Title: Reforms to the Investment Bank Special Administration Regime **IA No: RPC-HMT-3268(2)** **RPC Reference No:** **RPC-HMT-3268(2)** **Lead department or agency:** HM Treasury **Other departments or agencies:**	**Impact Assessment (IA)** **Date: 09062016** **Stage: Final** **Source of intervention: Domestic** **Type of measure: Secondary legislation** **Contact for enquiries: Katie Kochmann** **Tel: 0207 270 6039 Email: katie.kochmann@hmtreasury.gsi.gov.uk**

Summary: Intervention and Options

RPC Opinion: Green

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANDCB oIneen 2014 prices)	**In scope for One-in, Three-out (OI3O)?**	**Business Impact Target status**
£41.38m	£41.38m	-£4.73m	No	Non qualifying provision

What is the problem under consideration? Why is government intervention necessary?

The Investment Bank Special Administration Regulations (SAR) were introduced in 2011, when it became clear that normal insolvency legislation was not suitable for managing the failure of complex investment firms (such as Lehman Brothers). Under the Banking Act 2009, the SAR was required to be reviewed independently two years after coming into force. Peter Bloxham was appointed to evaluate the regime and his review of January 2014 identified areas of inefficiency and legislative gaps which the current SAR does not address. For example, the current SAR does not empower administrators to set a bar date for client money, only for client assets. This delays the return of client money as administrators need to go to court for directions.

What are the policy objectives and the intended effects?

The policy objective is to improve the functioning of the SAR by implementing the recommendations of the Bloxham review ('the review') and learning lessons from insolvency procedures that have taken place under the SAR since inception. These amendments will simplify and speed up the SAR process to reduce costs for both clients and creditors; provide legal certainty about the status of claims; and reduce the market impact of firm failures. This will lead to better outcomes for clients, creditors, and counterparties and a more efficient administration process.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Option 1 is to implement the recommendations of the review addressing the identified inefficiencies and legislative gaps. This option will benefit all those impacted by the failure of an investment firm by speeding up and reducing the cost of the administration process for clients, creditors and counterparties.

Option 2 is to do nothing and not implement the recommendations of the review. This option would result in future administration cases under the SAR taking longer than is necessary as administrators will need to go to court frequently for directions on matters not covered by the SAR. This ultimately increases the cost of an investment firm failure on clients, creditors and counterparties.

Will the policy be reviewed? It **will** be reviewed. **If applicable, set review date: January 2019**

Does implementation go beyond minimum EU requirements?		N/A		
What sizes of organisation are affected?	**Micro** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)		**Traded:** None	**Non-traded:** None	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options. Signed by the responsible: MINISTER		Date:	10.01.17

Summary: Analysis & Evidence

Policy Option 1

Description:

FULL ECONOMIC ASSESSMENT

Price Base Year 2014	PV Base Year 2016	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: 16.6	High: 66.2	Best Estimate: 41.4

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	0		0	**0**
High	0		0	**0**
Best Estimate	0		0	**0**

Description and scale of key monetised costs by 'main affected groups'

The costs of the SAR reforms are zero and no costs were indentified through the consultation process on the proposed amendments. When the original SAR was introduced in 2011, it was found to create no additional costs to firms. In developing these proposed reforms to the SAR, the Treasury has consulted and asked respondents to comment on costs and benefits of the changes. Respondents agree that the proposed reforms will make it a simpler, more efficient and less costly regime, which will provide greater legal certainty on how client and creditor claims under the SAR should be managed by administrators. Given that these are streamlining changes to zero cost regine, which stakeholders expect to create zero costs and some benefits, we expect the costs of SAR reforms to be zero.

Other key non-monetised costs by 'main affected groups'

None identified.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	0		1.9	**16.6**
High	0		7.7	**66.2**
Best Estimate	0		4.8	**41.4**

Description and scale of key monetised benefits by 'main affected groups'

Based on discussions with affected groups HM Treasury estimates that the SAR amendments should reduce costs of administration by an estimated 5-20%. Based on analysis of current SAR administration cases, in the case of a large firm failure the proposed amended SAR would represent a total saving for clients and creditors of £5m-20m. While for a smaller SAR administration case the cost savings would range between £240k-£970k.

Other key non-monetised benefits by 'main affected groups'

The amendments improve the efficiency of the SAR by shortening the administration process of a failed firm, therefore lowering costs for clients, creditors and counterparties. Clients benefit from improvements to the SAR, to the extent that this enables their assets to be returned more quickly and therefore reduces the market impact of firm failure. Consultation respondents believe the proposed amendments will lead to a clearer, faster process which will also benefit creditors of the failed firm.

Key assumptions/sensitivities/risks — **Discount rate (%)** 3.5%

The key assumption is that the amendments being proposed will provide all affected parties with more legal clarity to resolve the complex legal issues which can arise when investment firms fail. This should reduce the need for administrators to go to court for direction which is a time-consumning and expensive process.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			
Costs: 0	Benefits: 4.7	Net: 4.7	Score for Business Impact Target £N/A(qualifying regulatory provisions only)

Evidence Base (for summary sheets)

Special administration regime for investment firms

Policy Objective

1. The policy objective is to minimise the market impact of an investment firm failure on creditors, facilitate faster client access to monies and assets, and improve the integration of the FCA's client asset rules (CASS), the SAR and existing insolvency rules.

2. Investment firms are a core aspect of financial markets and, among other things, play a critical role in providing market liquidity. The failure of an investment firm carries the risk of imposing substantial strain on financial stability. The Bloxham Review ('the review'), in addition to the experience provided by subsequent insolvency procedures, has highlighted several areas for improvement in the SAR to address the identified market failures. The option to do nothing has been considered; however, leaving the SAR unchanged would result in higher costs for clients, creditors and counterparties than are necessary to manage the failure of an investment firm.

3. The reforms are being made to reduce the systemic impact of firm failures; as observed during the financial crisis, the disorderly failure of a large investment firm has financial stability implications – market participants can quickly lose confidence, causing widespread disruption throughout the financial system. The proposed reforms to the SAR makes the management of an investment firm failure less disorderly and more effective, helping to reduce financial systemic risks and restore market confidence. The reforms are therefore a non-qualifying regulatory provision and out of the scope of one-in-three-out: as set out in the Better Regulation Framework manual[1], measures which deal with issues falling under the definition of financial systemic risk are out of scope for the one-in-three-out rule.

Problem under consideration

4. The legislation implementing the SAR required the SAR to be independently reviewed within two years to ensure that any lessons learnt from subsequent administrations were taken into account.

5. Mr Peter Bloxham (Freshfields 1983-2006) was appointed to evaluate the regime, and his review of January 2014 recommends 72 reforms[2]. HM Treasury (HMT) has reviewed the legal and policy implications of the recommendations in detail, and consulted in March 2016 on the proposals which are within its remit to implement. The review is broad in scope, and contains cross-departmental recommendations which span several areas of responsibility. Other stakeholders currently considering their responsibilities following the review are: the Financial Conduct Authority (FCA), the Financial Services Compensation Scheme (FSCS), the Bank of England (BoE) and the Insolvency Service.

6. At the time of close of the last public consultation (April 2016) 12 firms that have failed and entered the SAR. The lessons learnt from a number of these were considered for the purposes of the review and the proposed amendments. Some of the current cases include:
   - MF Global - KPMG are the special administrators. https://home.kpmg.com/uk/en/home/insights/2011/11/mfglobaluk.html

[1] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/468831/bis-13-1038-Better-regulation-framework-manual.pdf

[2] https://www.gov.uk/government/publications/review-of-the-special-administration-regime-sar-for-investment-banks-final-report

- Pritchard Stockbrokers Ltd - Mazars are the special administrators. http://www.mazars.co.uk/Home/Our-Services/Financial-Advisory-Services/Restructuring-services/Pritchard-Stockbrokers-Ltd
- City Equities Limited - Hacker and Young are the special administrators. http://www.uhy-uk.com/services/turnaround-recovery/special-administration/city-equities/
- Worldspreads Limited - KPMG are the special administrators. https://home.kpmg.com/uk/en/home/insights/2015/04/worldspreads-special-administration.html
- Fyshe - Harrisons are the special administrators. http://www.harrisons.uk.com/fyshe-horton-finney-limited-special-administration-latest-update
- Hartmann Capital - Hacker and Young are the special administrators. http://www.uhy-uk.com/news-events/news/hartmann-capital-put-special-administration-uhy-hacker-young-appointed-special-administrators/
- Hume Capital Securities plc - Leonard Curtis are the special administrators. http://www.leonardcurtis.co.uk/index.php/news/31/15/Special-Administrators-appointed-to-Hume-Capital-Securities-plc
- Alpari (UK) Limited - KPMG are the special administrators. https://www.insolvency-kpmg.co.uk/case+kpmg+AF119D1101.html

Engagement with industry

7. The SAR reforms, made in response to the review, are the result of extensive engagement and consultation with industry. The review was the product of Bloxham working closely with the authorities and administrators and lawyers with direct experience of SAR administrations.
8. The Treasury worked closely with the financial authorities in designing the reforms and tested them with industry throughout the policy design process to ensure that they provide affected parties (e.g. firms, clients, creditors, administrators, and counterparties) with additional legal clarity.
9. The Treasury established the Banking Liaison Panel (BLP), in accordance with section 10 of the Banking Act 2009 ("the Act"), to advise the Treasury on legislation made under the Act, such as the SAR. The Panel is made up of representatives from the financial authorities, industry bodies (representing the interests of investment firms which may be eligible for entry into the SAR, and firms which may be clients, creditors or counterparties of such firms), lawyers with expertise in the UK financial system, and other relevant bodies[3].
10. The BLP discussed the SAR reforms on 5 occasions, including detailed discussions of the Information Sharing and Cooperation duties (18 September 2015) and the Bar Date Mechanism and Transfer proposals (19 January 2016). Panel members made suggestions for improving policy positions and providing additional legal clarity for parties involved in a SAR.
11. A subgroup of the BLP was established in March 2016 to consider closely the transfers proposals and the legal effect on set off and netting arrangements. The subgroup identified a set of issues the Treasury should give regard to when finalising the transfer proposals and these have been reflected in the reforms. The changes ensure that the proposals will operate effectively and provide legal clarity for the status of set off and netting arrangements in transfers of a failed firm's business – this will benefit all parties of an administration.
12. The reforms were discussed bilaterally with industry; including with administrators who have experience of the SAR, and with industry bodies representing i) firms which are eligible for

[3] A full list of the BLP's members can be found in the minutes of the Panel's meetings, which can be found on the website: https://www.gov.uk/government/publications/banking-liaison-panel

entry into the SAR, ii) firms which may be the clients, creditors, or counterparties of such firms, and iii) firms which may purchase the business of a failed investment firm.

13. The FCA hosted a series of roundtables with representatives from industry, including lawyers and administrators with experience of the SAR and individuals representing investment firms and trade associations, and other financial authorities (including the Treasury) to discuss their complementary changes to the client money distribution rules (CASS 7A) – which is part of the wider regulatory and insolvency regime for investment firms. As part of these roundtables we gathered views on the interrelationship between CASS and the SAR.

14. The Treasury published a consultation document in March 2016 setting out the proposed SAR reforms. The consultation included 6 questions specifically asking for feedback on costs and benefits of the reforms. Consultation respondents did not identify any costs to businesses as a result of the reforms. In particular one respondent, an administrator, noted that investment firms do not 'focus on the regime and rules that would apply following their insolvency, and instead focus on the rules that apply as a going concern'. The same respondent also noted that any familiarisation costs would be accommodated within 'ongoing learning and development programme[s]'. Across the consultation responses, respondents did not identify any costs as a consequence of the reforms but noted the benefit of 'streamlining the process'. This assessment of costs and benefits was confirmed in our bilateral discussions with stakeholders throughout the consultation process.

Summary of costs/benefits

15. There are not considered to be any costs associated with amending the SAR in line with the review's recommendations. The changes are all designed to improve the efficiency of the current regime, addressing market failures by providing legal certainty for administrators in areas which are not currently covered by the existing SAR. This will ultimately shorten the administration process of a failed firm and lower costs for clients, creditors and counterparties. The proposals impose no additional administrative or other burden on firms or individuals. The original SAR (brought into effect in 2011) was found to have zero costs to firms. Stakeholders agree that these reforms will result in a regime that is simpler, more effective and with lower administration costs. Therefore, our position is that the reforms will not entail any costs for businesses.

16. Of the c.1,000 investment firms eligible for entry into the SAR, their clients, creditors and counterparties can be individuals and businesses. For example, some investment firms (such as those offering ISAs) count retail investors as their main clients while the client base of others will be mostly large businesses and financial institutions. The actual industry wide split between retail and institutional clients is uncertain. Collecting data on the split between individuals and businesses would be disproportionately costly as it would entail asking individual firms how their business is split between retail and institutional clients. Similarly, it would be disproportionately costly to collect the data for the breakdown of creditors and counterparties between retail and institutional parties.

17. There are 2 proposals which affect the scope of the SAR but these do not incur costs for industry: i) bringing back into scope of the SAR firms which have fallen out, and ii) applying the bar date mechanism to a type of client asset not currently provided for. Making amendments to ensure firms that have fallen out of scope of the SAR for technical reasons are brought back in will not incur costs for those firms: the SAR does not concern them on a going-concern basis and therefore insolvency laws are not a burden for them. Applying the bar date mechanism to client money removes the need for administrators to have to go to court on an ad-hoc basis and ask the court to give them the same ability to set bar dates for client money claims that the SAR gives them for client asset claims. This proposal will save both administrator and court time and will speed up the return of client money to clients.

18. There has been no contention of these assumptions, particularly as insolvency practitioners have had several years to acclimatise to the SAR, and the proposed reforms have been extensively consulted upon.

19. This impact assessment now assesses the respective costs and benefits of each of HMT's priority areas for reform as proposed by the review, including:
    a. improving the bar date mechanism;
    b. removing statutory interest on clients' claims on the general estate;
    c. facilitating the transfer of client positions to alternative financial institutions; and
    d. providing guidance on the allocation of costs in the SAR.

20. This impact assessment also sets out all of the other more minor and technical proposals being consulted on and provides justification on why they will not incur any costs.

21. To estimate the benefits of the SAR, an assessment has been made of the potential cost savings that the amendments will bring by shortening the administration process. These cost savings will be passed onto clients and creditors of a failed investment firm as they ultimately bear the cost of the administration process.

22. 11 investment firms have entered the SAR since it came into force in 2011. Of these SAR cases, 10 have been in administration for sufficient time to be useful as a sample for providing data. The eleventh SAR case only entered the SAR in February 2016 and there is not sufficient data on administrative expenses incurred to-date to include it in the sample.

23. Under the expectation that the financial regulatory reforms and changes to the UK's approach to prudential regulation positively impacts the insolvency rate, it is assumed that 10 investment firms will enter the amended SAR over the next decade (the appraisal period). This is a conservative assumption. It is also assumed that the sample is representative of the size of the firms that will enter administration over the appraisal period.

24. To estimate the total benefits of the amendments, the monetary benefit for each future SAR (based on data from current SARs) has been calculated on a case-by-case basis before aggregating the results.

25. **Step 1**: Calculate the total administration and legal fees (the two types of fees that the SAR reforms are likely to reduce) charged for the administration of a SAR case to-date. To note, these legal fees primarily relate to instances where administrators have had to go to court for direction because the existing SAR does not provide for certain issues, such as a client money bar date mechanism.

    Step 2: Apply an annualised 5-20% estimated cost savings under the SAR reforms. This cost saving range accounts for and captures some of the assumptions used in the estimate of EANDCB which contain uncertainty. The range accounts for the reduction in the administrators' expenses and legal fees incurred in winding up the failed firm under the SAR reforms. The range also captures the uncertainty of the split between individuals and businesses within clients, credits and counterparties as set out in paragraph 16. Administrations involving a large proportion of businesses would save closer to 20% of costs counted towards the EANCB while administrations with largely individual parties would save costs nearer to the lower bound of 5%. The FCA have said that all investment firms would have at least one creditor or counterparty that is a business. The cost saving range is based on discussions with insolvency practitioners who have experience of working with the current SAR regime. Feedback from administrators during bilateral discussions during the

consultation and policy development period is that they agree that this figure is a sensible, if not conservative, estimate of the potential cost savings from the SAR reforms.

26. The resulting range is the expected yearly cost savings in every year of the appraisal period for the future administration of an investment firm of a similar or equal size. Aggregated across all SAR cases for an industry-wide benefit gives an estimated range for the policy reforms.

27. For example, in their latest administrator's progress report, KPMG had charged £103,895,247 in fees for the administration of MF Global UK under the SAR over 4.6 years. This represents an average annual cost of £22,734,871. By applying the 5-20% estimated cost savings, the proposed SAR amendments would represent a saving of £1,136,744-£4,546,974 per year compared to the baseline scenario of the current SAR. It is assumed that one investment firm the size of MF Global UK fails in the appraisal period. This implies the proposed SAR amendments would represent an average savings range of £1,136,744-£4,546,974 per year in this case.

28. The same assumptions and calculations applied to UHY Hacker Young's administration of City Equities Ltd, costing £362,810 in administrator fees as of the last progress report, find an average costs savings range of £6,919-£27,675 per year over the appraisal period for this case.

29. The total range of benefits per administration case is different depending on the size and complexity of the administration case. Aggregating the sample range of benefits from the existing SAR cases, an equal or similar set of insolvencies over the next ten-year appraisal period would yield an estimated benefits range of £1,922,913-£7,691,651 per year for the industry from the SAR amendments.

30. A higher cost saving within the assumed range of 5-20% could potentially be achieved in cases where the business of the investment firm is mostly in respect of client assets and client money. This is because the SAR amendments are specifically designed to help speed up the return of client assets and money.

31. An example of a SAR case mostly involving client money and asset issues can be seen from Mazars's administration of Pritchard Stockbrokers Ltd. In their last progress report, Mazars charged £6,087,206 in total for the administration. Assuming the proposed changes to the SAR reduce total administration costs by 5-20%, this represents an annual range of potential benefits of £70,624-£282,496. Since 86% of the administrator's fee relates to the cost of client issues, the proposed SAR amendments could have a proportionally greater impact on similar cases.

32. Consultation respondents noted that the streamlining of the process to distribute client assets is motive enough for implementing the necessary changes. Overall, the respondents considered that the reforms will give more certainty to administrators, creditors, counterparties and clients.

33. In terms of the associated additional costs, these are considered to be zero as outlined in more detail below.

34. Administrators believe that the additional costs of familiarising themselves with the new regime will be negligible. This is because, in the majority of cases, the amendments are providing legal certainty in areas where previously they had to go to court for direction. This means that they are already familiar with the issues being addressed and, given the extensive public consultation, they are also familiar with the amendments and what they are

seeking to achieve. Potential familiarisation costs have been discussed with some insolvency practitioners, but they consider them very negligible. Administrators stated in the consultation responses that "we do not consider [costs] will be material as this can be accommodated within our ongoing learning and development programme".

35. In terms of costs for clients or creditors of investment firms, respondents note that clients, creditors and counterparties are not likely to incur costs familiarising themselves with the regime until an insolvency that affects them actually occurs. However, these are the same costs that these parties would be expected to occur under the current SAR if a firm failed now. The SAR therefore does not place any additional administration or other burden on parties.

36. The rest of this IA explains the main reforms to the SAR and provides an assessment of the associated costs and benefits.

Improving the bar date mechanism

37. The SAR established a 'bar date' mechanism whereby administrators were empowered to set a deadline for clients to submit claims for the return of their assets. The bar date mechanism was designed to facilitate distributions of client assets so that administrators are able to return client assets in a timely manner. Importantly, the bar date allows administrators to accurately determine if there are any shortfalls between the client assets they have in their possession and client claims and get court approval on how to manage the shortfalls.

38. The review notes the bar date mechanism as currently designed is deficient in a number of respects. To address the current deficiencies in the bar date process the following amendments are being proposed.

Bar date proposals	**Assessment of costs and benefits**
Apply the bar date mechanism to client money	This amendment removes the need for the administrators to have to go to court on an ad-hoc basis and ask the court to give them the same ability to set bar dates for client money claims that the SAR gives them for client asset claims. This proposal will save both administrator and court time and will speed up the return of client money to clients. It is difficult to quantify the benefit of this saving as public information is not provided on how much time administrators spent on these court proceedings. However, the independent reviewer considered this would speed up the administrative process. Administrators view the legal process of obtaining the ability to set bar dates from the court as long, arduous and inefficient. Respondents noted that legal expenses are significant (although difficult to quantify) even in small SAR cases. Therefore, applying the bar date mechanism to client money will improve the efficiency of the current regime, ultimately shortening the administration process of a failed firm and lowering costs for clients, creditors and counterparties. Administrators stated in the consultation responses that this reform provides the administrator with "added flexibility and

	potentially saves significant costs and delays." No additional administrative or other costs have been identified.
The administrator will have the power to set 'hard' Bar Dates after one or more 'soft' Bar Dates have been used. The 'hard' Bar Date will extinguish client proprietary claims to assets where claims have not been submitted in time for the hard bar date.	The hard bar date proposal will resolve a market failure in previous SAR administration cases where administrators have been left with a residue of unclaimed client assets following the soft bar date process. This makes it difficult for administrators to close out the client estate which leads to increased administration costs as the process becomes increasingly protracted. No additional administrative or other costs have been identified as the hard bar date is an optional tool for administrators to manage the problem of clients, for whatever reason, not submitting claims for their assets. Due to the costs of managing the client asset pool being met from the client estate, eventually any residue client assets will be sold to meet the costs of the administrators having to manage the client asset pool but this is an inefficient process. Clients are given ample opportunity to submit claims for their assets and have them returned to them promptly. Hence this proposal should not incur any costs on them or leave them in a worse position then they are under the current regime.
Giving the administrator the ability to distribute client assets during the period from after the announcement of a Bar Date until a distribution plan is presented to the Court for approval. Currently administrators can only distribute client assets before a bar date is announced and after the bar date has expired and their distribution plan has been approved.	This proposal removes the unnecessary restriction on administrators distributing client assets in the period between when the bar date is announced and when their distribution plan has been finalised after the bar date has expired. There may be cases where it is appropriate for administrators to distribute assets during the bar date process for example, where clients are experiencing hardship and need an urgent return of their assets, or where there can be no dispute about ownership. This proposal reduces the market impact of firm failure by allowing the administrator to return assets quicker. No additional administrative or other costs have been identified as this proposal is essentially just increasing the flexibility given to administrators.
In any bar date distribution plan submitted to the court for approval, the Administrator will need to set out which client assets have already been returned and to which clients.	In practice administrators already need to maintain accurate records of which client assets have been returned and therefore this proposal will not incur additional costs.

Removing statutory interest on client claims on the general estate

39. A number of the review's recommendations addressed the need to harmonise the SAR with CASS and to clarify clients' rights in respect of the two regimes. One key area highlighted by the review is that in previous administrations, clients have delayed making claims in order to wait and see which of the client estate and general estate is largest. They have then sought to make claims as creditors against the general estate rather than as clients against the client estate to benefit from the high 8% rate of statutory interest that applies to creditor claims.

40. The clients' entitlement to receive statutory interest when they claim against the general estate as creditors to discourage the attempted arbitrage between client and creditor estates that has occurred in previous administrations.

41. This could therefore result in a transfer benefit from clients to the general creditor estate. However, together with the hard bar date proposal, clients will incentivised to submit their claims for client assets in good time, ultimately speeding up the administration process and reducing costs for both clients and creditors.

42. Administrators stated in the consultation responses that there is "compelling public interest to prevent arbitrage between the segregated pool and the general estate" as the reform should "result in more of the money that was actually held at the point of the firm's insolvency being available for distribution".

Facilitating transfers of client positions

16. Transferring client assets from a failed firm to an alternative financial firm is often preferable to returning those assets to clients. Clients whose assets are successfully transferred will benefit from continuity of services and more speedy access to their assets, as these will not be part of protracted insolvency proceedings. Any clients whose assets are not transferred may benefit from a smaller pool of client assets, which will be quicker to distribute, and creditors may benefit from any proceeds from a transfer. This reduces the market impact of insolvency.

17. The review notes that the transfer of client assets is already implicit in the SAR, and all that is needed are some practical and mechanical provisions to assist implementing them. The review highlighted a number of concerns to be addressed in any such mechanism and these have been incorporated when developing the proposed amendments to the SAR regulations, as set out below.

18. Carrying out a transfer will bring the administration process to an end sooner than returning client assets otherwise would, as there will be fewer assets (if any, in the case of a full bulk transfer) that will go through a protracted return process. In facilitating transfers, the below amendments will each contribute to the likelihood a transfer can be completed and therefore potentially reduce the time taken to complete administrations. This will ultimately reduce administration costs for clients and creditors.

Proposals	**Assessment of costs and benefits**
Statutory novation of client contracts without the need for individual client consent.	Removing the need for individual client consent before transferring their assets to a private sector acquirer removes an administrative burden on both clients and the administrators. We are introducing a key safeguard to mitigate the impact on clients (if for example they do not want to have their assets

	transferred). Clients may request their assets to be returned as soon as practicably possible after the transfer has occurred. One consultation respondent's view was that facilitating a transfer in this way may well provide the special administrator with significant costs savings. No additional administrative or other costs have been identified.
Introduce a provision to override data protection rules which might otherwise preclude the sharing of data with a transferee firm.	This will allow the administrator to share information with a transferee firm more readily, reducing the likelihood that a lack of information regarding the clients will be a cause for sale failure. A confidentiality provision will be included for recipients of information shared through this power. No additional administrative or other costs have been identified.
Apply regulation 14 (continuity of supply) to include firms carrying out custodian activities.	This provision prevents custodians from being able to exercise their termination rights as a result of a client firm's entry into the SAR, subject to the exceptions set out in the SAR. For example, if the custodian can demonstrate to the court that the provision of the service causes them financial hardship, they can terminate the service. It is expected that custodians would continue to provide these services as long as they are being paid. Therefore this proposal is not expected to generate any additional cost.

Cost allocations

43. The review made a number of recommendations concerning the allocation of costs incurred during the course of a SAR. The government proposes to make a number of changes in this area, which will make the allocation process simpler and ensure costs fall equitably between the client estate and the firm estate.

44. The review recommended that the government introduces guidance on the allocation of costs and the government proposes to adopt this recommendation in full. The government proposes to set out the relevant guidance in the SAR insolvency rules and legislation, where it will include the following:
    a. the costs of identifying whether assets are client assets or firm assets and the costs of recovering assets to be borne by the general estate;
    b. costs caused by breaches of the FCA CASS rules to be borne by the firm estate;
    c. costs of distributing the client assets to be borne by the client estate; and
    d. flexibility for administrators to take these costs (a-b) from the client estate where the firm estate is insufficient.

45. These changes will put in statute the best practice for cost allocation, which administrators are currently having to establish through the courts, incurring significant administrative expenses. Clarifying the appropriate cost allocation between the client and general estate in certain scenarios will benefit both the client and general estate.

46. The government also proposes to implement the review's recommendation to empower administrators to transfer amounts between the firm's bank accounts and client accounts following a reconciliation based on the firm's own reconciliation methods that reveals certain client money amounts are held in a firm account according to the firm's records.

47. This proposal will:
    - help reduce the number of client claims against the general estate for client money shortfalls;
    - lower the incentive for clients to challenge in court the right to monies deemed to be client money but which were not appropriately segregated and have ended up in the firm's own account; and
    - speed up distributions from both the client and creditor estates.

48. This proposal does not impose a cost on the general estate as the money in the firm's bank account being transferred to the client money account is money that should have been segregated into the client account but which, for valid reasons, was not transferred from the firm's account before the firm failed.

49. Consultation respondents agree that the current process is cumbersome and increases the administrator's costs.

Minor technical amendments

The table below sets out other minor and technical amendments which have been recommended to improve the functioning of the SAR:

Proposal	**Assessment of costs and benefits**
Scope of SAR	
Make amendments to ensure firms that have fallen out of scope of the SAR for technical reasons are brought back in. This will include the managers of Alternative Investment Funds (AIFs) and UCITs.	No costs have been identified as this proposal is simply ensuring that the firms which were originally caught by the SAR are still caught by the SAR following some technical definition changes in European legislation. Being re-included in the SAR does not impose any cost on these firms and has no effect on investment firms. The SAR sets out how the administrators should wind down a failed firm for clients, creditors and counterparties. It imposes no additional burden on the investment firm itself. As set out in paragraph 14, stakeholders agree that the SAR reforms do not place burdens on firms when they are a going concern. The original SAR (brought in in 2011), which included these firms, was found to have zero costs to firms. Stakeholders agree that this reformed SAR is a simpler, more effective and less costly regime. Therefore, re-including these firms should similarly impose no extra costs. This amendment will bring the total number of firms in scope for entry into the SAR to c.1,000. Without this amendment the total number is c.700.
Creditor Committees	
FSCS should be entitled to sit on creditors' committees, regardless of whether it has yet made	Administrators and the FSCS already have to work closely together in the event of an investment firm failure and this proposal will help facilitate

compensation payments, unless it is clear that no compensation will be payable.	cooperation and information sharing between the FSCS and the administrators. No additional costs have been identified.
Information Sharing and Cooperation Duties	
Entities holding client assets (including client monies) of failed firms should without amendment of the SAR investigate and return them promptly.	In practice, firms holding client assets and money already need to identify and return client assets and money to administrators of a failed firm so the proposal to lay down a legislative duty is not being implemented (it is unclear what benefit such a duty would have or how it would be enforced).
Counterparties of failed firms should without amendment of the SAR respond promptly to the administrator's request for information and financial data such as close out valuations.	In practice, counterparties of a failed firm already work closely with administrators to help close out positions.
Review	
Removal of requirements for review of SAR each time the Treasury makes new regulations pursuant to section 233 of the Act.	Another statutory review in the two years of the SAR after the Treasury makes the proposed amendments will be a disproportionate use of resources, especially as it is possible that only a very small number firms will enter the SAR in that period. We instead intend to adopt the required 5 yearly review clause for secondary legislation.

Risks and assumptions

50. The key assumption is that the amendments will provide all affected parties with more legal clarity to resolve the complex legal issues which can arise when investment firms fail. This should reduce the need for administrators to go to court for direction which is a time consuming and expensive process.

51. The proposals have been considered in detail by an independent review and through consultation, including with the Banking Liaison Panel. The government is confident that the amended SAR will allow administrators to take decisions in the interests of clients and creditors while ensuring there are appropriate checks and balances. For example, the administrators will still need to get the courts to approve their distribution plans for client assets after setting a bar date.

Impact on small firms and competition

52. The government believes there will be no impact on small firms, as the recommended reforms do not impose any additional financial or administrative burdens on firms. Furthermore, small and micro businesses will benefit from increased financial stability and improved continuity of financial services. The government anticipates that the amendments which relate to transfer of client assets could improve competition in the industry.

53. Administrators are the only party in an insolvency that have to comply with the SAR reforms regulations. Responses at consultation stage showed that administrators do not anticipate quantifiable costs associated with complying with the amendments. This applies to small and large administrators alike. Therefore, small businesses are not disproportionately burdened by the policy as there are no burdens associated with complying.

54. Investment firms do not have to comply with the reforms, the SAR does not concern them on a going-concern basis and therefore insolvency laws are not a burden for them. There are zero costs for investment firms of any size.

55. The clients and creditors of insolvent investment firms also incur no costs associated with the SAR reforms and therefore the policy represents zero costs for them. Clients and creditors do not familiarise themselves with the rules of the SAR until an insolvency that affects them happens. At this point, the costs of familiarisation to the policy is zero compared to the baseline (no reforms), as clients and creditors must familiarise themselves with the SAR whether it is reformed or not.

56. If small administrators were given exemption from the SAR amendments and allowed to not comply with regulations, any insolvency process would be slower at returning client assets and give less certainty to counterparties. This would increase the costs of the administration process when conducted under a small administrator. Using the indicative sample provided by current SAR administration cases and applying the same methods, it is estimated that exempting small administrators from the scope of the SAR reforms would reduce the benefits of the amendments by £28,689-£114,757 per year. In other words, the policy cost of exempting small firms from the SAR amendment is estimated to be £28,689-£114,757 per year for the appraisal period.

57. This cost does not take into account the fact that, if small administrators were given an exemption, it is less likely that they would be appointed to be an administrator of an investment firm which failed. Affected parties prefer to have an administration under the amended SAR as it is a more efficient and more certain process with a smaller market impact. Small administrators would therefore lose this business, worth an estimated £573,785 in fees per year for the appraisal period.

Equality impact

58. The government has considered its obligation under the Equalities Act 2010. The government does not believe these measures will impact upon discrimination, equality of opportunity or good relations towards people who share relevant protected characteristics under the Act. The government considers that the proposals are compatible with the Convention rights protected by the Human Rights Act 1998.

Summary and preferred option with description of implementation plan

59. The preferred option is to implement the reforms recommended by the review which are within the government's remit. The amendments will be laid before Parliament and subject to affirmative draft procedures. This measure will be for HMT to take forward.