



HM TREASURY

Implementation of EU Directive 2009/44/EC on settlement finality and financial collateral arrangements

summary of responses

December 2010



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1

Introduction

1.1 On 6 May 2009, the European Parliament and Council adopted Directive 2009/44/EC (the “Amending Directive”) which amends Directive 98/26/EC on settlement finality in payment and securities arrangements systems (the “SFD”) and Directive 2002/47/EC on financial collateral arrangements (“the FCD”). Member states have until 30 December 2010 to adopt and publish their implementing measures, which are to apply from 30 June 2011.

1.2 Key changes made by the Amending Directive include:

- Introducing the concept of interoperable systems into the SFD. The Amending Directive makes changes to ensure interoperable systems (i.e. clearing, settlement or payment systems which link with each other) are brought into the regime, with relevant protections clarified or extended where appropriate.
- Bringing credit claims into the scope of the FCD. The Amending Directive adds credit claims (i.e. individual loans) to the collateral types eligible for the FCD’s protections.

Consultation

1.3 HM Treasury published a consultation document on 13 August seeking views on its proposals for implementation of the Amending Directive. The document also sought views on certain issues relating to the wider treatment of floating charges. The consultation document can be viewed at www.hm-treasury.gov.uk/consult_amending_directive_implementation.htm

1.4 The consultation closed on 29 October. Sixteen responses were received, from law firms, members of the public, trade associations, a clearing and settlement firm, and banks. We are grateful for all responses received. Chapter 2 of this document summarises responses to the questions posed in the consultation document and other comments received.

1.5 A list of respondents to the consultation is provided at Annex A.

1.6 The revised Statutory Instrument is at Annex B.

1.7 The Impact Assessment is at Annex C.

2

Responses to the consultation

2.1 This chapter summarises responses to the seven questions posed in the consultation document. Not all respondents commented on all questions. It also covers other issues raised by respondents and identifies those issues, not necessary to implement the Amending Directive, which will be given separate further consideration.

2.2 In view of the varied and very detailed nature of some comments it is not practical to list every comment received. Therefore this Chapter aims to give the overall flavour of responses and references the more substantive comments.

2.3 References to “the 1999 Regulations” mean the Financial Markets and Insolvency (Settlement Finality) Regulations 1999. References to “the 2003 Regulations” mean the Financial Collateral Arrangements (No 2) Regulations 2003.

Question:

What costs (size and nature) will system operators need to incur in order to achieve compliance with the requirement to coordinate their rules on irrevocability?

2.4 One respondent commented that a designated system and the linked system would be sensitive to the systemic, legal and other risks created by any failure to co-ordinate their respective rules on the moment of entry of a transfer order and its irrevocability. Therefore, due to the natural development of arrangements, there would be no expectation of material costs. Another respondent commented that the definition of “interoperable systems” should be supplemented with a “system” definition.

Response

2.5 We have noted the comments about costs. With regard to definitions, we note that section 2(3) of the 1999 Regulations applies the same meanings for expressions used in the SFD to the same expressions used in the Regulations. The SFD includes a definition for “system”.

Question 2

Do you agree that electronic money institutions should be brought within the scope of the Settlement Finality regulations?

2.6 The majority of the respondents did not provide comments for this question, though those that did were generally in agreement. One respondent thought that “payment institutions” should also be brought within scope so that they can be participants in designated systems.

Response

2.7 The extension of the definition of “institution” to include “payment institution” would go further than the SFD, as amended – the definition of “institution” is set out in the directive and does not include “payment institutions”.

Question 3

Do you have any comments on regulation 4 of the draft SI?

2.8 This question specifically referred to amending the Banking and Diligence (Scotland) Act 2007 in order that Scottish floating charges which are created or arise under a security financial collateral arrangement are created when the document creating the charge is executed, not when the charge is registered on the Scottish register of floating charges. The question was addressed by four respondents.

2.9 The majority of respondents agreed that the provisions of the Banking and Diligence (Scotland) Act 2007 should be disapplied in relation to Scottish floating charges which form part of a security financial collateral arrangement. One respondent suggested that further amendments were required to both the 1999 Regulations and the 2003 Regulations to ensure that they are effective under Scottish law.

Response

2.10 Following discussions with the Scottish Executive we have amended the SI so that the provisions of the Banking and Diligence (Scotland) Act 2007 are modified in their application to this class of floating charges, rather than amended. We have also amended the 1999 Regulations and the 2003 Regulations to improve the implementation of the Settlement Finality Directive and the Financial Collateral Arrangements Directive under Scottish law.

Question 4

Do you agree that provision should be made to ensure that foreign insolvency orders or acts cannot be enforced by the UK courts in circumstances where an equivalent order made by a court in the UK could not be enforced because of the protections given in the 2003 Regulations?

2.11 This question attracted three responses. It was noted that draft regulation 3(3) and new regulation 15A of the 2003 Regulations may also affect the Cross Border Insolvency Regulations 2006 which implemented UNCITRAL Model Law.

2.12 One respondent challenged the assumption in the consultation paper (paragraph 2.19), commenting that even though it is unlikely that an English court would recognise or give effect to an order or act made by a foreign court which would allow a financial collateral arrangements to be set aside or prejudiced in circumstances in which there could have been no equivalent order or act in proceedings in the UK, it is prudent to make provision in the 2003 regulations to stop this from happening.

2.13 It was also suggested that the proposed provision might lead the unwary to assume that English law would necessarily govern proceedings.

Response

2.14 Regulation 15A, of the 2003 Regulations, as inserted by the Amending S.I. ensures that an English court will not give effect to an order made by a foreign court in insolvency proceedings if, in the same circumstances, that order could not be made in the UK because of the 2003 Regulations. We do consider that this provision will be beneficial rather than misleading, and we do not propose to amend it.

Question 5

Do you agree that credit claims should not be exempted from the protections of the FCD where the debtor is a consumer or small business?

2.15 As stated in the consultation document, article 2(4)(d) of the Amending Directive gives Member States the option (other than where the collateral giver or taker is a central bank) of excluding credit claims from the FCD regime where the debtor covered by the credit claim is a consumer or a small micro business. The consultation document explained that we did not propose to exercise this option.

2.16 We received four responses to this question, all agreeing with HM Treasury's proposed approach.

Response

2.17 We note the comments made, and do not propose to exercise this Member State option.

Question 6

Do you consider that floating charges which are "collateral security charges" within the meaning of the 1999 Regulations should be brought within the scope of the 2003 Regulations?

2.18 We received four responses to this question. The idea of "collateral security charges" being brought within the scope of the 2003 regulations was generally welcomed. One respondent, though welcoming the proposal, commented that it does not go far enough, suggesting (amongst other things) that all charges which form part of a wholesale arrangement should be brought within scope, and that a new and broader definition of control should be included.

2.19 It was also emphasised that uncertainty currently exists about whether floating charges over financial collateral currently fall within the definition of security financial collateral arrangements in the 2003 regulations. A number of consultees expressed concern over the effect of the judgment in *Gray v G.T.P Group*, and requested that the 2003 Regulations should be amended to include a definition of "possession".

Response

2.20 We note that there is a general consensus amongst respondents that current uncertainty around floating charges should be addressed. We have included a definition making it clear that "possession" for the purposes of the 2003 Regulations includes the case where financial collateral has been credited to an account of the collateral taker, or of someone acting on their behalf. The only proviso is that the rights of the collateral provider in relation to such collateral must be limited to rights to substitute financial collateral of the same (or greater) value, or to withdraw excess collateral, in line with the intention of the FCD that only those financial collateral arrangements providing for some form of dispossession should be within the scope of the directive.

2.21 We will give further consideration to wider issues raised around the treatment of floating charges. As some respondents acknowledged, the issues cannot be given proper consideration within the timescale imposed by the immediate need to make amendments to implement the Amending Directive, and can be considered separately to those amendments.

Question 7

Would you support the extension of the 1999 regulations to cover third country settlement systems? If so, what criteria should govern which systems are protected?

2.22 We received five responses to this question, with all five respondents supporting the extension of the 1999 regulations to cover third country settlement systems.

Response

2.23 We note responses on this point, and are considering the detailed comments, but are not addressing this issue in the current amending regulations as more work is necessary to determine what criteria would be used to recognise non-EEA systems.

Additional issues raised

Alignment

2.24 One respondent suggested that there were gaps in the current protections applying under the 2003 Regulations and the 1999 Regulations, and that this should be addressed so that, for example, the same protections against insolvency risk are provided by both sets of regulations.

Response

2.25 The question of whether collateral security charges should receive exactly the same protections as financial collateral arrangements does not need to be addressed for the purposes of implementing the Amending Directive, but can be given further consideration.

Continuity provisions

2.26 One respondent requested that provision should be made to clarify that the enactment of the amending regulations do not affect in any way the protections enjoyed by those systems which are already “designated systems” under the existing regulations.

Response

2.27 We have provided, for the avoidance of doubt, in regulation 3, that no designating order in force in relation to designated system is affected by the Amending Regulations. It is also made clear that it is not necessary for a system operator to apply for an amended designation order because of the 1999 Regulations have been amended. As this puts the status of existing designated systems beyond doubt, we do not consider that it is necessary to make further “continuity” provision in relation to transfer orders.

Increase in links between systems.

2.28 It was proposed that provisions intended to ensure that a UK designated system is protected from the insolvency of a participant in an interoperable system in relation to that system as well as one of its own participants should be made fully effective by the extension of their application beyond “designated systems”.

Response

2.29 In a number of cases these suggestions have been adopted. However, in some cases the drafting suggestions proposed would result in extension of the protections given by the regulations, giving the interoperable system full benefit of the protections given under the Regulations (in relation to transfer orders, or action taken under their default arrangements, for

example). This is not the intention of the Regulations. The amendments proposed amendments are intended to insulate the designated system from the effects of the insolvency of a participant in an interoperable system, but not to give the interoperable system precisely the same protections given to the designated system.

Administrator's and liquidator's remuneration, expenses and liabilities and moratorium expenses

2.30 A number of consultees suggested that provisions of the Insolvency Act 1986 relating to the payment of these expenses, remuneration and liabilities should be disapplied in relation to financial collateral arrangements.

Response

2.31 These provisions will be disapplied by the Amending Regulations (see regulation 4(6)-(9)).

Disapplication of section 136 of the Law of Property Act 1925

2.32 One respondent commented that in order to comply with the FCD the 2003 Regulations should be amended in order to disapply in its entirety section 136 of the Law of Property Act 1925.

Response

2.33 With regard to section 136, we note that Article 3 of the FCD does provide for "the performance of a formal act, such as registration or notification, for purposes of perfection, priority, enforceability or admissibility in evidence against the debtor or third parties". We consider that section 136 is an important safeguard for debtors' rights. If it was disapplied, those safeguards would be compromised. We do not therefore propose to disapply this provision.

Indirect participants

2.34 Several respondents commented that it is impractical for a system such as CREST to know all the "indirect participants" that may access the system through arrangements with direct participants. The requirement to know the identity of an indirect participant should be amended by providing that it can be satisfied if the identity is made known the system operator under its "default arrangements".

Response

2.35 The definition of "indirect participant" is set out in the SFD. An institution, central counterparty, settlement agent, clearing house or system operator which has a contractual relationship with a participant cannot be an indirect participant unless its identity is known to the system operator.

Next Steps

2.36 Member States have until 30 December 2010 to adopt and publish implementing measures for the Amending Directive. The amending SI will be laid before Parliament before the Christmas recess.

2.37 As explained previously, this instrument will not address all issues raised in the consultation – only those measures necessary to implement the Amending Directive – and the Treasury will give further consideration where appropriate to other issues.



List of respondents

1. Scottish Law Commission
2. Citi
3. Clifford Chance
4. Financial Law Committee of the City of London Law Society
5. ICMA
6. HSBC
7. Tods Murray
8. Linklaters LLP
9. Euroclear UK & Ireland.
10. Andrew McKnight
11. British Bankers Association
12. Association of Global Custodians
13. Financial Markets Law Committee
14. Peter Bloxham

B

Statutory Instrument

2010 No.

FINANCIAL SERVICES AND MARKETS

**The Financial Markets and Insolvency (Settlement Finality and
Financial Collateral Arrangements) (Amendment) Regulations
2010**

Made - - - - ***
Laid before Parliament ***
Coming into force - - 6th April 2011

The Treasury are a government department designated(a) for the purposes of section 2(2) of the European Communities Act 1972(b) in relation to measures—

- (a) relating to investment firms and to the provision of investment services and to the operation of regulated markets and clearing or settlement systems;
- (b) relating to payment systems; and
- (c) relating to the provision of cash, securities and interests in securities as collateral, and to collateral security provided to the central banks of Member States or to the European Central Bank.

These Regulations make provision for a purpose mentioned in section 2(2) of the European Communities Act 1972 and it appears to the Treasury that it is expedient for the reference to Council Regulation (EC) No. 44/2001 of 22nd December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters to be construed as a reference to that instrument as amended from time to time.

The Treasury make these Regulations in exercise of the powers conferred by section 2(2) of, and paragraph 1A of Schedule 2 to, the European Communities Act 1972(c)

Citation and commencement

1. These Regulations may be cited as the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010, and come into force on 6th April 2011.

(a) S.I. 1993/2661, S.I. 1998/2793 and S.I. 2003/1888.
(b) 1972 c. 68. Section 2(2), and Schedule 2 to the 1972 Act were amended by section 27 of the Legislative and Regulatory Reform Act 2006 (c.51); and by section 3 of, and the Schedule to, the European Union (Amendment) Act 2008 (c. 7).
(c) Paragraph 1A of Schedule 2 was inserted by section 28 of the Legislative and Regulatory Reform Act 2006 (2006 c.51).

Amendment of the Financial Markets and Insolvency (Settlement Finality) Regulations 1999

2.—(1) The Financial Markets and Insolvency (Settlement Finality) Regulations 1999^(a) are amended as follows.

(2) In regulation 2(1)—

(a) insert each of the following definitions at the appropriate place—

“business day” shall cover both day and night-time settlements and shall encompass all events happening during the business cycle of a system;”

“credit claims” means pecuniary claims arising out of an agreement whereby a credit institution grants credit in the form of a loan;”

“interoperable system” in relation to a system (“the first system”), means a second system whose system operator has entered into an arrangement with the system operator of the first system that involves cross-system execution of transfer orders;”

“system operator” means the entity or entities legally responsible for the operation of a system. A system operator may also act as a settlement agent, central counterparty or clearing house;

(b) in the definition of “central counterparty”, omit “designated”;

(c) in the definition of “clearing house”, omit “designated”;

(d) in the definition of “collateral security”—

(i) after “including” insert “credit claims and”;

(ii) in sub-paragraph (a), omit “designated” both times it occurs;

(e) in the definition of “credit institution” for “Article 4(1)(a)” substitute “Article 4(1)”;

(f) in the definition of “default arrangements”—

(i) after “designated system” insert “or by a system which is an interoperable system in relation to that system”; and

(ii) after “participant” insert “or a system operator of an interoperable system”;

(g) for the definition of “indirect participant” substitute—

“indirect participant” means an institution, central counterparty, settlement agent, clearing house or system operator—

(a) which has a contractual relationship with a participant in a designated system that enables the indirect participant to effect transfer orders through that system, and

(b) the identity of which is known to the system operator;”;

(h) in the definition of “institution”—

(i) insert after sub-paragraph (a)—

“(a) an electronic money institution within the meaning of Article 2.1 of Directive 2009/110/EC of the European Parliament and of the Council of 16 September 2009 on the taking up, pursuit and prudential supervision of the business of electronic money institutions amending Directives 2005/60/EC and 2006/48/EC and repealing Directive 2000/46/EC^(b);

(ii) omit the word “designated”;

(i) in the definition of “participant”, after sub-paragraph (a), insert—

“(a) a system operator;”

(j) in the definition of “relevant office-holder”—

(i) at the end of paragraph (c), omit “or”;

^(a) S.I. 1999/2979, amended by S.I. 2001/3929, 2002/1555, 2003/2096, 2006/50, 2006/3221, 2007/832, 2007/108, 2007/126, 2007/1655, 2009/1972.

^(b) OJ L 267, 10.10.2009, p7.

- (ii) at the end of paragraph (d), insert “or”;
- (iii) after paragraph (d), insert—
 - “(e) any person appointed pursuant to insolvency proceedings of a country or territory outside the United Kingdom;”;
- (k) in the definition of “settlement account” omit “designated”;
- (l) in the definition of “settlement agent”, omit “designated”;
- (m) in the definition of “the Settlement Finality Directive” insert at the end “as amended by Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements as regards linked systems and credit claims(a)”;
- (n) in the definition of “transfer order” after “a central bank” insert “, a central counterparty”;
- (o) for the definition of “winding-up”, substitute—
 - “winding-up” means—
 - (a) winding up by the court or creditors’ voluntary winding up within the meaning of the Insolvency Act 1986(b) or the Insolvency (Northern Ireland) Order 1989(c) (but does not include members’ voluntary winding up within the meaning of that Act or that Order);
 - (b) sequestration of a Scottish partnership under the Bankruptcy (Scotland) Act 1985(d);
 - (c) bank insolvency within the meaning of the Banking Act 2009(e).”
- (3) In regulation 4(1), after “designated system” insert “and identifying the system operator of that system”.
- (4) In regulation 5—
 - (a) in paragraph (2), after “charge” insert “the system operator of”;
 - (b) in paragraph (3)(b)—
 - (i) for “system continues” substitute “system and its system operator continue”;
 - (ii) for “is complying” substitute “are complying”;
 - (iii) for “it is subject” substitute “they are subject”.
- (5) In regulation 7(1)(b)—
 - (a) after “the system” insert “or the system operator of that system”;
 - (b) for “it is subject” substitute “they are subject”.
- (6) In regulation 7(4), after “consent of the” insert “system operator of the”.
- (7) In regulation 8(2) insert at the end “and to the system operator of that system”.
- (8) In regulation 9—
 - (a) in paragraph (1), after “to the designated system” insert “and to the system operator of that system”;
 - (b) after paragraph (1), insert—
 - “(2) Where a designating authority, in accordance with paragraph (1), treats an indirect participant as a participant in a designated system, the liability of the participant through which that indirect participant passes transfer orders to the designated system is not affected.”.

(a) OJ L 146, 10.6.2009, p37.
 (b) 1986 c. 45.
 (c) S.I. 1989/2405 (N.I. 19).
 (d) 1985 c. 66.
 (e) 2009 c. 1.

- (9) In regulation 10—
- (a) for paragraph (1), substitute—

“(1) The system operator of a designated system shall, when that system is declared to be a designated system, provide to the designating authority in writing a list of the participants (including the indirect participants) in the designated system and shall give written notice to the designating authority of any amendment to the list within seven days of such amendment.”;
 - (b) in paragraphs (2), (3), (4) and (5), for “a designated system” in each place where it occurs substitute “the system operator of a designated system”.
- (10) In regulation 13—
- (a) for paragraph (2)(a), substitute—

“(a) insolvency proceedings in respect of a participant in a designated system, or of a participant in a system which is an interoperable system in relation to that designated system;”
 - (b) at the end of paragraph (2)(b), insert “and”;
 - (c) after paragraph (2)(b), insert—

“(c) insolvency proceedings in respect of a system operator of a designated system or of a system which is an interoperable system in relation to that designated system;”
 - (d) after paragraph (3), insert—

“(4) References in this Part to “insolvency proceedings” shall include—

 - (a) bank insolvency under Part 2 of the Banking Act 2009; and
 - (b) bank administration under Part 3 of the Banking Act 2009;”.
- (11) In regulation 14—
- (a) in paragraph (1), after “insolvent estate” insert “or with the law relating to other insolvency proceedings of a country or territory outside the United Kingdom”;
 - (b) in paragraph (1)(d), after “designated system” insert “or in a system which is an interoperable system in relation to that designated system”;
 - (c) in paragraph (2)(b) for “its default arrangements” substitute “the default arrangements of a designated system”;
 - (d) in paragraph (2)(c), after “designated system” insert “or in a system which is an interoperable system in relation to that designated system”;
 - (e) for paragraph (5)(a)(iv), substitute—

“(iv) paragraph 100(3) of Schedule B1 to the Insolvency (Northern Ireland) Order 1989, Article 31(4) of that Order, as it has effect by virtue of Article 4(1) of the Insolvency (Northern Ireland) Order 2005, and Article 50 of the Insolvency (Northern Ireland) Order 1989; and”;
 - (f) in paragraph (5)(a)(v) after “2006” insert “(including that section as applied or modified by any enactment made under the Banking Act 2009)”;
 - (g) in paragraph (6), after “participant” insert “, system operator”.
- (12) In regulation 15(1), after “default arrangements” insert “of a designated system”.
- (13) In regulation 20—
- (i) in paragraph (1)(a), for “in respect of that participant” substitute—

“in respect of—

 - (i) that participant;
 - (ii) a participant in a system which is an interoperable system in relation to the designated system; or
 - (iii) a system operator which is not a participant in the designated system, or”;

- (b) in paragraph (1)(b) and (c), after “that participant” insert “, a participant in a system which is an interoperable system in relation to the designated system or a system operator of that designated system”;
 - (c) in paragraph (2)—
 - (i) in sub-paragraph (a), for “same day” substitute “same business day of the designated system”;
 - (ii) in sub-paragraph (b)—
 - (aa) for “the settlement agent, the central counterparty or the clearing house” substitute “the system operator”;
 - (bb) for “the time of settlement of the transfer order” substitute “the time the transfer order became irrevocable”;
 - (d) in paragraph (3), for “the relevant settlement agent, central counterparty or clearing house” substitute “the relevant system operator”.
- (14) In regulation 22(1), for “the system” substitute “the system operator of that designated system”.
- (15) In regulation 23(a)—
- (a) after “a participant” insert “, a system operator”;
 - (b) after “the participant” insert “, the system operator”.
- (16) In regulation 26—
- (a) in paragraph (1)(b), omit “in connection with a designated system”;
 - (b) for paragraph (2)(b), substitute—
 - “(b) “equivalent overseas security” means any realisable assets provided under a charge or a repurchase or similar agreement, or otherwise (including credit claims and money provided under a charge)—
 - (i) for the purpose of securing rights and obligations potentially arising in connection with such a system, or
 - (ii) to a central bank for the purpose of securing rights and obligations in connection with its operations in carrying out its functions as a central bank.”.
- (17) In the Schedule—
- (a) in paragraph 1, insert at the end—
 - “(5) An arrangement entered into between interoperable systems shall not constitute a system.”;
 - (b) in paragraph 3, for “system” in both places where it occurs, substitute “system operator”;
 - (c) in paragraph 4, for “the system”, substitute “the system operator”;
 - (d) in paragraph 5, after sub-paragraph (1), insert—
 - “(1A) Where the system has one or more interoperable systems, the rules required under paragraph (1)(a) and (b) shall, as far as possible, be co-ordinated with the rules of those interoperable systems.
 - (1B) The rules of the system which are referred to in paragraph (1)(a) and (b) shall not be affected by any rules of that system’s interoperable systems in the absence of express provision in the rules of the system and all of those interoperable systems.”.

Existing designations

3. Nothing in these Regulations affects any designation order in force under the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 in relation to a designated system, and no system operator shall be required to apply for an amended designation order in consequence only of these Regulations.

Amendment of the Financial Collateral Arrangements (No. 2) Regulations 2003

4.—(1) The Financial Collateral Arrangements (No. 2) Regulations 2003^(a) are amended as follows.

(2) In regulation 3—

(a) renumber the existing provision as paragraph (1);

(b) in paragraph (1)—

(i) insert in the appropriate place—

“credit claims” means pecuniary claims which arise out of an agreement whereby a credit institution, as defined in Article 4(1) of Directive 2006/48/EC of the European Parliament and of the Council relating to the taking up and pursuit of the business of credit institutions (recast), including the institutions listed in Article 2 of that Directive, grants credit in the form of a loan^(b)”;

(ii) in the definition of “financial collateral”, for “cash or financial instruments” substitute “cash, financial instruments or credit claims”;

(iii) in the definition of “reorganisation measures”, in sub-paragraphs (c) and (d), after “Scottish partnership,” on each occasion it occurs, insert “a protected trust deed within the meaning of”;

(iv) in the definitions of “security financial collateral arrangement” and “security interest”—

(aa) for “equivalent financial collateral” substitute “financial collateral of the same or greater value”,

(bb) after “excess financial collateral” insert “or to collect the proceeds of credit claims until further notice”;

(v) for the definition of “winding up proceedings” substitute—

““winding-up proceedings” means—

(a) winding up by the court or voluntary winding up within the meaning of the Insolvency Act 1986 or the Insolvency (Northern Ireland) Order 1989;

(b) sequestration of a Scottish partnership under the Bankruptcy (Scotland) Act 1985^(c);

(c) bank insolvency within the meaning of the Banking Act 2009.”;

(c) after paragraph (1), insert—

“(2) For the purposes of these Regulations “possession” of financial collateral in the form of cash or financial instruments includes the case where financial collateral has been credited to an account in the name of the collateral-taker or a person acting on his behalf (whether or not the collateral-taker, or person acting on his behalf, has credited the financial collateral to an account in the name of the collateral-provider on his, or that person’s, books) provided that any rights the collateral-provider may have in relation to that financial collateral are limited to the right to substitute financial collateral of the same or greater value or to withdraw excess financial collateral.”.

(3) In regulation 4—

(a) in paragraph (4), insert at the end “or, in Scotland, to relation to any charge created or arising under a financial collateral arrangement”;

(b) in paragraph (5), omit “security” both times it occurs.

(4) In regulation 5, omit “security” both times it occurs.

(a) S.I. 2003/3226. These Regulations have been amended by S.I. 2009/2462.

(b) OJ No L 177, 30.6.2006, p1 – 200.

(c) 1985 c. 66.

(5) In regulation 6A(a), insert at the end, “or, in Scotland, to any charge created or arising under a financial collateral arrangement.”

(6) In regulation 8—

- (a) in paragraph (1)(a), omit “and”;
- (b) after paragraph (1)(a), insert—
 - “(aa) paragraph 65(2) (distribution);”;
- (c) at the end of paragraph (1)(b), insert “and”;
- (d) after paragraph (1)(b), insert—
 - “(c) paragraph 99(3) and (4) (administrator’s remuneration, expenses and liabilities).”
- (e) in paragraph (3)—
 - (i) at the end of sub-paragraph (b), insert “and”;
 - (ii) after sub-paragraph (b), insert—
 - “(c) section 19(4) and 19(5) (administrator’s remuneration, expenses and liabilities).”

(7) In regulation 9—

- (a) at the end of paragraph (1)(a), omit “and”;
- (b) after paragraph (1)(b), insert—
 - “(c) Article 31(4) and (5) (administrator’s remuneration, expenses and liabilities); and
 - (d) Paragraphs 44(2), 45 (restriction on enforcement of security), 66(2) (distribution), 71, 72 (power of administrator to deal with charged property), 100(3) and (4) (administrator’s remuneration, expenses and liabilities) of Schedule B1 to the Order(b).”.

(8) In regulation 10—

- (a) after paragraph (2), insert—
 - “(2A) Sections 40 (or in Scotland, sections 59, 60(1)(e)) and 175 of the Insolvency Act 1986 (preferential debts) shall not apply to any debt which is secured by a charge created or otherwise arising under a financial collateral arrangement.
 - (2B) Section 176ZA of the Insolvency Act 1986 (expenses of winding up)(c) shall not apply in relation to any claim to any property which is subject to a disposition or created or otherwise arising under a financial collateral arrangement.”;
- (b) in paragraph (4), for “being wound up” substitute “subject to winding-up proceedings”; and
- (c) in paragraph (6) after “floating charge”, insert “(including that section as applied or modified by any enactment made under the Banking Act 2009)”.

(9) In regulation 11—

- (a) after paragraph (1), insert—
 - “(1A) Article 50 of that Order (payment of debts out of assets subject to floating charge) shall not apply (if it would otherwise do so), to any charge created or otherwise arising under a financial collateral arrangement.”;
- (b) after paragraph (2), insert—
 - “(2A) Articles 149 of that Order (preferential debts) and 150ZA (expenses of winding up)(d) shall not apply (if they would otherwise do so) to any charge created or otherwise arising under a financial collateral arrangement.”.

(10) In regulation 12—

(a) Regulation 6A was inserted by S.I. 2009/2462.
(b) Schedule B1 was inserted by S.I. 2005/1455 (N.I. 10).
(c) Section 176ZA was inserted by the Companies Act 2006 (c.46), section 1282.
(d) Article 150ZA was inserted by the Companies Act 2006, section 1282.

- (a) in paragraph (2)(b), after “winding-up of” insert “or, in Scotland, a petition for winding-up proceedings in relation to”;
 - (b) in paragraph (3)—
 - (i) in paragraph (a), after “winding-up order” insert “or, in the case of a Scottish partnership, the award of sequestration”, and
 - (ii) in paragraph (b) after “otherwise”, insert “or, in the case of a Scottish partnership, when a protected trust deed is entered into”;
 - (c) in paragraph (4) after “set-off”) insert “, or in Scotland, any rule of law with the same or similar effect to the effect of these Rules”.
- (11) In regulation 13(3)—
- (a) in paragraph (a) after “winding-up order” insert “or, in the case of a Scottish partnership, the award of sequestration”; and
 - (b) in paragraph (b) after “otherwise” insert “or, in the case of a Scottish partnership, the date of registration of a protected trust deed”.
- (12) In regulation 15—
- (a) after “goes into liquidation” insert “or administration”;
 - (b) for “section 49(3) of the Bankruptcy (Scotland) Act 1985 as applied by rule 4.16(1)(c) of those rules (claims in foreign currency)” substitute “the provisions of the Bankruptcy (Scotland) Act 1985 referred to in those rules and such rules and provisions as applied by rule 2.41 of the Insolvency (Scotland) Rules 1986”.
- (13) After regulation 15, insert—

“Insolvency proceedings in other jurisdictions

15A.—(1) The references to insolvency law in section 426 of the Insolvency Act 1986 (co-operation between courts exercising jurisdiction in relation to insolvency) include, in relation to a part of the United Kingdom, this Part of these Regulations and, in relation to a relevant country or territory within the meaning of that section, so much of the law of that country or territory as corresponds to this Part.

(2) A court shall not, in pursuance of that section or any other enactment or rule of law, recognise or give effect to—

- (a) any order of a court exercising jurisdiction in relation to insolvency law in a country or territory outside the United Kingdom, or
- (b) any act of a person appointed in such a country or territory to discharge any functions under insolvency law,

in so far as the making of the order or the doing of the act would be prohibited by this Part in the case of a court in England and Wales or Scotland, the High Court in Northern Ireland or a relevant office holder.

(3) Paragraph (2) does not affect the recognition of a judgment required to be recognised or enforced under or by virtue of the Civil Jurisdiction and Judgments Act 1982^(a) or Council Regulation (EC) No 44/2001 of 22nd December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters^(b), as amended from time to time and as applied by the Agreement made on 19th October 2005 between the European Community and the Kingdom of Denmark on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters^(c).”.

- (14) In regulation 16—
- (a) after paragraph (3), insert—

(a) 1982 c. 27.
 (b) OJ L 12, 16.1.2001, p1-23.
 (c) OJ L 299 16.11.2005, p62.

“(3A) In Scotland, paragraphs (1) and (3) apply to title transfer financial collateral arrangements as they apply to security financial collateral arrangements.”;

(b) at the end insert—

“(5) This regulation does not apply in relation to credit claims.”.

(15) For regulation 17, substitute—

“Appropriation of financial collateral under a security financial collateral arrangement

17.—(1) Where a security interest is created or arises under a security financial collateral arrangement on terms that include a power for the collateral-taker to appropriate the financial collateral, the collateral-taker may exercise that power in accordance with the terms of the security financial collateral arrangement, without any order for foreclosure from the courts (and whether or not the remedy of foreclosure would be available).

(2) Upon the exercise by the collateral-taker of the power to appropriate the financial collateral, the equity of redemption of the collateral-provider shall be extinguished and all legal and beneficial interest of the collateral-provider in the financial collateral shall vest in the collateral taker.”.

Registration of charges: Scotland

5.—(1) The Bankruptcy and Diligence etc. (Scotland) Act 2007^(a) has effect in relation to floating charges which are created by or otherwise arise under a financial collateral arrangement with the following modifications.

(2) In section 38 (creation of floating charges)—

(a) in subsection (3), after “subsection (3A)” insert “, subsection (3B)”;

(b) after subsection (3A), insert—

“(3B) If a floating charge is created or otherwise arises under a security financial collateral arrangement, it is created when the document granting the floating charge is executed by the company granting the charge and without registration in the Register of Floating Charges.”.

(3) In section 39 (advance notice of floating charges), for subsection (4), substitute—

“(4) This section does not apply—

(a) where a company proposes to grant a floating charge in favour of a central institution;

(b) where a floating charge is created or otherwise arises under a security financial collateral arrangement.”.

(4) In section 42 (assignment of floating charges), after subsection (4), insert—

“(5) This section does not apply to the assignment (whether in whole or to a specified extent) of a floating charge which was created or otherwise arises under a security financial collateral arrangement.”.

(5) In section 43 (alteration of floating charges), in subsection (4A)—

(a) at the end of paragraph (b), insert “, or”;

(b) after paragraph (b), insert—

“(c) the floating charge was created or otherwise arises under a security financial collateral arrangement.”.

(6) In section 44 (discharge of floating charges), for subsection (4), substitute—

(a) 2007 asp 3, as amended by the Banking Act 2009 (c.1) s. 253. The provisions modified by these Regulations have not yet been commenced.

“(4) This section does not apply where the floating charge to be discharged (whether in whole or to a specified extent)—

- (a) is or has been held by a central institution, or
- (b) was created or otherwise arises under a security financial collateral arrangement.”.

(7) In section 47 (interpretation), after the definition of “fixed security”, insert—

“security financial collateral arrangement” has the same meaning as in regulation 3 of the Financial Collateral Arrangements (No. 2) Regulations 2003;”.

	<i>Name</i>
	<i>Name</i>
Date	Two of the Lords Commissioners of Her Majesty’s Treasury

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations implement Directive 2009/44/EC of the European Parliament and of the Council amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements (OJ L146, 10.6.09, p 37). The Directive seeks to make further provision for linked or “interoperable” systems, and ensure that credit claims may be used as financial collateral.

Regulation 2 amends the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (S.I. 1999/2979) (“the 1999 Regulations”). Paragraph (2) amends the definition of “collateral security” to include credit claims, and defines credit claims. It also amends the definitions of participant and indirect participant, adds new definitions of “business day”, “interoperable system” and “system operator”, and amends a number of definitions to provide for interoperable systems.

Paragraphs (3) to (7) and (9) amend regulations 4 to 8 and 10 of the 1999 Regulations so that obligations previously imposed on the designated system itself are now imposed on the system operator of that system. Paragraph (8) clarifies the liability of a participant through which an indirect participant passes transfer orders to the designated system.

Paragraphs (10) and (11) amend regulations 13 and 14 of the 1999 Regulations so that the protection given in relation to insolvency proceedings in respect of a participant in a designated system is now extended to insolvency proceedings in respect of the system operator of a designated system, and in respect of participants in interoperable systems of a designated system.

Paragraph (13) amends regulation 20 so that modifications made to the law of insolvency cease to apply to a transfer order entered into a designated system following the insolvency not only of a participant in that system (and of an interoperable system), but also of a system operator who is not a participant in the system, unless the transfer order is carried out on the same business day as the insolvency and the system operator did not have notice of it when the order was settled.

Paragraph (14) amends regulation 22 to require the system operator of a designated system to be informed when a court makes an insolvency order in relation to a participant in a designated system. Paragraph (15) amends regulation 23 so that the rule in that regulation for determining the applicable law in relation to securities held as collateral security also applies in relation to securities provided to a system operator.

Paragraph (16) amends regulation 26 to ensure that Part 3 of the Regulations applies to equivalent overseas security provided to a central bank just as it applies to such security provided in connection with a designated system, and amends the definition of “equivalent overseas security” accordingly.

Paragraph (17) amends paragraphs 1, 3 and 4 of the Schedule to the 1999 Regulations to clarify what is a “system” for the purpose of the Regulations. It also amends paragraph 5 of the Schedule

to require the rules of interoperable systems in relation to the finality and revocation of a transfer order to be co-ordinated as far as possible.

Regulation 3 provides, for the avoidance of doubt, that these Regulations do not affect the designation of any existing designated system.

Regulation 4 amends the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226) (“the 2003 Regulations”). Paragraph (2) inserts a new definition of “credit claims”, amends the definitions of “financial collateral” and “security financial collateral arrangement” to include credit claims which are provided as financial collateral and inserts a definition of “possession” for the purposes of the Regulations.

Paragraphs (3) to (12) disapply a number of provisions of insolvency law in relation to financial collateral arrangements, and make some consequential amendments to reflect Scottish insolvency law.

Paragraph (13) ensures that an insolvency order made by a foreign court, or an act of a foreign insolvency office-holder, cannot be enforced by a UK court if such an order or act could not be made by a UK court or office-holder.

Paragraph (14) provides that the provision in the 2003 Regulations on the right of use apply to Scottish title transfer financial collateral arrangements in the same way as they apply to security financial collateral arrangements, and ensures that these provisions do not apply to credit claims. Paragraph (15) clarifies the power of appropriation in relation to security financial collateral arrangements.

Regulation 5 modifies the Bankruptcy and Diligence etc. (Scotland) Act 2007 (asp 3) in its application to floating charges which are created or arise under a financial collateral arrangement to ensure that such charges are created when the document creating the charge is executed, not when the charge is registered on the Scottish Register of Floating Charges, and makes further consequential amendments in relation to such charges.

An Impact Assessment of the effect of this instrument on the costs of business has been prepared and may be obtained from the Financial Regulation Strategy Team, HM Treasury, 1 Horse Guards Road, London SW1A 2HQ. It is also available on HM Treasury’s website (www.hm-treasury.gov.uk), and is annexed to the Explanatory Memorandum which is available alongside this instrument on www.legislation.gov.uk.

C

Impact Assessment

Title: Impact assessment of UK implementation regulations of the EU directive on settlement finality and financial collateral arrangements. Lead department or agency: HM Treasury Other departments or agencies:	Impact Assessment (IA)
	IA No:
	Date: 10/12/2010
	Stage: Development/Options
	Source of intervention: EU
	Type of measure: Secondary legislation
Contact for enquiries: Helena Forrest 0207 270 5694	

Summary: Intervention and Options

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

In April 2008 the Commission decided to amend the Settlement Finality Directive (SFD) and the Financial Collateral Arrangements Directive (FCD), bringing both Directives in line with market and regulatory developments in the post-trading area. The SFD aimed to reduce the systemic risk associated with participation in payment and securities settlement systems and FCD sought to expand on the role of collateral in SFD. These directives provide a key underpinning for the systemic robustness of the financial markets.

The Government now has to implement the directive to meet the European deadline of 30 December 2010, and is proposing to do this by amending existing domestic legislation.

What are the policy objectives and the intended effects?

The Commission produced a report in 2005 on the operation of the SFD and in 2006 on the operation of the FCD. Both reports concluded that the Directives had proved a success. However, some improvements were identified. The objectives of the amending Directive are to increase the efficiency and safety of the EU financial market and ensure a level playing field among the relevant participants, principally by facilitating the use of credit claims as collateral, ensuring the stability of settlement systems, and enhancing legal certainty. The proposed UK implementation regulations brings this into effect so UK industry stakeholders can benefit from these changes and work more effectively in a changing post trade environment.

What policy options have been considered? Please justify preferred option (further details in Evidence Base)

- 1) To amend the Financial Markets and Insolvency Regulations (1999) and the Financial Collateral Arrangements (No.2) Regulations 2003 in order to comply with the European Directive 2009/44/EC.
- 2) Not to implement.

Option 1 is preferred in view of the EU requirement to adopt and publish the laws, regulations and administrative provisions, necessary to comply with this Directive by 30 December 2010. The Directive will apply from 30 June 2011.

When will the policy be reviewed to establish its impact and the extent to which the policy objectives have been achieved?	It will be reviewed in 5 years
Are there arrangements in place that will allow a systematic collection of monitoring information for future policy review?	Yes

Ministerial Sign-off For consultation stage Impact Assessments:

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: 13/12/10

Summary: Analysis and Evidence

Policy Option 1

Description:

Impact of amending Financial Markets and Insolvency Regulations (1999) and the Financial Collateral Arrangements (No.2) Regulations 2003

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: 0.5bn	High: £35bn	Best Estimate: £15bn

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	0	0	0
High	£10m	0	£1m
Best Estimate	500k	0	500k

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

The principal monetised costs relate to system costs.

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

In the area of credit claims there could be indirect costs relating to any disadvantage suffered to creditors in the event of the insolvency of a company that has used credit claims as collateral.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	£0.5bn	TBC	£0.5bn
High	£35bn	TBC	£35bn
Best Estimate	£15bn	TBC	£15bn

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

The European Commission has estimated the potential benefits for the euro area from bringing credit claims into the scope of the Financial Collateral Directive may amount to between Euro 3.5bn and Euro 263billion. The assumptions behind this estimate are outlined in the Commission's impact assessment on its proposals (link on p 3). A simple adjustment based on the relative size of UK and Eurozone GDP would suggest this figure might be E0.5bn to E35bn for the UK.

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

The implementation of the Amending Directive should offer benefits from reduced legal risk, reduced risk of systemic disruption to the key financial architecture of London's markets and potentially reduced funding costs in the form of collateral savings and additional liquidity available to financial institutions.

Key assumptions/sensitivities/risks	Discount rate (%)	3.5
-------------------------------------	-------------------	-----

Impact on admin burden (AB) (£m):	Impact on policy cost savings (£m):	In scope
New AB:	Policy cost savings:	Yes/No
AB savings:	Net:	

Enforcement, Implementation and Wider Impacts

What is the geographic coverage of the policy/option?	United Kingdom				
From what date will the policy be implemented?	30/06/2011				
Which organisation(s) will enforce the policy?	UK courts/FSA				
What is the annual change in enforcement cost (£m)?	0				
Does enforcement comply with Hampton principles?	Yes				
Does implementation go beyond minimum EU requirements?	No				
What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent)	Traded:		Non-traded:		
Does the proposal have an impact on competition?	No				
What proportion (%) of Total PV costs/benefits is directly attributable to primary legislation, if applicable?	Costs:		Benefits:		
Annual cost (£m) per organisation (excl. Transition) (Constant Price)	Micro	< 20	Small	Medium	Large
Are any of these organisations exempt?	No	No	No	No	No

Specific Impact Tests: Checklist

Set out in the table below where information on any SITs undertaken as part of the analysis of the policy options can be found in the evidence base. For guidance on how to complete each test, double-click on the link for the guidance provided by the relevant department.

Please note this checklist is not intended to list each and every statutory consideration that departments should take into account when deciding which policy option to follow. It is the responsibility of departments to make sure that their duties are complied with.

Does your policy option/proposal have an impact on...?	Impact	Page ref within IA
Statutory equality duties¹ Statutory Equality Duties Impact Test guidance	No	
Economic impacts		
Competition Competition Assessment Impact Test guidance	No	
Small firms Small Firms Impact Test guidance	No	
Environmental impacts		
Greenhouse gas assessment Greenhouse Gas Assessment Impact Test guidance	No	
Wider environmental issues Wider Environmental Issues Impact Test guidance	No	
Social impacts		
Health and well-being Health and Well-being Impact Test guidance	No	
Human rights Human Rights Impact Test guidance	No	
Justice system Justice Impact Test guidance	No	
Rural proofing Rural Proofing Impact Test guidance	No	
Sustainable development Sustainable Development Impact Test guidance	No	

¹ Race, disability and gender Impact assessments are statutory requirements for relevant policies. Equality statutory requirements will be expanded 2011, once the Equality Bill comes into force. Statutory equality duties part of the Equality Bill apply to GB only. The Toolkit provides advice on statutory equality duties for public authorities with a remit in Northern Ireland.

Evidence Base (for summary sheets) – Notes

Use this space to set out the relevant references, evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Please fill in **References** section.

References

Include the links to relevant legislation and publications, such as public impact assessment of earlier stages (e.g. Consultation, Final, Enactment).

No.	Legislation or publication
1	EU impact assessment http://ec.europa.eu/internal_market/financial-markets/docs/proposal/impact_en.pdf
2	EU amending directive 2009/44/EC http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:146:0037:0043:EN:PDF
3	Settlement Finality Directive 98/26/EC http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:1998:166:0045:0050:EN:PDF
4	Financial Collateral Arrangements Directive 2002/47/EC http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2002:168:0043:0050:EN:PDF
5	The Financial Collateral Arrangements regulations 2003 Impact Assessment http://webarchive.nationalarchives.gov.uk/20100407010852/http://www.hm-treasury.gov.uk/d/idfca_ria_0104.pdf

Evidence Base

Ensure that the information in this section provides clear evidence of the information provided in the summary pages of this form (recommended maximum of 30 pages). Complete the **Annual profile of monetised costs and benefits** (transition and recurring) below over the life of the preferred policy (use the spreadsheet attached if the period is longer than 10 years).

The spreadsheet also contains an emission changes table that you will need to fill in if your measure has an impact on greenhouse gas emissions.

Annual profile of monetised costs and benefits* - (£m) constant prices

	Y ₀	Y ₁	Y ₂	Y ₃	Y ₄	Y ₅	Y ₆	Y ₇	Y ₈	Y ₉
Transition costs										
Annual recurring cost										
Total annual costs										
Transition benefits										
Annual recurring benefits										
Total annual benefits										

* For non-monetised benefits please see summary pages and main evidence base section

Microsoft Office
Excel Worksheet

Evidence Base (for summary sheets)

Background to the amending Directive (2009/44/EC)

On 6 May 2009 the European Parliament and Council adopted the Directive 2009/44/EC, which amends Directive 98/26/EC on settlement finality in payment and securities settlement systems, and Directive 2002/47/EC on financial collateral arrangements as regards linked systems and credit claims. Member states have until 30 December 2010 to adopt and publish the laws, regulations and administrative provisions, necessary to comply with this Directive, which will apply from 30 June 2011.

The Settlement Finality Directive (98/26/EC) was adopted in 1998, in order to reduce the systemic risk associated with participation in payment and securities settlement systems. Since 1998, the post-trading environment has changed considerably. When the original SFD was passed, systems operated on an almost exclusively national and independent basis. However since then systems have become increasingly linked /interoperable. In 2005, the Commission published an evaluation report and concluded that certain parts of the Directive needed to be revisited and amended.

The Financial Collateral Arrangements Directive (2002/47/EC) sought to expand on the role of collateral from the Settlement Finality Directive. The objective was to achieve greater integration and cost –efficiency of European financial markets, by simplifying the collateral process, improving legal certainty in the use of collateral and reducing risks for market participants. In December 2006, the European Commission published an evaluation report, which concluded that the directive was largely working well, but that some aspects would benefit from revision.

Due to the close links between the Settlement Directive and the Financial Collateral Arrangements Directive, the Commission concluded that both directives should be amended together under Directive 2009/44/EC.

These implementation regulations seek to amend the UK Financial Markets and Insolvency Regulations 1999, and the Financial Collateral Arrangements (No.2) Regulations 2003 in order to comply with the European Amending Directive 2009/44/EC.

Option 1 - To amend the Financial Markets and Insolvency Regulations (1999) and the Financial Collateral Arrangements (No.2) Regulations 2003 in order to comply with the European Directive 2009/44/EC.

Group of Measures 1: Introducing the concept of interoperable systems into law

Benefits: The Amending Directive changes various definitions and introduces various terms to ensure interoperable systems are brought into the regime with relevant protections clarified or extended where appropriate. At present, it is unclear whether interlinked systems fully benefit from the protections of the Settlement Finality Directive. By thus reducing the legal uncertainty surrounding the protections enjoyed by systems (e.g. clearing houses, settlement agents), which are linked to other systems, the risk of contagion in the financial system should be reduced. As such systems are vital for the proper functioning of financial markets, a contagion spreading through interlinked settlement systems could, in a worst-case scenario, cause widespread failures, leading to billions of pounds of costs.

As an illustration of the importance of maintaining the resilience of the systems designated under the SFD, we note that for example CHAPS handled an average daily value of £255 billion in 2009; representing almost 20% of annual UK GDP. Meanwhile the daily average value of cash moving through CREST was in the order of £908 billion in March 2010, including self-collateralising repo transactions.

Costs: These changes are clarifying ones and we have not identified any costs associated with them

Group of Measures 2: Providing clarity on calendar days and moments of entry

Benefits: The Directive clarifies that the SFD's protections apply to settlements that take place on the same business day as an insolvency is initiated, and obliges settlement systems to seek to co-ordinate their rules regarding the moment of entry and irrevocability of transfer orders. As with the measures outlined above, by reducing the legal uncertainty surrounding the protections enjoyed by systems (e.g.

clearing houses, settlement agents) which are linked to other systems, the risk of contagion in the financial system should be reduced. As such systems are vital for the proper functioning of financial markets, a contagion spreading through interlinked settlement systems could, in a worst case scenario, cause widespread, leading to billions of pounds of costs.

Costs: this could mean some implementation costs to industry, which we would not expect to be unduly burdensome. Systems which are interlinked will need to take steps to ensure that their rules governing the moment of entry and irrevocability of transfer orders are co-ordinated as far as possible. We are using the consultation process to seek more information from industry on the nature and scale of these costs, but have estimated them as between £0m and £10m in the meantime.

Group of Measures 3: Bringing credit claims into the scope of the FCD

Benefits: The Directive brings credit claims into the scope of the FCD's protections. The intention of this measure is to increase the pool of available collateral that banks can use. In principle, the availability of credit claims as a form of collateral could decrease the cost of funding for credit institutions, thus increasing lending with associated economic benefits. The Eurosystem has since 2007 accepted credit claims as collateral in its credit operations. Certain EU countries (such as Luxembourg) already include credit claims in the scope of their implementation of the FCD, meaning that implementation of the Amending Directive will put relevant UK entities on a level playing field with Entities in other EU jurisdictions. The European Commission has estimated (see reference 1 in list above) that the measure may benefit Euro area countries by E3.5bn to E263bn, in the form of collateral savings/additional liquidity available to financial institutions. (This estimate takes into account only the first-round effects and does not include any additional benefits that could come from financial institutions using this liquidity to fuel their businesses.) These potential benefits are of increased relevance to the UK in light of the Bank of England's announcement that it will accept credit claims as collateral for its Discount Window Facility. A simplistic adjustment based on the relative size of UK and Eurozone GDP would suggest this figure might be E0.5bn to E35bn for the UK. No comments were made on this estimate during the consultation stage.

Costs: There may be costs among industry relating to implementing systems for handling credit claims in case such systems are not already in place, although it should be borne in mind that there is no obligation for industry to use credit claims as collateral. In addition it can be observed that in the extended regime, if a credit institution were to go bankrupt, any credit claims pledged as collateral would not be available to repay the institution's creditors, disadvantaging those creditors versus a situation in which they had a claim on the collateral.

Option 2 – Not to implement

Benefits: Existing legislation would stay the same for the industry. The costs described above would not accrue.

Costs: The risks described above would not be addressed. In addition the UK runs the risk of infraction proceedings being initiated by the European Commission if we do not meet the implementation date of 31 December 2010.

Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

Basis of the review: [The basis of the review could be statutory (forming part of the legislation), it could be to review existing policy or there could be a political commitment to review];

Within 5 years of the implementation of the statutory instrument the Treasury will review the implementing regulations.

Review objective: [Is it intended as a proportionate check that regulation is operating as expected to tackle the problem of concern?; or as a wider exploration of the policy approach taken?; or as a link from policy objective to outcome?]

To ensure that the regulations remain an appropriate method of implementing the Amending Directive.

Review approach and rationale: [e.g. describe here the review approach (in-depth evaluation, scope review of monitoring data, scan of stakeholder views, etc.) and the rationale that made choosing such an approach]

Treasury officials will seek views of relevant stakeholders, such as system operators, the Bank of England and the FSA.

Baseline: [The current (baseline) position against which the change introduced by the legislation can be measured]

Success criteria: [Criteria showing achievement of the policy objectives as set out in the final impact assessment; criteria for modifying or replacing the policy if it does not achieve its objectives]

The Treasury and stakeholders consider that the implementing regulations continue to satisfactorily implement the provisions of the amending directive.

Monitoring information arrangements: [Provide further details of the planned/existing arrangements in place that will allow a systematic collection of monitoring information for future policy review]

Treasury officials are in regular contact with affected stakeholders.

Reasons for not planning a PIR: [If there is no plan to do a PIR please provide reasons here]

HM Treasury contacts

This document can be found in full on our website at:
hm-treasury.gov.uk

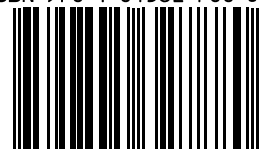
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