of the European Union, following careful consideration it was deemed inappropriate to publish these Regulations during the period of purdah before the referendum. In light of HM Treasury’s legal obligation to both take the necessary measures to implement SFTR in the UK by 13 July and ensure that the Financial Conduct Authority and the Bank of England have the necessary powers to effectively supervise and enforce obligations imposed by SFTR in the UK it was not feasible to delay the coming into force date to comply with the 21

day rule. HM Treasury apologises for the inconvenience caused by reducing the time available to the Committee to consider the Regulations.

Other matters of interest to the House of Commons

- 3.2 As this instrument is subject to the negative resolution procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

4. Legislative Context

- 4.1 These Regulations implement in part the SFTR.
- 4.2 The SFTR introduces a supervisory framework within which the following requirements are imposed on counterparties to securities financing transactions and financial collateral arrangements:
- Counterparties are required to report to an authorised trade repository information on the securities financing transactions they undertake.
 - There are certain restrictions on the re-use of collateral by counterparties to financial collateral arrangements.
 - Asset managers have to report to investors and potential investors on relevant activity in financial statements.
- 4.3 The SFTR is directly applicable, and most aspects of the SFTR do not require implementation via domestic legislation.
- 4.4 The Regulations follow an approach consistent with existing enforcement regimes elsewhere in the sector. They remove conflicting provisions of domestic legislation, designate the Bank of England and the Financial Conduct Authority (FCA) as competent authorities for SFTR purposes and enact provisions to ensure that the competent authorities have all of the supervisory, investigatory and enforcement powers necessary for the exercise of their functions under the SFTR. Many of these powers are provided by amending the Financial Services and Markets Act 2000 (Qualifying EU Provisions) Order 2013 (S.I. 2013/419) to designate SFTR requirements as qualifying EU provisions for various FSMA purposes. FSMA is also amended to ensure consistency with the SFTR. The Regulations provide additional powers to the FCA and to the Bank to temporarily prohibit a person responsible for breach of an SFTR requirement from being concerned in the management of a counterparty.
- 4.5 Explanatory Memorandum 6020/14 relating to the proposal for the SFTR was sent to both EU Parliamentary scrutiny committees on 26 February 2014. It was cleared by the House of Lords on 4 November 2014. It was cleared by the House of Commons on 19 November 2014.

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, Harriett Baldwin MP, has made the following statement regarding Human Rights:

“In my view the provisions of the Financial Services and Markets Act 2000 (Transparency of Securities Financing Transactions and of Reuse) Regulations 2016 are compatible with convention rights.”

7. Policy background

- 7.1 Securities financing transactions occur when financial counterparties, such as banks or insurers, trade or loan assets in exchange for cash, often over very short timeframes. They are undertaken with the broad intention of borrowing money but without having to go to a regulated bank. This activity was found to have contributed to the scale of the financial crisis and it was agreed by the G20 and the Financial Stability Board that regulatory action was required. It was decided that the primary regulatory action should be to increase oversight and build a data set from which policy makers could determine whether any further regulatory action was required. Other recommendations included work to increase awareness among market participants about how collateral is re-used by collateral takers. This work involved significant consultation by the Financial Stability Board with industry.
- 7.2 The Government supported the development of this work at the G20 and Financial Stability Board after consulting with regulators and industry. This work was then taken forward by the European Commission who brought forward proposals on 29 January 2014. The Government’s objectives were met in the ensuing negotiations, and it supported political agreement in July 2015.
- 7.3 The SFTR came into force on 12 January 2016, and the first substantive provisions to have effect do so from 13 July 2016. These Regulations come into force on the 13 July 2016. A draft of the directly applicable regulatory technical standards to be adopted under Article 4(9) and (10) of the SFTR are expected to be submitted by the European Securities and Markets Authority to the European Commission by 13 January 2017. These will add further detail to the reporting requirements in Article 4 of the SFTR.
- 7.4 Typically, there is no need for the UK to transpose EU Regulations into domestic law as they are binding in their entirety and directly applicable in all Member States. However, the UK is obliged to ensure that its domestic law is compatible with such EU Regulations, and that such EU Regulations are enforceable within the UK.
- 7.5 As noted above, the SFTR requires competent authorities to have all the supervisory and investigatory powers necessary for the exercise of their functions. The Regulations give the FCA the power to require any information and documents it needs to exercise its functions as a competent authority in relation to non-financial counterparties. The FCA and the Bank will have such powers in relation to financial counterparties under FSMA as a result of amendments made by the Regulations.
- 7.6 The SFTR requires the UK to ensure there are effective, proportionate and dissuasive penalties in place and that certain sanctions and other administrative measures are available to the competent authorities as a minimum. The Regulations enact provisions to satisfy these requirements. The Regulations provide for regulators to be able to:
- direct or require a counterparty to cease conduct resulting in a breach of an SFTR requirement;
 - impose financial penalties;
 - publicly censure a counterparty for breach of an SFTR requirement;

- temporarily prohibit a person responsible for breach of an SFTR requirement from being concerned in the management of a counterparty.

7.7 The Regulations also introduce a criminal penalty for misleading the regulator in purported satisfaction of requirements imposed under the Regulations.

Consolidation

7.8 These Regulations make amendments to domestic legislation to implement in part the SFTR. Since the amendments are limited in scope, consolidation of the secondary legislation is not merited.

8. Consultation outcome

8.1 The SFTR is a directly applicable EU Regulation with requirements and obligations that apply without implementation in domestic law. The domestic legislative requirement is therefore to ensure that existing domestic legislation is consistent with the SFTR. No formal consultation was necessary as the changes to domestic legislation required are minor, and the enforcement approach taken is in line with existing enforcement regimes elsewhere in the sector.

8.2 HM Treasury has consulted the FCA and the Bank of England extensively in the preparation of this instrument. They are content that the approach adopted will enable them to meet their obligations under the SFTR and supervise counterparties effectively.

8.3 In addition HM Treasury conducted regular informal consultation with industry stakeholders, banks and relevant sectoral trade groups. These informal consultees supported the approach adopted.

9. Guidance

9.1 HM Treasury does not propose to produce any guidance in relation to these Regulations. ESMA and the UK's competent authorities have the power to issue guidance in relation to the SFTR and these Regulations.

10. Impact

10.1 The financial impact on UK businesses of the changes contained within this instrument will be negligible, in terms of regulatory impact.

10.2 The impact on charities and voluntary bodies is negligible.

10.3 The impact on the public sector is negligible.

10.4 An Impact Assessment was not conducted as the Regulation is mechanical in its amendment to the supervisory framework, and does not itself significantly impact individuals or businesses.

11. Regulating small business

11.1 The legislation applies to activities that are undertaken by small businesses.

11.2 There is no provision to minimise the impact of the requirements on small firms employing up to 50 people. The SFTR does not provide any basis for excluding small or micro businesses from regulation. It is also undesirable to exempt smaller firms from the SFTR as this would hinder its effectiveness, and run the risk of regulatory arbitrage based on firm size.

- 11.3 There was informal consultation throughout negotiations with market participants on the European Commission's proposals for the SFTR, including a number of round table meetings, as well as the European Commission's public consultation which informed the SFTR proposals. There was no formal consultation and the Treasury did not formally consult with small firms on possible exemptions for small businesses; such an exemption would not be possible due to the direct applicability of the SFTR.

12. Monitoring & review

- 12.1 HM Treasury is required to review the operation and effect of Parts 2 and 3 of the Regulations within a five year period after the Regulations come into force and within every five years after that. This instrument does not contain a requirement to conduct a separate review into the regulatory provisions it amends. The Economic Secretary to the Treasury, Harriett Baldwin MP, has made the following statement: "In my view, and having had regard to "Small Business, Enterprise and Employment Act 2015 – Statutory Guidance for Departments", it is not appropriate to make provision requiring the review of the regulatory provisions amended by the Financial Services and Markets Act 2000 (Transparency of Securities Financing Transactions and of Reuse) Regulations 2016. Such a provision would be disproportionate taking into account the economic impact of those provisions."
- 12.2 Under Article 29 of the SFTR, the Commission is required to review and prepare a general report on the efficacy of the SFTR and submit that report together with any appropriate proposals to the European Parliament and Council reflecting on international regulatory developments by 31 October 2017.

13. Contact

- 13.1 Thomas Kenny at HM Treasury (Telephone: 02072702833 or email: tom.kenny@hmtreasury.gsi.gov.uk) can answer any queries regarding the instrument.