EXPLANATORY MEMORANDUM TO

THE CAPITAL REQUIREMENTS REGULATION (AMENDMENT) REGULATIONS 2021

2021 No. 1078

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 The Financial Services Act 2021 (FS Act) empowers HM Treasury to revoke provisions in the Capital Requirements Regulation[1] (CRR)[2], in order to allow the Prudential Regulation Authority (PRA) to introduce updated prudential rules for credit institutions and PRA-designated investment firms.

2.2 The primary purpose of this instrument is, therefore, the exercise of the fore-mentioned revocations power, contained in section 3(1) of the FS Act.

2.3 This instrument also contains additional EU Exit-related amendments to the CRR which are required to ensure that these pieces of legislation continue to operate effectively now the UK has left the EU.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 In accordance with the requirement in section 3(4) of the FS Act, HM Treasury has considered the PRA's near final-rules, which will be made once this instrument is made[3], in accordance with Part 9D of the Financial Services and Markets Act 2000 (FSMA)[4] and are satisfied that the revoked provisions of the CRR will be adequately replaced by PRA rules or it is appropriate for the provision not to be replaced.

3.2 A number of provisions to be revoked do not need to be replaced by PRA rules. The reasons for this include the following:

- the PRA is able to use other powers, such as its ability to waive or modify its rules or impose individual requirements, to achieve a similar effect;
- the provisions are not needed in relation to the revised requirements in PRA rules;

[1] REGULATION (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012

[2] Hereafter any reference to CRR, unless stated otherwise, refers to the Capital Requirements Regulation EU retained law version.

[3] The PRA has not made the rule instruments at this stage because HM Treasury must first revoke the parts of the onshored CRR, as provided for in the FS Act, before the PRA can replace them in PRA rules.

[4] Inserted by Part 1 of Schedule 3 to the FS Act.

- the provisions do not currently impose requirements on firms, as they are subject to delayed commencement in the CRR;
- the provisions relate to powers for the PRA to make technical standards or HM Treasury to make regulations in relation to matters where responsibility is being transferred to the PRA; or
- the provisions are time limited and are no longer needed at the point of the introduction of PRA rules.

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 includes Scotland and Northern Ireland.

3.4 The powers under which this instrument is made cover the entire United Kingdom and the territorial application of this instrument is not limited by either the Act or by the instrument.

4. Extent and Territorial Application

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

4.2 The territorial application of this instrument is 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 Capital Requirements Regulation (Amendment) Regulations 2021 are compatible with the Convention rights."

6. Legislative Context

6.1 The UK, as a member of the G20, is committed to the implementation of the Basel standards on banking. Now that the UK has left the EU, the UK needs to implement those standards which do not currently form part of domestic requirements – including those standards contained in the EU's 2nd Capital Requirements Regulation (CRR2)[5]– domestically.

6.2 The FS Act enables HM Treasury to transfer responsibility for implementing the Basel standards to the PRA, by providing a power for HM Treasury to revoke relevant provisions within the CRR, thereby allowing the PRA to make rules in those areas. The FS Act does this within the existing regulatory framework for regulator rules provided by the FSMA alongside a new accountability framework to provide appropriate democratic oversight from Government and Parliament.

6.3 The instrument exercises the powers contained in section 3 of the FS Act to revoke provisions of the CRR and make consequential amendments. The instrument also exercises powers in the European Union (Withdrawal) Act 2018 to fix deficiencies which have arisen out the UK's exit from the EU.

[5] REGULATION (EU) 2019/876 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements, and Regulation (EU) No 648/2012

7. Policy background

What is being done and why?

7.1 The global financial crisis of 2007-09 demonstrated the importance of the stability of the banking sector. During the crisis UK banks made large losses and this had an adverse impact on the real economy and resulted in a fall in lending and large bailouts using taxpayer's money.

7.2 In response to the financial crisis, the Basel Committee on Banking Supervision (BCBS) agreed the Third Basel Accord, beginning in late 2010. These standards sought to strengthen the existing framework, notably by improving the quality and quantity of financial resources banks are required to maintain and expanding requirements to ensure a wider set of risks that banks are exposed to are covered. The BCBS also agreed some entirely new prudential measures, including macroprudential capital buffers, additional capital buffers for global systemically important banks, a minimum leverage ratio, and liquidity requirements, to help ensure banks are able to meet both short-term and long-term financial obligations.

7.3 The UK played an active role in negotiating and agreeing Basel 3, and is committed to its full, timely and consistent implementation.

7.4 Prior to the end of the implementation period, the UK had implemented the majority of the earlier Basel Standards through EU law. The most recent EU implementing legislation was CRR2 and the 5th Capital Requirements Directive (CRDV)[6]. Some aspects of CRR2, however, came into application following Implementation Period Completion Day (IPCD) and therefore do not form part of EU retained law.

7.5 The UK is committed to provide for the implementation of the outstanding Basel 3 standards contained in CRR2.

7.6 Accordingly, HM Treasury is, through this instrument, revoking certain provisions of the CRR. The PRA will then replace relevant provisions with rules, taking into account the updated Basel standards. The PRA will make these rules once this instrument is made, in accordance with provision in section 144A FSMA.

7.7 Following IPCD, overseas Central Counterparties (CCPs) are required to be recognised by the Bank of England as set out in Article 25 of the European Market Infrastructure Regulation[7] (EMIR)[8] in order to provide clearing services to UK firms under the clearing obligation as set out in EMIR.

7.8 Recognised CCPs are automatically granted Qualifying CCP status (QCCP) status. Such status also allows UK clearing members to use that CCP without being subject to stricter capital requirements under the CRR.

7.9 There are three ways to be granted QCCP status:

[6] The UK implemented CRDV, per its obligation to implement EU directives during the implementation period, through the Financial Holding Companies (Approval etc.) and Capital Requirements (Capital Buffers and Macro-prudential Measures) (Amendment) (EU Exit) Regulations 2020 and PRA rules.

[7] Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories

[8] Hereafter any reference to EMIR, unless stated otherwise, refers to the European Market Infrastructure Regulation EU retained law version.

- Through recognition from the Bank of England under Article 25 of EMIR. This relies on HM Treasury making an EMIR Article 25 equivalence decision for the relevant jurisdiction;
- overseas CCPs who have not yet received recognition but were recognised under the EU regime and qualified for the UK's Temporary Recognition Regime (TRR) (and are therefore treated as if recognised under Art 25 EMIR); and
- for firms outside of the TRR, there is a separate transitional regime within Article 497 CRR that allows CCPs, who submitted applications for recognition ahead of IPCD to be treated as if it were a QCCP for 2 years whilst applications under Article 25 EMIR are being considered. For overseas CCPs that made a recognition application under Article 25 EMIR before IPCD they can be treated as QCCPs until the end of 2022. This is to ensure there is continuity for UK firms with exposures to these CCPs while both jurisdictional equivalence and CCP recognition are being determined. HM Treasury can extend the two year transitional period (via SI) for one year only. Only a limited number of CCPs are within this transitional regime.

7.10 This instrument amends Article 497 CRR to provide HM Treasury with the ability to extend the transitional period (the third method above) indefinitely (one year at a time).

7.11 This is needed because there are some CCPs, who submitted applications for recognition ahead of IPCD, that will likely be unable to receive equivalence and recognition under EMIR for a prolonged period following their application but who HM Treasury considers it beneficial that they retain QCCP status. The affected CCPs can clear specific products that other CCPs will not and it is preferable for UK firms to continue clearing those products in those CCPs rather than not clearing them at all. Losing QCCP status would make it prohibitively expensive for UK firms to continue using those services.

7.12 HM Treasury will keep these arrangements under review going forward to ensure they are fit for purpose, whilst a permanent solution is considered.

7.13 Under Article 391 of the CRR, HM Treasury may by regulations determine that an overseas jurisdiction applies prudential and regulatory requirements at least equivalent to those applied in the UK. The effect of these Regulations is that the Large Exposures limits in Article 395(1) of the CRR that apply to exposures to institutions authorised in such an overseas jurisdiction are the same as the limits that apply to exposures to institutions in the UK.

7.14 The UK's only equivalence determination in this area is with respect to European Economic Area States. Prior to IPCD the European Banking Authority had issued guidance which allowed institutions authorised in countries found equivalent under other articles in the CRR to be treated as equivalent for the purposes of Article 391.

7.15 To continue this effect post-IPCD, HM Treasury would need to carry out a large number of assessments (with support from the PRA under the terms of the equivalence MOU) and make corresponding equivalence determinations under Article 391 of the CRR. Completing these assessments quickly will not be possible, therefore, in these Regulations, HM Treasury is putting in place transitional arrangements to maintain the effect of the pre-existing treatment that was allowed under the EU arrangements.

7.16 In parallel, given that the equivalence assessment carried out under Article 391 of the CRR is identical to that under Article 107 of the CRR, HM Treasury will seek a legislative opportunity to streamline the system by providing that an existing equivalence decision made for the purposes of Article 107 will also apply for the purposes of Article 391, removing the need to make further equivalence decisions under Article 391 where an Article 107 decision has already been made.

7.17 The transitional arrangement will end in relation to an overseas jurisdiction either:

- when an equivalence determination is made by HM Treasury under Article 391 of the CRR in relation to that overseas jurisdiction; or
- when the transitional arrangement becomes ineffective because Article 391 of the CRR has been amended.

7.18 The intended effect of this approach is to provide continuity for firms on the scope and definition of an institution for Large Exposures purposes.

Explanations relating to EU Exit amendments

What did any law do before the changes to be made by this instrument?

7.19 The Capital Requirements Regulation was extensively amended for EU exit by the Capital Requirements Regulation (Amendment) EU Exit) Regulations 2018 and 2019[9], and further changes were made in other EU Exit instruments. Following IPCD there are a few further aspects of the CRR that fail to operate effectively and contain other deficiencies as a result of the withdrawal of the United Kingdom from the EU. Therefore, in addition to the provisions discussed above this instrument makes certain small deficiency fixes changes under section 8 of the European Union (Withdrawal) Act 2018.

Why is it being changed?

7.20 To correct references to EU institutions and other deficiencies arising from EU Exit. These should not be considered policy changes.

What will it now do?

7.21 The references will now refer to UK institutions and legislation.

8. European Union Withdrawal and Future Relationship

8.1 Some elements of this instrument are being made using the powers in section 8 of, and paragraph 21 of Schedule 7 to, 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.

8.2 In accordance with the requirements of the European Union (Withdrawal) Act 2018 the Minister has made the relevant statements as detailed in Part 2 of the Annex to this Explanatory Memorandum.

8.3 Alongside the European Union (Withdrawal) Act 2018 powers the instrument is also being made under FS Act section 3 powers.

[9] SI 2018/1401 and SI 2019/1323.

9. Consolidation

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

10. Consultation outcome

10.1 HM Treasury ran a public consultation on the implementation of certain aspects of Basel 3 and the Investment Firms Prudential Regime (IFPR) which closed on 01/04/2021. This consultation included HM Treasury's proposed approach to the exercise of the revocations power in section 3 of the FS Act. HM Treasury received no substantive comments on the proposed exercise of this revocations power.

10.2 A more detailed analysis of the consultation outcome and the Treasury's policy response to the opinions expressed can be found at https://www.gov.uk/government/consultations/implementation-of-the-investment-firms-prudential-regime-and-basel-3-standards-consultation

11. Guidance

11.1 HM Treasury does not propose to issue guidance on the content of these Regulations.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 An Impact Assessment has not been prepared for this instrument because in line with Better Regulation guidance, HM Treasury considers that the net impact on businesses will be less than £5 million a year. Due to this limited impact, a de-minimis impact assessment has been carried out and is published alongside this instrument.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses, if they currently fall within the scope of the CRR.

13.2 However, the number of small businesses (banks) that fall within scope are minimal and HM Treasury does not consider there is a further need to minimise the impact of the requirements on small businesses.

14. Monitoring & review

14.1 The instrument does not include a statutory review clause and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015 the Economics Secretary to the Treasury (John Glen MP) has made the following statement:

"It is not proportionate to include a review clause in this instrument because the number of small businesses in scope is very low; the provisions revoked are to be replaced by PRA rules or do not need to be replaced and therefore amendments to the scope of the revocations contained in this instrument may lead to a situation where legislation and PRA rules contradict each other on the same prudential matters. Furthermore, these Regulations are allowing for the implementation of the Basel 3 standards, so a review that required changes to this legislation could leave the UK in breach of its international commitments."

15. Contact

15.1 Jamie Loxton at HM Treasury email: jamie.loxton@hmtreasury.gov.uk can be contacted with any queries regarding the instrument.

15.2 Fayyaz Muneer, Deputy Director for Green and Prudential, 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 and the European Union (Future Relationship) Act 2020

Part 1A

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) or 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) or 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) or 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) or 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) or 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 IP completion 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) or	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 section 8 or 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 5 or 19, Schedule 7.	Statement of the reasons for the Minister's opinion that the SI is urgent.
Scrutiny statement where amending regulations under 2(2) ECA 1972	Paragraph 14, Schedule 8	Anybody making an SI after IP completion day under powers conferred before the start of the 2017-19 session of Parliament 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.
Explanations where amending regulations under 2(2) ECA 1972	Paragraph 15, Schedule 8	Anybody making an SI after IP completion 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 IP completion day, and explaining the instrument's effect on retained EU law.

Part 1B

Table of Statements under the 2020 Act

This table sets out the statements that may be required under the 2020 Act.

Statement	Where the requirement sits	To whom it applies	What it requires
Sifting	Paragraph 8 Schedule 5	Ministers of the Crown exercising section 31 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

Part 2

Statements required under the European Union (Withdrawal) 2018 Act or the European Union (Future Relationship) Act 2020

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 Capital Requirements Regulation (Amendment) Regulations 2021 does no more than is appropriate".

1.2 This is the case because of the reasons set out in section 7.

2. Good reasons

2.1 The Economics 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 the reasons set out in section 7.

3. Equalities

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

"The draft 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 draft instrument, I, John Glen 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 7 of the main body of this explanatory memorandum.