HM Treasury

The Central Securities Depositories Regulations 2017:

response to the consultation

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Contents

1 Introduction

1.1 On 23 June 2016, the EU referendum took place and the people of the United Kingdom voted to leave the European Union. Until exit negotiations are concluded, the UK remains a full member of the European Union and all the rights and obligations of EU membership remain in force. During this period the Government will continue to negotiate, implement and apply EU legislation. The outcome of these negotiations will determine what arrangements apply in relation to EU legislation in future once the UK has left the EU.

1.2 The Treasury published a consultation on proposed changes to domestic legislation in respect of Regulation EU 909/2014, the Central Securities Depositories Regulation (CSDR), on 8 December 2015. The consultation closed on 4 February 2016.

1.3 The government has decided to publish its response to this consultation in two stages. This document gives a summary of responses submitted and government decisions in relation to the Central Securities Depositories Regulations 2017. A response focussing on the Uncertificated Securities (Amendment) Regulations 2017 will be published in due course.

1.4 The CSDR was adopted by the European Parliament on 15 April 2014. It was published in the Official Journal of the European Union (OJEU) on 28 August 2014, and entered into force in part on 17 September 2014.

1.5 Provisions of the CSDR which came into full effect at this time and required implementation were implemented by the Central Securities Depositories Regulations 2014 (S.I. 2014/2879) ("2014 Regulations"). These Regulations designated the Financial Conduct Authority (FCA), Prudential Regulation Authority (PRA) and the Bank of England as competent authorities in relation to different provisions in the CSDR and provided those bodies with powers for the enforcement of the CSDR and for sanctions.

1.6 Additional provisions of the CSDR came into full effect following the publication of regulatory and implementing technical standards and delegated acts in the OJEU on 10 March 2017. The Central Securities Depositories Regulations 2017 ensure that domestic legislation is compatible with these provisions of the CSDR including regulatory and implementing technical standards and delegated acts. It also contains further competent authority designations and additional enforcement powers.

1.7 The Central Securities Depositories Regulations 2017 will be laid before Parliament in due course.

1.8 Additional provisions of the CSDR will apply once a CSD is authorised under CSDR. The Uncertificated Securities (Amendment) Regulations 2017 to be laid in due course will update the Uncertificated Securities Regulations 2001 (S.I. 2001/2755) as appropriate to ensure full compatibility of UK domestic legislation with the CSDR.

1.9 The consultation paper published on 8 December 2015 did not address the CSDR Article 3(1) provision requiring issuers of transferable securities admitted to trading or traded on trading venues to arrange for those securities to be "represented in book-entry form as immobilisation or subsequent to a direct issuance in dematerialised form." This requirement will instead be addressed in a separate consultation from the Department for Business, Energy and Industrial Strategy.

1.10 The government received three responses to its consultation which it considered in making its final policy decisions.

2 Competent authorities

2.1 The CSDR requires Member States of the European to designate competent authorities. Shortly after CSDR's publication in the OJEU in 2014, initial designations were made designating the Bank of England, the FCA and the PRA for a number of provisions that were applicable at that time and for authorisation and supervision of CSDs. In the consultation draft, the government proposed further designations as follows: for the FCA, the supervision of investment firms for CSDR purposes; for the Bank, the supervision of settlement internalisers and central counterparties ("CCPs") for CSDR purposes, and an extension to the designation of the Bank as competent authority for CSDs to make it clear that they are also responsible for EEA and third country CSDs.

Question 1: Do you agree with the designations set out above? If not, please provide your reasons for this to help us understand your view.

2.2 In view of the government's wish to ensure that any changes stemming from CSDR build on existing practices and capitalise on expertise already in place, it will designate the FCA as the competent authority for supervising investment firms under CSDR. The FCA is already the relevant competent authority responsible for supervising these firms for the purposes of Directive 2014/65/EU, the Markets in Financial Instruments Directive (MiFID).[1]

2.3 The government has additionally made the FCA the relevant competent authority in relation to participants in securities settlement systems for the purposes of monitoring and enforcing Article 38(5) and (6) of CSDR as no designation was made in the consultation draft. Information-gathering and sanctions powers have also been granted to the FCA with regard to CSD participants who are neither authorised persons nor recognised bodies.

2.4 As proposed in the consultation draft, the government has designated the Bank of England as the competent authority for enforcing the requirements of CSDR related to settlement internalisers and CCPs. The Bank of England is the relevant competent authority for CCPs under Regulation (EU) No 648/2012 the European Market Infrastructure Regulation (EMIR).[2] With regard to settlement internalisers, it will take on responsibilities relating to Article 9 of CSDR which requires settlement internalisers to report to the Bank transactions settled outside of a CSD. The government also decided to clarify in the Regulations as made that the Bank is the competent authority for EEA and third country CSDs and to add additional wording to ensure it is understood that the Bank of England has all CSDR competent authority functions relating to CSDs.

[1] http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32004L0039
[2] http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32012R0648

3 Settlement internalisers

3.1 A settlement internaliser is defined by CSDR as "any institution, including one authorised in accordance with Directive 2013/36/EU or with Directive 2014/65/EU, which executes transfer orders on behalf of clients or on its own account other that through a securities settlement system". Examples of settlement internalisers may include custodian banks and large stockbrokers.

Question 2: Do you agree with the provision of powers to the Bank of England in support of its function under Article 9 of CSDR with respect to reporting by settlement internalisers, as drafted in Annex A? If not, please provide your reasons for this to help us understand your view.

3.2 Article 9 of the CSDR specifies that a settlement internaliser shall report to its competent authority the aggregated volume and value of all securities transactions that it settles outside securities settlement systems on a quarterly basis. The government, in the further designations discussed in Section 1, proposed the Bank of England as the relevant competent authority for settlement internalisers.

3.3 To support the Bank of England's functions with respect to reporting by settlement internalisers, in the consultation draft the government proposed a range of powers including the power to obtain information to determine whether an institution is a settlement internaliser and verify whether it has complied with the reporting requirement in the CSDR; and the power to impose penalties and publish statements of censure where settlement internalisers have not complied with CSDR or Bank of England requirements under the Regulations. One respondent agreed that the provision of these powers are appropriate to support the Bank's functions under Article 9. No further comments were received.

Question 3: Should paragraph 36(2) of Schedule 17A to FSMA

be amended to permit the Bank of England to recover costs of setting up the necessary systems for reporting by settlement internalisers?

3.4 In the consultation draft the government proposed to give the Bank of England the power to charge fees to settlement internalisers in connection with the discharge of the Bank's functions under CSDR. It queried whether this power should be worded such that it explicitly applies for the purpose of meeting expenses incurred in preparation for the exercise of the Bank of England's powers under the CSDR.

3.5 One respondent shared views on this issue and maintained that there should not be a provision for the Bank to recover costs incurred in setting up the necessary systems for reporting by settlement internalisers.

3.6 Paragraph 36 of Schedule 17A to FSMA (Financial Services and Markets Act 2000) has been amended to permit the Bank to recover costs of setting up the necessary systems for reporting by settlement internalisers. The government considers that an IT solution is necessary in order for the Bank to adequately carry out its functions with respect to settlement internaliser reporting and that this cost should be met by the affected firms.

Question 4: Do you believe that the Bank of England should be given powers equivalent to sections 166 and 166A of FSMA in its role as the competent authority for settlement internalisers?

3.7 In the consultation draft the Bank of England was not given powers equivalent to sections 166 (reports by skilled persons) and 166A (appointment of skilled person to collect and update information) of FSMA in relation to settlement internalisers. However views were sought on this possibility in the consultation document.

3.8 The government has considered the one response, which was favourable, on whether provision should be made for the Bank of England to have section 166 and 166A of FSMA powers in its role as the competent authority for settlement internalisers. These powers would permit the Bank to require an expert's report on whether reporting obligations are being complied with and appoint a skilled person to collect and update information where the settlement internaliser has failed to do so.

3.9 The government believes that these powers will be an effective, proportionate and dissuasive means to address compliance problems and has decided to provide these to the Bank of England.

4 Recognised CSDs and authorisation

CSDR introduces a requirement on CSDs to apply for authorisation in order to be permitted to provide certain services specified in the Annex. The CSDR and subsequent regulatory technical standards (RTS) and implementing technical standards (ITS) set out how the authorisation process will be applied. Consequently, the government needs to ensure that overlapping domestic requirements are removed and that powers are extended where necessary to permit the Bank of England as the competent authority for CSDs to fulfil its role.

Question 5: Do you agree with the proposed approach of creating a new recognised body category – a recognised central securities depository?

4.1 In order to implement requirements in the CSDR regarding the authorisation and supervision of CSDs, in the consultation draft the government proposed to amend existing domestic legislation including Part 18 of FSMA which sets out a recognition requirements regime for specific financial market infrastructure.

4.2 In particular, the government proposed the creation of a new recognised central securities depository (RCSD) category for CSDs. This would mark a departure from the current position in which CSDs, along with CCPs, are recognised as a recognised clearing house (RCH). Respondents agreed with the government's approach to this new category which avoids unnecessary duplication or excessive requirements, and better reflects the differences between CSDs and CCPs. The Regulations will therefore maintain the proposed line of amending FSMA and other legislation applying to clearing houses to add RCSDs.

Question 6: Do you believe the proposed scope of the exemption in section 285(3D) and the recognition order in section 290(1E) for RCSDs to be suitable? Specifically, should the recognition order record any authorisation under Article 54(2)(a) or (b) of CSDR and list the ancillary banking services to which its authorisation relates, even though the CSD does not benefit from the FSMA exemption in section 285 for banking services? Do you consider that having outsourced activities and CSD links listed in the recognition order, but not explicitly mentioned in the section 285 exemptions, would cause confusion?

4.3 The government proposed in the consultation draft that RCSDs would be exempt from the general prohibition in section 19 of FSMA. This would allow RCSDs to carry on a regulated activity in the UK without the need to obtain authorisation as an authorised person. The exemption covers RCSDs in connection with any core services of CSDs and non-banking type ancillary services listed in Section A and B of the CSDR Annex, that they are authorised to provide under the CSDR authorisation, and certain investment services. The exemption does not cover banking type ancillary services listed in or permitted under Section C of the CSDR Annex. In the consultation draft the recognition order would in addition list additional authorisations granted to the CSD for CSD links and outsourcing. But the recognition order would not list banking type ancillary services.

4.4 The government queried whether the scope of this exemption was appropriate and invited views on what the CSD recognition order, which would be granted to a CSD upon authorisation, should list.

4.5 The Regulations as made follow the approach in the consultation draft for the exemption in that the exemption will cover RCSDs in connection with any core services of CSDs and non-banking type ancillary services listed in Sections A and B of the CSDR Annex. However taking account of

one consultation response which considered more detailed issues in the drafting, the exemption will not cover investment services and activities in addition to those explicitly listed in Sections A and B of the CSDR Annex.

4.6 One respondent believed that the recognition order should exhaustively record any ancillary banking services authorised under Article 54(2)(a) or (b) of the CSDR. The government accepts the view offered which is that this would make the information more accessible about exactly what banking risks the CSD is taking on. It is convenient to have all the authorisations for the RCSD listed in a single document.

4.7 The government also notes the comments of another respondent which maintained that, since Article 16(2) of the CSDR refers to the authorisation specifying "the core services listed in Section A of the Annex and non-banking type ancillary services permitted under Section B of the Annex, which the CSD is authorised to provide", the recognition order should not include the activities under Section A of the CSDR Annex that are permitted to be outsourced and any CSD link that the RCSD is authorised to maintain. The government believes that listing these activities in the recognition order is consistent with Article 16(2) and would enable the recognition order to fully document the scope of the CSDR authorisation.

4.8 The recognition order will therefore record ancillary banking services authorised under Article 54(2)(a) or (b) of the CSDR, activities under Section A of the CSDR Annex that are permitted to be outsourced, any CSD link that the RCSD is authorised to maintain and investment services and activities which the CSD is authorised to provide.

Question 7: Is the scope of the exemptions for EEA and third country CSDs appropriate?

4.9 In relation to European Economic Area (EEA) CSDs providing services in the UK under Article 23 of CSDR and third country CSDs recognised by ESMA, in the consultation draft the government proposed an exemption from the general prohibition in section 19 of FSMA, as for RCSDs. However, it also included provisions aimed at preventing EEA CSDs that have not complied with the relevant arrangements in Article 23 of CSDR from taking advantage of the exemptions.

4.10 No respondents disagreed with these provisions and they are therefore maintained in the Regulations as made.

Question 8: Where the second sub-paragraph of Article 24(5) of CSDR applies in relation to an EEA CSD, should the Bank of England be obliged under section 298 of FSMA to allow a period for representations before giving a direction to the EEA CSD? Should the period for representations be retained in circumstances where EEA CSDs have persistently breached CSDR?

4.11 The consultation draft permitted representations to be made in all cases before the Bank could give a direction under section 296, including where the second sub-paragraph of Article 24(5) applied in relation to an EEA CSD.

4.12 One respondent commented that it was not appropriate to oblige the Bank of England to allow a period for representations before giving a direction to an EEA CSD on the grounds of systemic risk mitigation, and that there should not be a period for representations where EEA CSDs have persistently breached CSDR.

4.13 The government has considered these comments in light of the requirements in Article 24(5) which sets out that the host competent authority must refer to the home competent authority and to the European Securities and Markets Association (ESMA) where it has grounds for believing that an EEA CSD within its territory is in breach of its obligations under the CSDR. It is only where, despite measures taken by the home competent authority, the CSD persists in breaching CSDR that the authority of the host Member State is required to take all appropriate measures to ensure compliance with CSDR in its territory.

4.14 The government believes that before the situation in the second sub-paragraph of Article 24(5) arose there would have been a sufficient opportunity for the relevant EEA CSD to make representations, and that an opportunity to make representations should not then be mandatory in the circumstances set out in the second paragraph of Article 24(5) where, despite measures taken by the home competent authority, an EEA CSD persists in infringements of the CSDR. The consultation draft of the Regulations has been altered accordingly.

Question 9: Do you agree that section 291 of FSMA need not be amended?

4.15 The government proposed in the consultation document to retain the principle of statutory immunity and its application to RCSDs. Under section 291 of FSMA, recognised bodies benefit from limited statutory immunity when carrying out their regulatory functions under FSMA. The government considered that the application of section 291 in relation to RCSDs, which will be recognised bodies and therefore captured by the provision, falls outside the scope of CSDR and should be retained without amendment.

4.16 Two respondents agreed with this approach and commented that the continued application of section 291 of FSMA to RCSDs is essential, including to maintain equal treatment with other financial market infrastructure under this section.

Question 10: Do you agree with the proposed amendments suggested in the RRRs?

4.17 As a consequence of the proposed removal of CSDs from the RCH category, in the consultation draft the government proposed amendments to the Financial Services and Markets Act 2000 (Recognition Requirements for Investment Exchanges and Clearing Houses) Regulations 2001 (S.I. 2001/995) (RRRs) creating new recognition requirements for RCSDs. This included retaining, for RCSDs, the requirement on RCHs to ensure appropriate measures are adopted to reduce the extent to which its facilities can be used for a purpose connected with market abuse or financial crime.

4.18 One respondent agreed with all of the proposed amendments, while another questioned whether consequential amendments that maintain the existing regulatory framework are consistent with CSDR, given that it is a maximum harmonisation regulation. They also noted that in view of the CSDR's aim to create a competitive and level playing field it is important that CSDs in one member state are not subject to requirements not imposed on other CSDs.

4.19 The government agrees that retaining the consequential amendment referenced above which requires that "a central securities depository must ensure that appropriate measures are adopted to reduce the extent to which its facilities can be used for a purpose connected with market abuse or financial crime, and to facilitate their detection and monitor their incidence" would go beyond the beyond the ambit of the CSDR. The amendment has been removed accordingly. The government notes that existing market abuse standards will continue to apply to CSD participants.

4.20 Additionally, the consultation document noted that the consultation draft included an amendment transposing Article 34 of MiFID 1. The government has considered the apparent contradiction between this MiFID obligation which permits a CSD to refuse access to CCPs or trading venues on commercial grounds with the requirement in the CSDR that access may only be refused on the basis of a comprehensive risk assessment or on financial stability grounds.

4.21 The government notes that MiFID II adjusts the obligation outlined above and does not expressly permit a CSD to refuse access on commercial terms, thus removing the potential for conflict. MiFID II comes into force on 3 January 2018, and the new recognition requirement will not affect any existing RCH until it obtains RCSD status. The statutory instrument has therefore been adjusted to refer to the MiFID II obligation instead.

Question 13: Do you agree with the approach to supplemental legislation with regards to the authorisation of banking-type ancillary services? If not, please provide your reasons for this that would help us to understand your view.

4.22 A CSD is permitted to provide banking type ancillary services if it has obtained an additional authorisation to provide such services in accordance with Article 54. The government designated the Bank of England as the relevant competent authority for this in the 2014 Regulations. The PRA will receive the completed application for such authorisations. A CSD that is successful in its application must be authorised as a credit institution under Part 4A of FSMA. The PRA is responsible for such authorisation.

4.23 The consultation document stated that the government considered that little supplemental legislation is needed with regard to this process as no incompatible domestic legislation has been identified. It made the point that banking type ancillary services which the CSD is authorised to provide will be published on the FCA register of authorised persons. A new right of appeal to the Upper Tribunal for disappointed applicants was proposed in order to implement Article 66 of CSDR.

4.24 No respondents disagreed with the government's proposed approach. However (as mentioned in the response to question 6, banking-type ancillary services for which a CSD is authorised will be listed in the CSD's recognition order.

Question 14: Do you agree with the proposed transitional provisions? Should any further modifications be made to legislation applying to applicants for authorisation under CSDR during the transition period?

4.25 Following from Article 69 of CSDR, the government will need to provide for the one CSD already recognised as a RCH in the UK to make the transition from RCH status to the newly-created RCSD status. CSDR requires that CSDs apply for all necessary authorisations within six months of entry into force of the RTS referred to in Article 69. The consultation draft contained transitional provisions for RCHs seeking RCSD status, including for any CSDs which might be providing services in the UK under article 72 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (S.I. 2001/544). The consultation draft also preserved the effect of designation orders under the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (S.I. 1999/2979).

4.26 Respondents did not suggest any further changes be made to the legislation applying to applicants for authorisation under CSDR during the transition period. The government will therefore maintain the provisions in the consultation draft without substantive amendment.

5 Enforcement powers and additional provisions

Question 15: Do you believe that section 293 of FSMA should be amended to extend the scope beyond recognised bodies to include EEA CSDs?

5.1 In order to comply with CSDR, in the consultation document the government proposed to extend the scope of existing monitoring and enforcement powers of competent authorities which apply to RCHs to RCSDs. The consultation document queried whether the scope of the Bank of England's power to make rules in relation to notification requirements for recognised bodies under section of 293 FSMA should be further extended to include EEA CSDs.

5.2 All respondents were supportive of extending the section of 293 FSMA power to EEA CSDs. The government will proceed with this change which supports the Bank of England in fulfilling the cooperation requirements between competent authorities in different member states, which are set out in Article 24 of the CSDR. The Regulations have been updated accordingly.

Question 16: Should section 293A of FSMA be limited to EEA CSDs with branches in the UK? Are other restrictions on the power appropriate?

5.3 The government also queried whether its proposed extension in the consultation draft of section 293A of FSMA, which allows an appropriate regulator to require information from a relevant body in order to satisfy itself of compliance with EU requirements, should apply to all EEA CSDs or be limited to EEA CSDs with branches in the UK.

5.4 Two respondents offered their views on this question. One of the respondents was in favour of restricting the power to EEA CSDs with branches in the UK while another respondent maintained that, since EEA CSDs are entitled to provide CSD services in the UK without setting up a UK branch, it is not necessary to limit the section 293A power to EEA CSDs with branches in the UK. In line with this view, the government has decided that the power should apply to all EEA CSDs.

5.5 The consultation document also queried whether any additional restrictions on this power are appropriate. One respondent suggested that the section 293A power should be drafted with reference to what information is reasonably required in connection with the functions of the EEA CSD that are subject to CSDR. The government is in agreement with this view and has amended the statutory instrument accordingly.

Question 17: Do you agree the proposed changes in section 295A and section 296 are appropriate for the purposes of CSDR?

5.6 The government also proposed in the consultation document to give the Bank of England a power permitting on-site inspections of UK branches of EEA CSDs, and the power to give directions to RCSDs and EEA CSDs in specified cases under section 296 of FSMA.

5.7 One respondent did not consider it necessary to expressly provide for the failure of a CSD to grant access in draft FSMA section 296(1A)(b).They noted that in such circumstances, the CSD would have failed to comply with obligations in accordance with section 296(1A)(a). Two respondents, however, agreed that the powers proposed are appropriate for the purposes of the CSDR, and the powers set out in the consultation draft are retained in the Regulations with some technical changes.

Question 18: In the context of Article 25 of CSDR, is it appropriate to give the Bank of England any information-gathering or enforcement powers in respect of third country CSDs providing services in the UK, and if so, which powers and in what circumstances?

5.8 CSDR provides for CSDs established in third countries which are recognised by ESMA to offer their services within the EU. For these third country CSDs, ESMA is primarily responsible for addressing the situation where the conditions for recognition are not met. The consultation document did not propose any specific information-gathering or enforcement powers for the Bank of England in respect of third country CSDs providing services in the UK and queried whether this was appropriate.

5.9 Two respondents provided views on this matter. One respondent considered that the Bank of England did not require such powers subject to ESMA providing effective enforcement and provided the UK is not disadvantaged by reciprocal obligations from third countries. The other respondent suggested that the Bank of England should have these powers and that there might be an argument for even wider powers to provide for the case where the Bank of England does not have direct arrangements with the home regulator of a third country CSD.

5.10 The government notes that Article 25 of CSDR is framed with reference to the host competent authority being permitted to request information from the home competent authority and not through direct dealing with the third country CSD. The government considers that since ESMA is required to put in place cooperation agreements between competent authorities and the powers of Member States in Article 25 of CSDR must be exercised in close cooperation with ESMA, it is not appropriate to provide for the Bank of England with specific information-gathering or enforcement powers in respect of third country CSDs.

5.11 Additionally, one respondent commented that Article 63(1) limits the application of sanctions to infringements set out in that Article. They suggested such limitations should be reflected in FSMA section 312E. This change has not been made in the statutory instrument as it would be inconsistent with the government's usual approach. The government's approach, consistent with the implementation of other European financial services directives and regulation, refers to the existing FSMA regime. The FSMA regime potentially attaches to any breach of an EU measure and has no ceiling on fines.

Question 19: Do you consider that the tests for individual liability under section 312FA(1) and (2) are appropriate?

5.12 In the consultation draft, the government proposed extending the range of sanctions in line with Title V of CSDR, including a power permitting the Bank of England to impose penalties on individuals where a CSD has contravened a relevant requirement. One respondent agreed that the tests for individual liability under this power are appropriate. The government will maintain section 312FA(1) and (2) in the terms set out in the consultation draft.

Question 20: Should the Bank of England be given additional powers of investigation and enforcement in relation to EEA CSDs in support of its functions under Article 24(4) and the first sub-paragraph of Article 24(5) of CSDR, and if so what powers? In particular, should the penalties in sections 312E, 312F or 312FA be available in relation to EEA CSDs, and if so, in what circumstances?

5.13 The consultation document described key powers of the Bank of England which the government proposed to extend in relation to EEA CSDs. It sought comments on whether to extend a range of FSMA powers that currently apply to RCHs, such as the power to require information, to EEA CSDs for the purposes of enforcing specific provisions in Article 24 and Article 25 of the CSDR. In particular, the consultation document proposed extending certain powers only in the circumstances in the second sub-paragraph of Article 24(5) of the CSDR where, despite

measures taken by the home competent authority or because such measures prove inadequate, the EEA CSD persists in acting in infringement of the obligations arising from CSDR. The government queried whether the Bank of England should also be given powers in support of other parts of Article 24, namely paragraph 4 and the first subparagraph of paragraph 5.

5.14 The government received two responses on this issue. One respondent said that the Bank did not need to be given additional powers under Article 24. Another explained that, since the intention of CSDR is to level the playing field for European CSDs, the investigatory and enforcement powers available to the Bank in their remit over EEA CSDs should be equivalent to those applicable to RCSDs and that they should support the Bank's functions under Article 24(4) and Article 24(5).

5.15 The government has concluded that the Bank's powers in respect of EEA CSDs should be more extensive than those provided for in the consultation draft in order to support their functions under Article 24. The main changes following consultation are as follows.

- Powers of investigation in Part 11 of FSMA (applied to the Bank by Schedule 17A) are made available in relation to EEA CSDs in the circumstances of Article 24(4) or (5) of CSDR, and not merely where the second subparagraph of Article 24(5) of CSDR applies.
- The powers to apply for injunctions and to apply for or require restitution in Part 25 of FSMA (also applied to the Bank by Schedule 17A) will be available in relation to EEA CSDs in the same way as they are available in relation to RCSDs.
- The penalties and sanctions in sections 312E, 312F and 312FA of FSMA are made available in relation to EEA CSDs in the circumstances of the second subparagraph of Article 24(5) of CSDR.

Question 21: Do you believe that the sanctions for non-compliance with CSDR provided in this section are sufficient, together with sanctions under FSMA, particularly in view of the omission of the sanction of removal of USRs Operator status under the SI at Annex B?

5.16 The government invited views on whether the range of sanctions for non-compliance with the CSDR, and the sanctions under FSMA are appropriate. Two respondents agreed that the range of sanctions are sufficient for these purposes. As this consultation response document is focused only on comments received in relation to the Central Securities Depositories Regulations, those comments which focused on issues relating to the amendments to the USRs will be addressed in the consultation response document to follow.

Question 22: In regulation 5E, what timeframe would you deem appropriate to permit the Bank of England to require additional information or documentation relevant to the decision around any proposed change of control of a CSD? Do you consider that it is appropriate and proportionate to provide that the 60 day time limit for decisions on a change of control runs from receipt of the information requested? If not, can you suggest alternative approaches to enable the Bank of England to obtain the information necessary to assess an application of approval of a change of control?

5.17 The government invited views on the appropriate time frame for the Bank to give notice of additional information or documentation reasonably required relevant to the change of control of a CSD (governed by Article 27 of CSDR). The consultation draft proposed a period of 14 working days starting with the receipt of the Article 27 notification for the Bank to make such a request. One respondent suggested that, in the context of a change of control, as short a time as is reasonably possible should be provided and that provision should be made for 14 calendar days.

The government will maintain its proposal for 14 working days. The provision is found in regulation 5G of the 2014 Regulations in the Regulations as made.

5.18 As regards the question of when the 60 day period for considering applications in Article 27(8) of CSDR runs from, the consultation document proposed that the 60 day period should be interpreted as running from the receipt by the Bank of England of all the required information in support of the application. This approach was reflected in regulation 5E of the 2014 Regulations in the consultation draft.

5.19 One response received in respect of when the 60 day time limit for decisions should run suggested that this time limit should be extended by 30 days. However, this is not permitted by the CSDR which requires that a decision must be made within 60 working days from the receipt of the relevant information by the competent authority.

5.20 Another response was received agreeing with the position set out in consultation. The government will maintain its position that this should be after receipt of the information requested. The Regulations as made therefore maintain the approach set out in the consultation draft, but the relevant provision is now numbered regulation 5G.

Question 23: Regarding regulation 5F, should the CSD (in addition to the person giving notice) have a right of redress if the Bank of England opposes the change of control?

5.21 The consultation document also sought views on whether a right of redress should apply to a CSD (in addition to the person giving the notice) where the Bank of England opposes a change of control under Article 27 of CSDR. Two respondents were in favour of giving the CSD a right of redress.

5.22 The government has re-examined regulation 5F and considers that it does give a CSD a right to refer the Bank's decision to the Tribunal in all cases where the Bank notifies the CSD of its decision under Article 27(8) of CSDR. The right to refer the decision for review is available to any person to whom notice of the Bank's decision is given, and that includes the CSD. Regulation 5F is renumbered regulation 5H in the Regulations as made.

Question 24: What would be the most practical and appropriate means of enforcing regulation 5L?

5.23 In order to comply with Article 65(3) of CSDR, regulation 5L of the 2016 Regulations in the consultation draft requires trading venues, investment firms, CCPs, settlement internalisers and credit institutions designated under Article 54 of CSDR to have appropriate procedures in place for their employees to report actual or potential infringements. The government consulted on what the most practical and appropriate means of enforcing regulation 5L would be, since the consultation draft did not contain an enforcement mechanism.

5.24 The government received one response to this question. It noted that any means for enforcing regulation 5L should be consistent with existing procedures and warns that developing new processes would be duplicative and cumbersome.

5.25 The government has decided that for recognised investment exchanges and CCPs, Article 65(3) would best be implemented through recognition requirements so the FSMA enforcement routes for recognition requirements will be available. The Regulations as made contain these amendments: see new paragraphs 9B and 31A of the Schedule to the RRRs.

5.26 In order to facilitate the use of existing enforcement mechanisms, FCA and PRA rules will be used to implement Article 56(3) with regard to investment firms and credit institutions (including those operating trading venues). Regulation 5L of the 2014 Regulations (which has become regulation 5N in the Regulations as made) will therefore apply only to settlement internalisers, who might include persons who are neither authorised nor recognised under FSMA.

5.27 The enforcement mechanism chosen for regulation 5N and set out in the Regulations as made is regulations 5A concerning obtaining information and 5B concerning statements of censure and penalties. This provides the Bank of England with investigation powers and sanctions powers in the event of an infringement of regulation 5N.

Question 25: Do you agree that Article 66 of CSDR requirement that decisions and measures must be properly reasoned generally does not require implementing?

5.28 The CSDR requires Member States in Article 66 to ensure that decisions and measures taken under the CSDR are properly reasoned and subject to a right of appeal.

5.29 The government expressed the view in the consultation document, that it is not necessary to implement the requirement to ensure that decisions are properly reasoned since this is directly applicable. One response was received in agreement with the government's position.

Question 26: Does regulation 5J need to make it clearer that a right to refer to the Upper Tribunal arises after any reference to ESMA under CSDR has been determined?

5.30 To implement the right of appeal under the CSDR, regulation 5J in the consultation draft set out the decisions under the CSDR which may be referred to the Upper Tribunal. The government sought views on whether, in cases where these decisions may also be referred to ESMA, the legislation should state that the right to refer to the Upper Tribunal arises after any reference to ESMA has been determined.

5.31 One respondent commented that this was appropriate but, having reconsidered the various scenarios which might arise under the relevant Articles of CSDR, the government has taken the view that a referral to ESMA and a referral to the Upper Tribunal are distinct and separate remedies exercisable by different persons which can potentially run concurrently.

5.32 By way of illustration, Article 33 of the CSDR allows an EEA competent authority to refer decisions taken by the Bank of England to ESMA for conciliation. At the same time, in accordance with Article 66 of the CSDR, relevant CSDs and complainants have the right to appeal decisions taken by the Bank of England – including under Article 33 of the CSDR – to the Upper Tribunal.

5.33 The government has therefore concluded that provision of the sort consulted on would not be appropriate and has maintained the approach in the consultation draft. This can be found in regulation 5L of the Regulations as made.

Question 27: Is the proposed approach to defining authorised CSD services appropriate in including both non-banking and banking type ancillary services?

5.34 In the consultation draft, the government proposed a range of amendments to the Companies Act 1989 and related secondary legislation which are consequential to the creation of the RCSD category.

5.35 One amendment in the consultation draft was proposed to section 155 of the Companies Act 1989 (market contracts). The new definition of "market contract" as it applies to RCSDs referred to contracts for the purpose of providing authorised CSD services. The definition of authorised CSD services included the core services and both the non-banking and banking-type ancillary services listed in Sections A, B and C of the Annex to CSDR. This consultation question sought comments on the appropriateness of the definition. One respondent agreed that the approach in the consultation draft was the correct approach. The government has maintained the proposed approach of including non-banking and banking-type ancillary services in the authorised CSD services definition in the Regulations as made.

Question 28: Is the proposed approach to amending section 182 of the Companies Act 1989 adequate in ensuring compliance with Article 38 of CSDR?

5.36 The consultation document sought responses on whether proposed new section 182B of the Companies Act 1989 was adequate to ensure compliance with Article 38 of the CSDR. The underlying concern was that insolvency law provisions on mutual credit and set-off would otherwise negate the segregation requirements in Article 38 of CSDR. Respondents provided a range of views on whether to dis-apply those insolvency law provisions through a new section 182B.

5.37 One respondent suggested that the proposed amendment was useful, even in the absence of Article 38 of the CSDR. However, two other respondents maintained that the amendment was neither appropriate nor necessary to ensure compliance with Article 38. They expressed the views that Article 38 only relates to the need for a CSD operator to maintain segregated accounts and that, under UK insolvency law, set-off provisions are about the cross application of mutual monetary claims.

5.38 The government considers that participants' accounts at a CSD are unlikely to contain assets capable of being set off. Securities held in accounts are not likely to be capable of being set off, and neither are other proprietary entitlements. It is not considered that there is a realistic prospect of set off applying. The government also agrees that section 182B is not required to secure consistency with Article 38 of CSDR. The government does not consider that section 182B would serve a useful purpose, and the provision is omitted in the Regulations as made.

Question 29: Regarding the treatment of margin and default fund contributions in the Companies Act 1989, should the protections afforded to RCHs apply to RCSDs? Please provide reasons for your answer.

5.39 RCHs are afforded protections related to margin and default fund contributions. These normally apply to CCPs, but at present in the UK CSDs do not require margin and do not have a default fund to which participants could contribute.

5.40 Two respondents commented that these protections are not necessary as they apply more directly to the activities of CCPs. However, one of these respondents considered that it would be appropriate to put in place legislative provisions in relation to margin and default fund contributions for RCSDs.

5.41 The consultation draft took the precautionary approach of extending the same protections to RCSDs as currently apply to RCHs as regards margin and default funds, even if it was not certain that they would be needed.

5.42 While the government is not aware of any intention that either of these features will be introduced, it considers that the option should not be restricted by the protections offered in law to RCSDs. The government has decided to maintain current drafting and to afford margin and default fund contributions the same protection as RCHs.

Responses to the MIFID II consultation relevant to CSDR implementation

5.43 The response to the consultation on the transposition of the Markets in Financial Instruments Directive (2014/65/EU) ("MiFID II") published in February 2017 referred to two responses received in relation to the CSDR.

5.44 Respondents noted their view that CSDs authorised under the CSDR should be exempt from MiFID II authorisation if they provide an approved reporting mechanism (ARM) service as this should fall under paragraph 4(b) of Section B of the Annex to the CSDR.

5.45 The government has carefully considered this issue and consistent with advice published by the European Securities and Markets Authority (ESMA)[1] has come to the view that providing an ARM service goes beyond the scope of paragraph 4(b) of Section B of the Annex and therefore requires MiFID II authorisation.

[1] https://www.esma.europa.eu/sites/default/files/library/esma70-708036281-2_csdr_qas.pdf

6 Glossary

Banking or banking-type ancillary services means the services referred to in Section C of the Annex to CSDR (including services not explicitly listed in that Section).

CCP means a central counterparty. EMIR defines a CCP as "a legal person that interposes itself between the counterparties to the contracts traded on one or more financial markets, becoming the buyer to every seller and the seller to every buyer".

CRD4 or the Capital Requirement Directive 4 means Directive (EU) 2013/36 of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

Credit institution means a credit institution authorised under CRD4.

CSD means a central securities depository. CSDR defines a CSD as "a legal person that operates a securities settlement system referred to in point (3) of Section A of the Annex [to CSDR] and performs as least one other core service listed in Section A of the Annex [to CSDR]".

CSDR (the Central Securities Depositories Regulation) means Regulation (EU) 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on Central Securities Depositories (CSDs) and amending Directive 98/26/EC.

Delegated act refers to a non-legislative act adopted by the European Commission of general application that amends or supplements certain non-essential elements of a legislative act.

Dematerialised form means the fact that financial instruments exist only as book entry records.

EEA means the European Economic Area.

EEA CSD means a CSD established in an EEA State other than the UK which has been authorised under CSDR. A definition is proposed to be inserted into section 285 of FSMA, see draft subsection (1)(f).

EMIR (the European Market Infrastructure Regulation) means Regulation (EU) 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories.

ESMA means the European Securities and Markets Authority.

7 List of respondents

The British Bankers' Association (BBA) and the Association of Financial Markets in Europe (AFME)

The City of London Law Society (CLLS)

Euroclear United Kingdom and Ireland (EUI)

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