

OPINION OF THE EUROPEAN MONETARY INSTITUTE

On a consultation received from the Bank of England, under Article 109f (6) of the Treaty establishing the European Community (the "Treaty") and Article 5.3 of the Statute of the EMI (the "Statute"), in relation to regulations to be made under the UK Companies Act 1989 (the "Act") (specifically under Part VII thereof), being regulations made jointly by the Secretary of State for Trade and Industry and HM Treasury in accordance with powers granted to such authorities under the terms of Part VII of the Act, such regulations being referred to as The Financial Markets and Insolvency (Money Market) Regulations 1995 (the "Regulations").

CON 95/10

1. The present consultation was initiated on 3rd July 1995 by the Bank of England which, for this purpose, transmitted to the EMI the relevant documents concerning the Regulations, requesting receipt of an opinion by 21st July 1995 and referring, in support of this timetable, to Article 4 of the Council Decision of 22nd November 1993 on consultation of the EMI (93/717/EC) (the "Council Decision"). This timetable being requested on the basis that the scheduled start date for the ECHO foreign exchange clearing system is set for early August 1995 (see paragraph numbered 2 below).
2. The purpose of the Regulations is to improve the security and stability of the UK financial markets. This is to be achieved by ensuring that, in the event of the default of a member of certain key clearing houses and exchanges (specifically where such default is occasioned by the insolvency of such a member), the rules of the relevant clearing house or exchange covering default will take precedence over certain of the normal provisions of UK insolvency law. Initially, the Regulations will only have effect in relation to the ECHO foreign exchange clearing system, which is expected to become operational in early August 1995. However, it is anticipated that other clearing houses and exchanges will become subject to the Regulations in due course. All entities which are subject to the Regulations will be bodies in relation to which the Bank of England will exercise certain relevant supervisory powers (e.g. ensuring the adequacy and acceptability of the rules of any system applying to be subject to the Regulations). It is noted that similar modifications to UK insolvency law are already operational in relation to the Central Gilts Office and the London Clearing House (over which the Bank of England does not exercise relevant supervisory authority).
3. The EMI's competence to deliver an opinion in this consultation is based on Article 109f (2), fourth indent, and (6), second paragraph, (as elaborated by the Council Decision) on the grounds that the Regulations have the potential to affect the stability of the financial markets, both in the

UK and, as some of the clearing houses and exchanges which are likely to be impacted (including ECHO) have memberships drawn from many jurisdictions, indirectly in other EU Member States also.

4. The EMI notes that the Regulations are similar in their scope to provisions being brought into effect in several other EU Member States and that the move to adopt such rules results from a general recognition of the need to disapply certain insolvency provisions which might otherwise frustrate the default rules of clearing houses and exchanges and thereby prevent the orderly winding up of a defaulter's position. Such insolvency provisions might otherwise prevent the effective settlement of positions in the relevant market system and might therefore lead to consequent systemic difficulties. The EMI therefore welcomes these Regulations in principle and considers that they are likely to have a positive effect in enhancing the stability of relevant exchanges and clearing houses and, consequently, in contributing to the stability of certain key financial markets based in London and overseen by the Bank of England.
5. The EMI also notes that the Bank of England, in fulfilling its role of administering the Regulations, has wide-ranging powers to determine which clearing houses and exchanges should be added to the list of those organisations which will be subject to the Regulations. The Bank also has very wide ranging powers and discretions in administering the Regulations. The EMI recognises that such powers constitute a powerful tool to ensure the suitable and effective operation of the Regulations and, therefore, in turn may have a significant, positive effect upon financial stability.
6. The EMI notes that the drafting of the Regulations and the detail of their mechanics is highly complex and does not readily lend itself to immediate comprehension. The EMI acknowledges, however, that the subject matter with which the Regulations deal is highly complex and, indeed, that Part VII of the Act, on which they are based, is a highly complex piece of legislative drafting. The EMI therefore attributes the degree of complexity encountered in the Regulations to these factors.
7. In more general terms, the EMI notes that attempts are currently being made, in various fora, to harmonise European rules on insolvency, particularly as they relate to financial markets and participants on those markets. Whilst the EMI appreciates that all Member States retain the freedom to adapt their laws on insolvency related issues as they see fit, in particular to allow them to deal with issues which have specific relevance to their jurisdiction and markets within their jurisdiction, sufficient flexibility should exist to allow for subsequent, concrete harmonisation measures in this field to be catered for. Equally, where appropriate, in adopting insolvency regulations which are relevant to participants in financial markets, Member States may wish to

consider the impact of such measures upon the orderly winding-up and speedy settlement of positions on markets which are established in other jurisdictions.

- 8 The EMI agrees that this opinion may be made public by the competent United Kingdom authorities at their discretion.

21st July 1995