UK Finance response to the Bank of England's consultation on its approach to resolution statements of policy and onshored Binding Technical Standards

2nd January 2019

Introduction

UK Finance is pleased to respond to the Bank of England's consultation on its approach to resolution statements of policy and onshored Binding Technical Standards[1], whilst taking into consideration the separate PRA/Bank of England CP 26/18 on the UK withdrawal from the EU: Changes to the PRA Rulebook and onshored Binding Technical Standards[2].

UK Finance represents more than 250 of the leading firms providing finance, banking, markets and payments related services in or from the UK. UK Finance was created by combining most of the activities of the Asset Based Finance Association, the British Bankers' Association, the Council of Mortgage Lenders, Financial Fraud Action UK, Payments UK and the UK Cards Association. Our members are large and small, national and regional, domestic and international, corporate and mutual, retail and wholesale, physical and virtual, banks and non-banks. Our members' customers are individuals, corporates, charities, clubs, associations and government bodies, served domestically and cross-border. These customers access a wide range of financial and advisory products and services, essential to their day-to-day activities. The interests of our members' customers are at the heart of our work.

General observations

We and our members fully support the Government's and the regulators' objectives of ensuring the UK has a fully functioning regulatory framework for financial services in place once the UK leaves the EU – indeed, all the more so if no implementation period is agreed with the EU. Our members are committed to ensuring that, in spite of Brexit, the UK's financial services sector remains robust, transparent and internationally competitive.

Although we understand that there is no formal requirement to consult stakeholders on the changes proposed in this consultation, we very much support the Bank's decision to do so, as well as the constructive exchanges we have had so far. We and our members look forward to a continued dialogue on these important issues as the process evolves.

We support the Bank's clearly stated intention to deploy the powers delegated to them under the 'Financial Regulators' Powers Regulations 2018' draft SI to fix deficiencies in onshored Binding Technical Standards (BTS) that arise as a result of the UK's exit from the EU, rather than to make policy changes. This is key

[1] https://www.bankofengland.co.uk/-/media/boe/files/paper/2018/uk-withdrawal-from-eu-boe-approach-to-resolution-sops-and-onshored-bts-complete.pdf?la=en&hash=450BE158DDF0D972247AC794438B0E8ED8179431

[2] https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2018/cp2618-complete.pdf?la=en&hash=2A1C385C5C157974FDDE36FC5D72F515AD667AA1

in order to provide as orderly a transition as possible for firms, especially in the event of no agreement being found between the UK and the EU. Nevertheless, the UK's exit from the EU creates important, broader resolution-related policy issues than are touched upon by this consultation, which merit careful attention and guidance.

Contractual recognition of bail-in, stays and transitional relief

Article 55 of the Bank Recovery and Resolution Directive (BRRD) states that where instruments which are subject to bail-in are governed by third country law, firms must insert contractual terms recognising the potential for the instrument to be bailed-in.

Since its inception, firms have found the provision to be very burdensome, as the contractual terms cannot be amended without counterparty consent; this proves to be particularly difficult for securities issues, as consent may be impossible to obtain and will in any event induce significant costs in seeking it.

During our previous discussions with policymakers on the UK's application Article 55 to EU Member States as part of its onshoring the BRRD, we understand that to remove this provision would amount to a material policy change, thereby cutting across the objectives of the EU Withdrawal Act. We support the PRA and Bank of England's pragmatic approach by proposing to allow firms to insert these contractual terms only where the contract is being amended otherwise as well as the proposal to apply transitional relief to Phase 2 liabilities, as outlined in CP 26/18. This would help firms to spread the burden over a longer time period and to focus on compliance with various other changes to requirements in the run up to exit day.

Nevertheless, as also stated in our responses to CPs 25/18 and 26/18, **our members generally support a period of transitional relief of two years**, unless there is an international development relevant to the individual policy area that is likely to be implemented after its expiration. Where this is the case, the transition period should be extended to avoid sequential changes that may arise. We therefore believe such a transitional period should apply in the case of contractual recognition of bail-in and particularly for contractual stays, since firms will be required to immediately repaper all clients with master agreements to ensure that new trades are covered by the required language and this will take some time to complete.

Recovery and resolution plans

We understand that the scope of Government's and regulators' 'onshoring' exercises is to implement EU legislation with minimal changes, in this case the BRRD and BRRD BTS, so that the UK has a fully functioning resolution framework as soon as the UK leaves the EU. However, our members – especially those that operate cross-border and particularly in the EU - are keen to understand whether or not Brexit will have a significant impact on their current recovery and resolution plans and, if so, the Bank of England's proposed approach. Indeed, it is not yet understood whether firms will be required to draw up and maintain standalone plans for their UK operations. Given the significant resources required to produce and comply with recovery and resolution plans, as well as the fact that thus far our members are not aware of the Bank's preferred approach, we recommend that **all current plans are grandfathered until their review as part of the normal planning process**.

Considerations regarding the draft EU Exit Instrument

Aside from the policy concerns detailed above, our members would also like to highlight a number of issues of a more technical and legal nature.

References to EU legislation: There is an issue regarding newly added references to retained direct EU legislation, as such references will not be to such legislation as amended from time to time. Set out below are the details of this analysis:

- Schedule 8, Part 1, paragraph 1(1) of the European Union (Withdrawal) Act 2018 provides that any reference, which exists immediately before exit day in any enactment, to any EU regulation, EU

decision or EU tertiary legislation is to be read, on or after exit day, as a reference to the EU regulation, EU decision or EU tertiary legislation as modified by domestic law from time to time. The term "enactment" is defined to include any retained direct EU legislation, which includes EU tertiary legislation such as the BTS (sections 20(1) and 3(2) of the European Union (Withdrawal) Act 2018). As a result, references to retained direct EU legislation (which existed immediately before exit day) in BTS will automatically be references to the relevant EU legislation as amended.

- However, references to retained direct EU legislation that did not exist before exit day will not benefit from this treatment. While a provision with similar effect exists under section 20(2) of the Interpretation Act 1978 (which provides that references to enactments will be to the enactment as amended), the Interpretation Act 1978 does not apply to amendments to BTS made by Bank of England EU Exit Instruments. Notably, section 23ZA of the Interpretation Act does apply certain provisions of the Interpretation Act 1978 to retained direct EU legislation. However, this is only the case for retained direct EU legislation so far as it "*is amended by [...] subordinate legislation*". EU Exit Instruments made under the Financial Regulators' Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018 do not fall under the definition of "subordinate legislation" in section 21(1), as such instruments are not made under "*any Act*" or "*retained direct EU legislation*" (the latter being a pending amendment to this provision under Schedule 8, Part 2, paragraph 19 of the European Union (Withdrawal) Act 2018).

This means that newly added references to UK/EU legislation under this CP will be static as such provisions will not benefit from the "*as amended*" treatment under section 20(2) of the Interpretation Act, and will instead be ossified as at the version "*as amended [by the relevant Brexit SI]*" but nothing else. This is inappropriate, since references to legislation should best be dynamic to avoid difficulties in making future amendments.

In order to rectify this, we would suggest adopting one of the following options:

1) Option 1 – adding either of the following interpretive provisions on the face of each EU Exit Instrument, or in the "Interpretation" provisions of each BTS:

    - "*Any reference in this [instrument/BTS] to any enactment (within the meaning in Schedule 1 of the Interpretation Act 1978) is, unless the contrary intention appears, a reference to that enactment as amended, and includes a reference thereto as extended or applied, by or under any other enactment.*" This provision has been drafted based on the Interpretation Act 1978 provision described above.

    - "*Paragraph 1 of Part 1 of Schedule 8 of the Act will apply to any reference in this [instrument/BTS] to any EU regulation, EU decision, EU tertiary legislation which is to form part of domestic law by virtue of section 3 of the Act as if such reference existed in an enactment immediately before exit day.*" This provision applies the provision of the European Union (Withdrawal) Act 2018 described above as if the new references were also in scope. However, this provision would not apply to references to UK legislation, and therefore leaves the issue partially unresolved.

2) Option 2 – specifically stating either on the face of each EU Exit Instrument, or in the "Interpretation" provisions of each BTS, that the Interpretation Act 1978 applies to each EU Exit Instrument or BTS as follows: "the *Interpretation Act 1978 applies to this [instrument/BTS].*"

We note that this is the approach taken under the FCA Handbook and PRA Rulebook, to which the Interpretation Act 1978 also do not apply. See GEN 2.2.11, which provides that "*[t]he Interpretation Act 1978 applies to the Handbook*" and paragraph 2.3 of the Interpretation part of the PRA Rulebook which provides that *"[s]ave as otherwise indicated, the Interpretation Act 1978 applies to the PRA Rulebook"*. As these Handbook and Rulebook provisions do not apply to onshored BTS, they would need to be added to each EU Exit Instrument or BTS as suggested above to resolve the issue in relation to onshored BTS.

Furthermore, there are a number of provisions which make direct reference to EU legislation "as that law has effect on exit day", namely in **Annex B**, Article 41 paragraph 5 and **Annex E**, Article 4 paragraph 3. These provisions would effectively freeze the interpretation of the references to EU law at exit day, which is the day on which the Regulations will become 'retained EU law' under the EU Withdrawal Act, potentially in a different form reflecting changes to the Regulations after this date. Given the effect of this provision would be immediate and therefore applicable during a potential transitional period with the EU, it would be inconsistent with the UK's current EU obligation to apply the 'in force' provisions of EU regulations. Over time, the particular versions of these regulations in force at exit day may become difficult to find as the EU text will be updated, which could make compliance lengthy and complex.

Paragraph 1.1.3: In the Interpretative Provisions section of this BTS, it should be stated that the scope of application of the Bank Recovery and Resolution BTS does not extend to either CCPs or investment firms. The Banking Act 2009, which implements the BRRD in the UK, also applies to CCPs – but in a modified form in which the amendments to this legislation that were made to implement BRRD do not apply to such organisations. The BRRD does not apply to CCPs or to most investment firms. However, the Banking Act does apply to CCPs and certain investment firms pursuant to the Banking Act itself and the Investment Bank Special Administration Regulations 2011, respectively. This potentially creates certain issues when it comes to the BTS, because the on-shoring of the BRRD refers to various provisions of the Banking Act, some of which could, as a result of this paper, be interpreted as applying to out-of-scope clearing houses or investment firms, which are not currently subjected to BRRD provisions. **We would therefore suggest the following additional text to clarify the scope beyond doubt, in a way that is consistent with the consultation paper:**

"For the avoidance of doubt, the Bank Recovery and Resolution BTS does not apply to central counterparties (even though the Banking Act applies to them by virtue of section 89B of the Banking Act) or investment firms (even though the Banking Act applies solely to them by virtue of the Investment Bank Special Administration Regulations 2011) and any references herein to the Banking Act shall be interpreted accordingly as being inapplicable to organisations which fall under the Banking Act only as a result of those provisions."

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