

EXPLANATORY MEMORANDUM TO
THE DEPOSIT GUARANTEE SCHEME AND MISCELLANEOUS PROVISIONS
(AMENDMENT) (EU EXIT) REGULATIONS

2018 No. 1285

1. Introduction

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

2. Purpose of the instrument

2.1 This instrument is principally being made in order to address deficiencies in retained EU law in relation to the UK's deposit guarantee scheme, the Financial Ombudsman Service (FOS) and certain inquiries and investigations. Deposit Guarantee Schemes (DGSs) protect depositors of banks and other credit institutions in the event that they are unable to repay deposits due. If this situation arises, DGSs protect depositors up to defined levels and provide compensation to depositors, removing the need for depositors to seek to recover their money through insolvency proceedings. The UK's DGS is the Financial Services Compensation Scheme (FSCS).

2.2 These are deficiencies arising from the withdrawal of the United Kingdom (UK) from the European Union (EU). The instrument will ensure the legislation continues to operate effectively at the point at which the UK leaves the EU.

2.3 The instrument also amends the definitions of "deposit" and "eligible deposit" in regulations relating to the DGSs to ensure consistency with provisions stating that the credit unions are compensation scheme members.

Explanations

What did any relevant EU law do before exit day?

2.4 The Deposit Guarantee Schemes Directive 2014/49/EU (DGSD), adopted in 2014, created a harmonised system of DGSs across the EU to ensure that depositors are adequately protected. Certain provisions of the DGSD were transposed into UK law through the Deposit Guarantee Scheme Regulations 2015 (S.I. 2015/486).

2.5 The Alternative Dispute Resolution Directive 2013/11/EU (ADR Directive) sets out quality requirements for entities that provide alternative dispute resolution (ADR) services within the EU. The FOS is the UK's ADR service for financial services and is established by the Financial Services and Markets Act 2000 (FSMA) and operates under rules made by the Financial Conduct Authority (FCA).

2.6 Section 82 of the Financial Services Act 2012 sets out provisions for HM Treasury to publish reports of independent inquiries arranged by HM Treasury and investigations into possible regulatory failure. It obliges HM Treasury to publish such reports in full and lay them before Parliament, but also sets out conditions under which HM Treasury may withhold material in the report from publication. One such condition is that material can be withheld to such extent as is required by any enforceable EU obligation.

Why is it being changed?

- 2.7 Once the UK leaves the EU, it will no longer be subject to EU obligations such as those set out in the DGSD and the ADR Directive.

What will it now do?

- 2.8 This SI removes EU references and arrangements which will no longer be appropriate after withdrawal. This instrument also transfers to the UK's Prudential Regulation Authority (PRA) the power to review and adjust the deposit coverage level, which is currently set by EU institutions in accordance with the DGSD. Further details can be found in paragraphs 7.9 - 7.16 below.
- 2.9 This SI will have no substantive impact on the operation of the FOS or HM Treasury's publication of reports of inquiries and investigations.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 None.

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

- 3.2 The territorial application of this instrument includes Scotland and Northern Ireland.
- 3.3 The powers under which this instrument is made cover the entire United Kingdom 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 extent of this instrument is the whole United Kingdom.
- 4.2 The territorial application of this instrument is the whole United Kingdom.

5. European Convention on Human Rights

- 5.1 The Economic Secretary to the Treasury (John Glen) has made the following statement regarding Human Rights:

“In my view the provisions of the Deposit Guarantee Scheme and Miscellaneous Provisions (Amendment) (EU Exit) Regulations 2018 are compatible with the Convention rights.”

6. Legislative Context

- 6.1 This instrument amends FSMA, the Financial Services Act 2012 and the Deposit Guarantee Scheme Regulations 2015 (S.I. 2015/468) to address deficiencies arising from the UK's exit from the EU. The instrument also makes a correcting amendment to the definitions of “deposit” and “eligible deposit” under those regulations.

7. Policy background

What is being done and why?

- 7.1 The UK will leave the EU on 29 March 2019. The UK and the EU have agreed the terms of an implementation period that will start on 29 March 2019 and last until 31

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

- 7.2 The government is seeking a deep and special future partnership with the EU, which should be greater in scope and ambition than any such agreement before and encompass financial services. Given the highly regulated nature of financial services, the volume of trade between UK and EU markets, and a shared desire to manage financial stability risks, the UK proposes a new economic and regulatory arrangement that will preserve mutually beneficial cross-border business models and economic integration for the benefit of businesses and consumers. Decisions on market access would be autonomous in our proposed model, but would be underpinned by stable institutional processes in a bilateral agreement and continued close regulatory and supervisory cooperation.
- 7.3 While the government has every confidence that a deal will be reached and the implementation period will be in place, it has a duty to plan for all eventualities, including a 'no deal' scenario. The government is clear that this scenario is in neither the UK's nor the EU's interest, and the government does not anticipate it arising. To prepare for this unlikely eventuality, HM Treasury intends to use powers in the European Union (Withdrawal) Act 2018 (EUWA) to ensure that the UK continues to have a functioning financial services regulatory regime in all scenarios.
- 7.4 The EUWA repeals the European Communities Act 1972 and converts into UK domestic law the existing body of directly applicable EU law (including EU Regulations). It also preserves UK laws relating to EU membership – e.g. legislation implementing EU Directives. This body of law is referred to as "retained EU law". The EUWA also gives ministers a power to prevent, remedy or mitigate any failure of EU law to operate effectively, or any other deficiency in retained EU law, through SIs. These contingency preparations for financial services legislation are sometimes referred to as 'onshoring'. These SIs are not intended to make policy changes, other than to reflect the UK's new position outside the EU, and to smooth the transition to this situation. The scope of the power is drafted to reflect this purpose and is subject to further restrictions, such as the inability to use the power to impose or increase taxation, or establish a public authority. The power is also time-limited and falls away two years after exit day.
- 7.5 Wherever practicable, the proposed approach is that the same laws and rules that are currently in place in the UK would continue to apply at the point of exit, providing continuity and certainty as we leave the EU. However, if the UK does not enter an implementation period, some changes would be required to reflect the UK's new position outside the EU from 29 March 2019.
- 7.6 In the unlikely scenario that the UK leaves the EU without a deal, the UK would be outside the EU's framework for financial services. The UK's position in relation to the EU would be determined by the default Member State and EU rules that apply to

third countries at the relevant time. The European Commission has confirmed that this would be the case.

- 7.7 In light of this, the approach in this scenario cannot and does not rely on any new, specific arrangements being in place between the UK and the EU. As a general principle, the UK would also need to default to treating EU Member States largely as it does other third countries, although there are cases where a different approach would be needed including to provide for a smooth transition to the new circumstances.
- 7.8 HM Treasury published a document on 27 June 2018, which sets out in more detail HM Treasury's approach to financial services legislation under the European Union (Withdrawal) Act. (<https://www.gov.uk/government/publications/financial-services-legislation-under-the-eu-withdrawal-act>)

Amendments of the Deposit Guarantee Scheme Regulations 2015

- 7.9 DGS protect depositors of banks and other credit institutions in the event that they are unable to repay deposits due. If this situation arises, DGS protect depositors up to defined levels and provide compensation to depositors, removing the need to seek to recover their money through insolvency proceedings. The UK's DGS is the Financial Services Compensation Scheme (FSCS).
- 7.10 The DGSD created a harmonised system of DGS across Europe; the UK transposed the DGSD through the Deposit Guarantee Scheme Regulations 2015. Those regulations contain provisions for the FSCS to work with DGS in different member states and a requirement for the PRA to provide certain information to the European Banking Authority.
- 7.11 UK legislation on deposit guarantee schemes treats countries in the European Economic Area (EEA) differently from other third countries in certain respects, which will no longer be appropriate after exit day. In line with the approach taken in the other Financial Services EU Exit instruments, this SI will amend the Deposit Guarantee Scheme Regulations 2015 so that the UK treats the EEA no differently to other third countries except in certain cases, set out below, where the government believes an alternative approach is justified.
- 7.12 Save for Part 2, this instrument corrects deficiencies in retained EU law arising out of the UK's withdrawal from the EU. In particular, this SI makes amendments to transfer from EU institutions to the PRA the power to set the maximum compensation payable by the FSCS. The PRA will have the power to review, adjust and set the deposit coverage level with approval from HM Treasury. The government views the PRA as the most appropriate body to review and adjust the deposit coverage limit in light of the PRA's technical expertise and understanding of wider market conditions.
- 7.13 The SI also removes the (reciprocated) arrangement whereby the FSCS administers, as an agent, compensation payments to depositors at UK branches of credit institutions that are members of an EEA DGS. However, the SI includes a transitional provision allowing the FSCS to continue to make payments after Exit in respect of compensation claims due prior to exit from the EU. This ensures that the FSCS can still make payments, on receipt of instructions and funds from EEA DGS, to persons who deposited funds with the UK branches of EEA credit institutions where compensation becomes due before the UK's exit from the EU. This provision has

been saved to enable compensation to be paid to UK depositors as quickly and as easily as possible in these limited circumstances.

- 7.14 Aside from this saving provision, the overall effect of regulation 5(7) will be that, after EU exit, the deposit guarantee schemes of EEA member states will be treated on the same basis as those of third countries for the purpose of the UK's deposit guarantee scheme arrangements.
- 7.15 This SI removes the requirements of the PRA to notify certain matters to the EBA, notably the total number of covered deposits and contents of cooperation agreements between the FSCS and a non-UK DGS, which is required under the DGSD.
- 7.16 The SI also amends EU references which will no longer be appropriate after exit.
- 7.17 Part 2 of this SI is being made in exercise of the powers in section 2(2) of the European Communities Act 1972 (c.68) in order to make minor amendments to the Deposit Guarantee Scheme Regulations 2015 (S.I. 2015/468). These amendments bring certain shares in credit unions within the meaning of "deposit" in the Deposit Guarantee Scheme Regulations 2015 and make corresponding updates to the meaning of "eligible deposit". These amendments ensure consistency with the definition of "compensation scheme member" in that instrument (which includes credit unions).

Amendments of Primary Legislation

- 7.18 Parts 1 and 2 of Schedule 17 to FSMA provide that the FCA must exercise its functions in relation to the FOS in a way which is consistent with enabling the FOS to qualify as an ADR entity under, and to meet the quality requirements in, the ADR Directive. This SI amends references to the ADR Directive in this primary legislation as they will no longer be appropriate after exit.
- 7.19 Under Part 5 of the Financial Services Act 2012, in certain circumstances HM Treasury may arrange an independent inquiry and the PRA and FCA must conduct an investigation into possible regulatory failure. HM Treasury must publish in full reports of such investigations or inquiries. However, under section 82(3)(a) of FSMA HM Treasury may withhold material in the report from publication to such an extent as is required by any enforceable EU obligation.
- 7.20 This SI makes an amendment to the ability of HM Treasury to withhold material on this basis as the UK will no longer be bound by EU obligations after withdrawal except where the obligations are contained in retained EU law, therefore, the reference in this provision of primary legislation is no longer appropriate and requires amendment.

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

- 8.1 This instrument is being made using the power in section 8 of the EUWA in order to address failures of retained EU law to operate effectively or other deficiencies arising from the withdrawal of the United Kingdom from the European Union. In accordance with the requirements of that Act the Minister has made the relevant statements as detailed in Part 2 of the Annex to this Explanatory Memorandum.
- 8.2 Alongside the EU (Withdrawal) Act 2018 powers, the instrument is also being made under section 2(2) of the European Communities Act 1972 (c.68) in order to make

minor amendments to the Deposit Guarantee Scheme Regulations 2015 (S.I. 2015/468) in order to ensure consistency of certain defined terms.

9. Consolidation

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

10. Consultation outcome

10.1 HM Treasury has not undertaken a consultation on the instrument, but has engaged with relevant stakeholders (banks, financial services industry bodies) on its approach to Financial Services legislation under the EUWA, including on this instrument.

10.2 The instrument was also published in draft, along with an explanatory policy note, on 15 August 2018, in order to maximise transparency ahead of laying.
(<https://www.gov.uk/government/publications/draft-deposit-guarantee-scheme-and-miscellaneous-provisions-amendment-eu-exit-regulations-2018/deposit-guarantee-scheme-and-miscellaneous-provisions-amendment-eu-exit-regulations-2018-explanatory-information>).

11. Guidance

11.1 No further guidance is being published alongside this instrument. The PRA and FCA will, in due course, consult on and update their rules accordingly.

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, 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.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring & review

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

15. Contact

15.1 Connie Chen at HM Treasury Telephone: 020 7270 5856 or email: connie.chen@hmtreasury.gov.uk can be contacted with any queries regarding the instrument.

15.2 Lowri Khan, Director of Financial Stability, 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	Set out the 'good reasons' for creating a criminal offence, and the penalty attached.

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

Part 2

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

1. Appropriateness statement

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

“In my view the Deposit Guarantee Scheme and Miscellaneous Provisions (Amendment) (EU Exit) Regulations 2018 does no more than is appropriate”.

1.2 This is the case because: the amendments to the role of the PRA and the FSCS are necessary to address deficiencies in legislation arising from EU exit. The post-exit transfer of power from EU institutions to the PRA to review and adjust the deposit coverage level is necessary to ensure the coverage level remains fit for purpose in the future. The PRA’s expertise makes them the most appropriate body to complete this task.

1.3 The provision allowing the FSCS to make payments in respect of compensation claims due prior to exit is designed to provide assurance to customers of UK branches of EEA credit institutions. Other amendments are minor and technical in nature.

2. Good reasons

2.1 The Economic Secretary to the Treasury, John Glen, 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 PRA already converts the EU’s deposit coverage level into sterling and it is best placed to review and adjust the future level, subject to approval from HM Treasury. This allocation of responsibility would be consistent with the general rule-making responsibilities already delegated to the PRA by Parliament under FSMA and associated legislation. Transferring this power to the PRA is the most effective way of ensuring that the UK’s deposit coverage level will continue to provide effective and appropriate protection to depositors after exit. The PRA’s expertise makes them the most appropriate body to complete this task.

2.3 The provision allowing the FSCS to make payments after exit on behalf of EEA DGS is designed to ensure that assurance is provided to customers of UK branches of EEA credit institutions whose compensation claims become due immediately before exit.

3. Equalities

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

“The Deposit Guarantee Scheme and Miscellaneous Provisions (Amendment) (EU Exit) Regulations 2018 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, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

“In relation to the Deposit Guarantee Scheme and Miscellaneous Provisions (Amendment) (EU Exit) Regulations 2018, 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 2 of the main body of this explanatory memorandum.

5. Legislative sub-delegation

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

“In my view it is appropriate to create a relevant sub-delegated power in the Deposit Guarantee Scheme and Miscellaneous Provisions (Amendment) (EU Exit) Regulations 2018.”

5.2 This is appropriate because: it will give the PRA the responsibility of reviewing and adjusting the deposit coverage level as necessary to reflect UK circumstances and so it remains fit for purpose. It is necessary for the PRA to perform this task, given that it is mainly a technical exercise.