

EXPLANATORY MEMORANDUM TO

THE FINANCIAL SERVICES AND MARKETS ACT 2000 (CONSEQUENTIAL AMENDMENTS OF REFERENCES TO RULES) REGULATIONS 2021

2021 No. 1388

1. Introduction

1.1 This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument makes consequential amendments to definitions in legislation which refer to, and include, rules made by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) to update the prudential regime for banks and investment firms in the UK. The changes to rules made by the PRA and the FCA stem from the use of powers taken by HM Treasury through the Financial Services Act 2021 (FS Act).¹

2.2 Overall, these FS Act powers enable the implementation of the Investment Firms Prudential Regime (IFPR) and remaining aspects of the Third Basel Accord (Basel 3 standards).

2.3 The PRA has made “CRR rules” (as defined in section 144A of the Financial Services and Markets Act 2000 (c. 8)) which implement the remaining Basel 3 standards.² The FCA has made “Part 9C rules” (as defined in section 143F of the Financial Services and Markets Act 2000) to implement the IFPR.³ These rules come into force on 1 January 2022.

2.4 Given this, the purpose of this instrument is to update references in legislation to the rules made by the regulators as they apply on 1 January 2022.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

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:

¹ Financial Services Act 2021 c. 22.

² The PRA rules on the Basel standards are contained in the legal instruments PRA 2021/13 (Basel 3) and PRA 2021/14 (Leverage rules).

³ The final IFPR rules are contained in the legal instruments FCA 2021/38, FCA 2021/39, FCA 2021/49, FCA 2021/50 and FCA 2021/51.

“In my view the provisions of the Financial Services and Markets Act 2000 (Consequential Amendments of References to Rules) Regulations 2021 are compatible with the Convention rights”

6. Legislative Context

- 6.1 This instrument makes consequential amendments to references in legislation to rules made by the PRA and FCA so that they refer to the rules as they apply on 1 January 2022. This ensures that the references in legislation capture the changes that have been made to the regulators’ rules under powers in Part 9C and Part 9D, Financial Services and Markets Act 2000 (FSMA). Parts 9C and 9D FSMA were inserted by the FS Act in order to implement the IFPR and Basel standards, as explained above.
- 6.2 The UK, as a member of the G20, is committed to the implementation of the international Basel standards on banking. As explained below, after the financial crisis of 2007 to 2008, those standards were updated in stages, referred to as the Basel 3 standards and Basel 3.1 standards. As the UK has left the EU, the UK is domestically implementing those standards which do not currently form part of domestic law. This includes some of those standards contained in the EU’s 2nd Capital Requirements Regulation (CRR)⁴.
- 6.3 The FS Act enables the implementation of the remaining Basel 3 standards by giving powers to HM Treasury to revoke provisions of the Capital Requirements Regulation (CRR).⁵ Following repeal, the PRA can write rules on the subject areas deleted.
- 6.4 The FS Act also introduced a bespoke prudential regime for non-systemic investment firms – the IFPR - by placing an obligation on, and providing powers for, the FCA in sections 143C to 143E (contained in Part 9C) of FSMA⁶ to introduce prudential rules for investment firms (Part 9C rules).
- 6.5 This instrument exercises HM Treasury’s power in section 141A of FSMA to amend legislation in consequence of the regulators amending their rules.⁷ The effect of these amendments is that the references to rules made by the regulators in legislation will include the changes that have been made to the regulators’ rules as a result of the making of Part 9C rules and CRR rules.

7. Policy background

What is being done and why?

Basel Implementation

- 7.1 The global financial crisis of 2007-09 demonstrated the importance of the stability of the banking sector. This sector provides essential services to the economy, such as deposit taking, the facilitation of payments and the provision of credit.

⁴ Regulation 2019/876 of the European Parliament and of the Council of 20 May 2019 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.

⁵ EUR 575/2015. HM Treasury’s power to revoke provisions of this Regulation is found in section 3, FS Act.

⁶ As inserted by Schedule 2 to the FS Act.

⁷ This power is contained in section 141A, FSMA. The use of this power requires the negative procedure and so these amendments could not form part of the Financial Services Act 2021 (Prudential Regulation of Credit Institutions and Investment Firms) (Consequential Amendments and Miscellaneous Provisions) Regulations 2021.

- 7.2 In response to the financial crisis, the Basel Committee on Banking Supervision (BCBS) agreed the Basel 3 standards. The UK played an active role in negotiating and agreeing these standards and has always been committed to their implementation.
- 7.3 These standards sought to strengthen the existing prudential 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.
- 7.4 Prior to the end of the implementation period, the UK had implemented the majority of the earlier Basel Standards through EU law.
- 7.5 The most recent EU legislation which implemented some of the Basel standards was CRR2 and the 5th Capital Requirements Directive (CRDV).⁸ Some aspects of CRR2, however, came into application following Implementation Period Completion Day (IPCD) and therefore do not form part of retained EU law. Under the FS Act, the remaining Basel 3 and 3.1 standards will be implemented through the PRA's CRR rules.

The Investment Firms Prudential Regime

- 7.6 Many investment firms are currently subject to the CRR framework, while others are exempt from the CRR and related requirements.
- 7.7 Investment firms differ from credit institutions (banks) in that they do not typically accept deposits or grant traditional loans; instead, investment firms provide investment services and perform investment activities. This means that, whilst there is some overlap, the risks posed and faced by investment firms, and the impact of those risks, are different from those of credit institutions.
- 7.8 As such, the CRR framework in its current form does not appropriately cater for the differences between credit institutions and investment firms and can be disproportionate, burdensome, and inappropriate to the risks these firms face.
- 7.9 To address these issues, the FCA is creating a tailored regime specifically for non-systemic investment firms (the IFPR), to fulfil its duty introduced in the FS Act. PRA designated investment firms (systemic investment firms) will continue to remain subject to the CRR framework.
- 7.10 The FCA has published all its final Part 9C rules.⁹

Basel 3 and IFPR consequential amendments

- 7.11 This instrument will amend the definition of "Directive 2013/36/EU UK law" within certain pieces of legislation. "Directive 2013/36/EU UK law" is currently defined as meaning "the law of the United Kingdom which was relied on immediately before IP completion day to implement the capital requirements directive and its implementing measures as it has effect a) on IP completion day, in the case of rules made by the FCA or the PRA under this Act, and b) as amended from time to time, in all other cases".

⁸ 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.

⁹ The final IFPR rules are contained in the legal instruments FCA 2021/38, FCA 2021/39, FCA 2021/49, FCA 2021/50 and FCA 2021/51. See also the FCA's IFPR website for IFPR discussion paper, consultations and policy statements.

- 7.12 This instrument also updates the definitions of the Collective Investment Schemes sourcebook, the FCA Handbook and the PRA Rulebook where they appear in the statute book to ensure that those definitions capture CRR rules and Part 9C rules made as of 1 January 2022.
- 7.13 The amendments substitute the reference to ‘IP completion day’, in the context of rules made by the FCA or the PRA, with ‘1 January 2022’. This will ensure that the definitions capture regulator rules as they have effect on 1 January 2022 (rather than 31 December 2020). This is because, as a consequence of the PRA and the FCA making CRR and Part 9C rules, respectively, they have had to amend some of their rules which implemented the Capital Requirements Directive (CRD).

8. European Union Withdrawal and Future Relationship

- 8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

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, as well as the amendments to the PRA RAO and scope of the Resolution regime.
- 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-investmentfirms-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 The measures in this instrument are accounted for in a de minimis assessment of the impact of consequential amendments to legislation further to the Financial Services Act 2021 (c. 22). A copy of the assessment is published on legislation.gov.uk with 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 or will fall in the scope of the IFPR.
- 13.2 However, the number of small businesses (banks and investment firms) 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 regulator rules and therefore amendments to the scope of the revocations”

15. Contact

- 15.1 Moshin Hamim at HM Treasury email: moshin.hamim@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.