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Treasury Committee

Lessons from Greensill Capital: Responses to the Committee's Sixth Report of Session 2021–22

Fifth Special Report of Session 2021–22

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The Treasury Committee

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Contacts

All correspondence should be addressed to the Clerk of the Treasury Committee, House of Commons, London SW1A 0AA. The telephone number for general enquiries is 020 7219 5769; the Committee's email address is treascom@parliament.uk.

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1. The Committee published its Sixth Report of Session 2021–22, Lessons from Greensill Capital, on 20 July 2021. In that Report, the Committee made recommendations to the Government and the financial regulators arising from the lessons learned from the failure of Greensill Capital.

2. The Committee received a letter from the Chancellor of the Exchequer, Rt Hon. Rishi Sunak MP, on 20 September 2021, constituting the Government response to its Sixth Report. That letter is appended to this Report.

3. The Committee received a letter from Sam Woods, Deputy Governor for Prudential Regulation, Bank of England, and Chief Executive Officer of the Prudential Regulation Authority, on 25 August 2021, constituting the PRA's response to the Committee's Sixth Report. The Chair of this Committee wrote to Mr Woods on 14 September 2021 seeking clarification on certain points made in that letter. Mr Woods' subsequent reply was received on 17 September 2021. These letters are appended to this Report.

4. The Committee received a letter from the Chief Executive of the Financial Conduct Authority, Nikhil Rathi, on 17 September 2021, constituting the FCA's response to the Committee's Sixth Report. That letter is appended to this Report.

Appendix 1: Response from HM Treasury

Letter from the Chancellor of the Exchequer to the Chair of the Committee

TREASURY COMMITTEE REPORT: LESSONS FROM GREENSILL CAPITAL

I am grateful to your Committee for its report of 20 July 2021 into the failure of Greensill Capital and for the thorough and detailed approach you have taken to this subject.

I particularly welcome the Committee's recognition that the Treasury was right to consider seriously—and right to reject—Greensill's proposals for inclusion in the CCFF, and that Treasury officials and ministers behaved with complete and absolute integrity with respect to their handling of Mr Cameron's lobbying.

However, I am committed to ensure we learn any wider lessons from this episode, such as for financial regulation. This letter aims to respond to the key recommendations to the Government contained in the report.

Financial regulation

The report rightly examines the case for improvements to financial regulation arising from the failure of Greensill and makes several recommendations.

Securitisation

The Committee finds that the definition of securitisation may be too narrow.[1]

A securitisation is defined by the Securitisation Regulation as a transaction or scheme where payment is dependent on the performance of the underlying pool of exposures. The Regulation specifies that a securitisation must have at least two tranches with different levels of risk, where investors in the lower tranche(s) are exposed to more risk than investors in the higher tranche(s). This definition is consistent with the international Basel standards. Tranching often involves additional parties like credit ratings agencies and various modelling techniques and adds to the complexity of securitisation. The funding of supply chain finance through the issuance of notes, described in the Committee's report to be Greensill's funding model, does not involve tranches, and instead investors typically all take on the same level of risk.

Revising the definition of securitisation to include the onward sale of a pool of loans comprising supply chain finance would mean regulating these transactions in the same way as securitisations. There are some elements of the Securitisation Regulation which could be relevant, for example requirements to provide transparency about the underlying loans and for investor due diligence. However, applying the Securitisation Regulation to the onward sale of supply chain finance loans—with its detailed and prescriptive requirements—would in my view be inappropriate, as the onward sale of a pool of loans poses different risks to a securitisation, as presently defined. For example, the Securitisation Regulation addresses the leverage associated with lower securitisation tranches and systemic risks that come with it. The Government has not seen evidence that supply chain finance presents a similar degree of leverage or systemic risk. In a

1 Paragraph 22

similar vein, securitisations carry with them higher capital requirements (reflecting the potential leverage and risk associated with them) than would necessarily be appropriate for investing in a pool of untranched business loans.

Moreover, amending the Securitisation Regulation definition to remove the tranching requirement could capture the financing of any pool of exposures, thus bringing into scope a large part of the well-established commercial lending market. This could negatively impact businesses' abilities to access finance, particularly because capital requirements for such exposures would likely increase as a result of them being in scope of the Securitisation Regulation, thus making it more expensive for businesses to engage in such activities.

Nonetheless, I recognise that some regulatory requirements or guidance, elsewhere than the Securitisation Regulation, for example relating to transparency and due diligence, could be relevant to the onward sale of loans where tranching isn't present. The benefits and impact of making such a change would require careful consideration so as not to disrupt the supply of credit to businesses. The Government, in consultation with the regulators, will consider whether any new requirements or guidance might usefully apply, taking account of the Committee's recommendation.

Appointed Representatives

I welcome the Committee's recommendation to consider reforms to the Appointed Representatives (AR) regime.[2] The regime enables appointed representatives to carry on certain regulated activities without direct authorisation from the FCA, provided those appointed representatives are subject to oversight by an FCA authorised firm. In my view, strong and effective oversight of appointed representatives is essential for safe operation of the regime.

The Treasury has already started work to review the regime, and as part of this will consider legislative reforms that may be necessary to strengthen the oversight of appointed representatives and to prevent opportunities for abuse of the system. The Treasury is of course working closely with the FCA and will take into account the evidence gathered through the FCA's upcoming data request to firms that use appointed representatives, as well as the FCA's autumn consultation on changes to FCA rules governing the regime.

In addition, the Treasury plans to issue a Call for Evidence to gather views from the broadest range of stakeholders on the overall aim, scope, benefits and risks of the current AR regime.

Information sharing

The report raises the issue of information collection and sharing, and regulatory cooperation, in respect of non-bank finance.[3]

As the report notes, in 2020 the Chancellor asked the Bank of England's Financial Policy Committee (FPC) for a detailed assessment of the adequacy of the risk oversight and mitigation systems for non-banks. In response, the July 2021 Financial Stability Report, alongside analysis provided in the Bank's report 'Assessing the resilience of market-based

2 Paragraph 51
3 Paragraph 76

finance', detailed the work carried out by the Bank so far, alongside other UK regulators, both domestically and internationally, to remediate a number of the data gaps identified by the FPC.

The FPC will continue to use the data and analysis available to scan the horizon for new and growing risks to financial stability as the financial system continues to evolve. The FPC has mechanisms to help inform government policy as needed, including in-depth assessments of particular risks and a power to make recommendations to the Treasury and other regulators, and will continue to work proactively with the regulators to consider such risks. The Treasury will continue to work closely with the Bank, the PRA and the FCA to consider challenges around data collection, and will consider carefully whether any additional powers are required to deliver on financial stability objectives.

Non-bank data gaps remain an international issue that regulators globally are working to address. Given many non-banks operate across multiple jurisdictions, an international solution will be required to effectively mitigate these gaps. To progress this work, the Treasury will continue to strongly support and remain actively engaged in the international work being coordinated by the Financial Stability Board to address these gaps and work with the UK regulators to consider whether any domestic options (e.g. legislative amendments) could improve data collection and mitigate the issue within the UK.

The report also raises the question of whether there is scope to reform the information gateways under the Financial Services and Markets Act 2000 (FSMA) to provide better information sharing in a more timely fashion.[4] I note the Governor of the Bank of England's and Sam Woods' evidence on this, and agree that tight constraints around onward information sharing are important to promote open cooperation between firms and the regulators. Importantly, the FSMA gateway did not prevent the Treasury from sharing the relevant information in this case. Specifically, I would note, as Charles Roxburgh did in his oral evidence of 27 May, that the Treasury did share with BEIS the information it had received from the Bank of England in May and August 2020 concerning Wyelands Bank and GFG.

Changes of control

Regarding potential reforms of the regulatory regime surrounding changes of control of banks,[5] I can confirm that HM Treasury is now working with both the PRA and the FCA to consider how change of control applications are dealt with and what changes might need to be considered, for example to ensure sufficient relevant information is received from an applicant for a change of control, enabling the Regulators to fully assess the risks of the proposal in a timely manner.

Other areas of regulation

I acknowledge the FCA's letter to the Committee regarding other areas where there may be a case for fresh regulation, and in particular the topics listed in paragraph 83 of the Committee's report. I have discussed our work on Appointed Representatives above and can confirm that the FCA's investigation and penalty powers in the event of firm failure, the criteria for fitness and propriety under the Money Laundering Regulations, access to UK investors through listing securities on overseas markets that are not Recognised

4 Paragraph 200
5 Paragraph 82

Overseas Investment Exchanges or regulated markets, and Employer Salary Advance Schemes are the subject of ongoing work, or have been discussed between the Government and the FCA.

The Committee's report highlights the importance of keeping the regulatory perimeter under review. Since 2014, the FPC has been regularly assessing risks beyond the core banking sector and published a series of annual assessments from 2015 to 2019.[6] As noted above, the FPC has a statutory power to make recommendations to HM Treasury in relation to the regulation of the UK financial system, to maintain financial stability. This could involve recommending activities move within the boundary between regulated and non-regulated activities—known as the 'regulatory perimeter'—or recommending changes in regulation for activities already within the perimeter. HM Treasury is represented on the FPC via its non-voting member and will continue to carefully consider any recommendations made by the Committee.

Separately, the FCA publishes an annual perimeter report to give clarity on the FCA's role at the edges of and beyond the perimeter. The Government regularly engages with the FCA on perimeter issues, including through an annual perimeter meeting between the Economic Secretary to the Treasury and the Chief Executive of the FCA, which provides a dedicated forum to discuss issues raised in the FCA's annual perimeter report.

There is of course a fine balance between the costs and benefits of bringing activities into the regulatory perimeter. The Government is committed to ensuring that this balance is maintained, by continually keeping the perimeter under review, and working with the regulators to consider any potential amendments to the perimeter.

Supply chain finance in Government

I note the Committee's comments on supply chain finance, and its observation of the importance of prompt payment to government suppliers.[7] This principle is supported by the Treasury's Managing Public Money (MPM) publication,[8] which states that the public sector should set a strong example by paying promptly. In particular, central government departments should aim to pay 80% of undisputed invoices within 5 days (see paragraph A4.8.4).

I agree that, as a matter of course, public sector organisations should not normally rely on obtaining finance by borrowing from commercial banks or supply chain finance as it is almost always more expensive than relying on the Government's credit rating. This position is set out in MPM (paragraph 5.9.1) and reiterated in a "Dear Accounting Officer" (DAO) letter from June 2019.[9]

As your report notes,[10] MPM is also relevant to the Committee's findings on Greensill's Earnd product. Paragraph 5.12.4 of MPM states: 'When assessing an unfamiliar financing technique, it is important to remember that providers of finance and complex financial

6 See the July 2019 Financial Stability Report: https://www.bankofengland.co.uk/financial-stability-report/2019/july-2019
7 Paragraph 92
8 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1000670/MPM_Spring_21_with_annexes_080721.pdf
9 https://www.gov.uk/government/publications/dao-0219-guidance-on-novel-financing-arrangements
10 Paragraph 101

instruments intend to profit from their business. And providers' costs of finance are always inferior to the UK government's cost of borrowing. So it is usually right to be cautious about any novel techniques. The Treasury will always refuse proposals to speculate.'

The requirement for HMT consent for novel financing techniques is reiterated in the DAO letter mentioned above. Accounting Officers must consider when cases are novel and must be referred to HMT. Even where there is no direct expenditure, repercussive costs resulting from the gratuitous supply of services or propriety issues that flow from the acceptance of such services may require HMT consent.

I should also note that, as you know, the Government commissioned Nigel Boardman to conduct a Review into the Development and Use of Supply Chain Finance in Government, especially the role of Lex Greensill and Greensill Capital. The Boardman Review has recently published its recommendations. The Government will carefully consider its recommendations alongside the work of the Treasury Committee and other bodies, and will set out a substantive Government policy statement in due course.

Greensill's lobbying of Government

While the report highlights the integrity with which the Treasury responded to Mr Cameron's lobbying of the Government, the Committee says that the Treasury should have considered, and as necessary mitigated, any reputational risks to the Government. The report also calls on the Treasury to put in place more formal processes to deal with any such lobbying in the future.[11]

I would note in this regard that, throughout the period of Greensill's engagement, all substantive discussions with Greensill were properly handled and recorded. This not only ensured that the department was able to engage with the Committee's subsequent inquiry accurately and in considerable detail but also that I was receiving high quality and evidence-based analysis of the proposals put forward, which I ultimately rejected.

The report expresses doubt that Mr Cameron's lobbying did not result in the Treasury treating Greensill differently.[12] On this I can only reiterate the evidence we have previously given to the Committee. Greensill and supply chain finance did not take up a very significant part of my time, nor of Charles Roxburgh's, nor of the department's overall, particularly compared with other Covid interventions. In line with the Committee's report, it was right to listen to Greensill's initial proposal, which we promptly rejected. Given the acute financing needs of SMEs at the time, it was also right to invest a small proportion of time and resource in exploring the option of an industry-wide solution for supply chain finance.

However, the ability of former ministers to lobby government—which is restricted today under ACOBA's rules—is a serious and live policy matter for the Government as a whole, in assessing current propriety standards and their application in the digital age. For this reason, the Prime Minister included in the Terms of Reference of Nigel Boardman's work that consideration should be given to 'the relationship between current and former Ministers and officials and Greensill Capital, including processes for consideration and management of conflicts of interest during and following Crown Service'.

11 Paragraph 143
12 Paragraph 204

As set out above, the Government will respond to Mr Boardman's recommendations in due course and the Treasury will follow any resulting cross-government approach.

As regards the Treasury's policy on the deletion of records on mobile devices,[13] I can confirm that this has been put in place having regard to the Minimum Cyber Security Standard (a minimum set of cyber standards that the Government expects departments to adhere to), which states that departments must have the ability to remotely wipe and/or revoke access from an end user device. While we accept that, in exceptional circumstances, this security feature could potentially result in the loss of information that may not have been transferred to the departmental record, in the vast majority of cases, all the substantive information held on the device will also be held on Treasury systems. Given that the aim of the Treasury's policy is to ensure that all data is protected in circumstances where a device is either lost or stolen (where it could potentially be in the possession of malign actors), we consider that the balance of risk falls decidedly in favour of retaining the security feature in order to prevent unauthorised access to Treasury information or data, which is often particularly high-profile and sensitive.

Civil contingency planning

The report recommends that the Treasury liaise with the Cabinet Office to ensure that major emergency planning exercises involve consideration of economic impacts and policy responses.[14]

It is inevitably the case that there will be lessons for Government to learn from the Covid crisis and the Treasury will ensure that it continues to be involved in relevant future policy discussions.

I would like to assure you that the Treasury works closely with the Cabinet Office on contingency planning where appropriate. The Treasury will continue to engage with them and with other departments to assure our capability to understand the full impacts of potential shocks, follow organisational best practice for contingency planning for a crisis, and to respond to and recover from civil emergencies.

As far as the Treasury's own contingency planning goes, it is worth recalling that following the financial crisis, and the 2012 review by Dame Sharon White into the Treasury's management of that episode, the department took steps to increase the flexibility of its workforce to rapidly be deployed to priority areas and strengthen its horizon scanning capabilities. The actions taken in response to the White Review enabled us to respond quickly and flexibly to the Covid crisis.

The department has procedures in place to continually monitor the UK economy, including identifying and preparing for emerging economic risks, as well as to ensure the public finances are resilient to those risks.

While it is difficult to contingency plan for every specific scenario, I believe the department demonstrated its capability to respond quickly and responsibly to the emergence of the pandemic to protect jobs and livelihoods, support businesses and prevent deep long-term scarring to the economy.

13 Paragraph 220
14 Paragraph 216

The UK's Covid support schemes have been among the most generous in the world. The schemes have been widely recognised as successful and a key part of the Government's response to the Covid emergency, saving millions of jobs and protecting the incomes of millions of people.

Thank you again for your comprehensive work on this report. I am proud of our response to the Covid crisis and believe that the department acted entirely appropriately in relation to Greensill. Nonetheless, as I hope that this letter makes clear, we are exploring a number of potential policy avenues identified in your report in relation to financial regulation, and I would be happy to discuss progress on these matters at a future hearing.

Best wishes,

RISHI SUNAK

20 September 2021

Appendix 2: Correspondence between the Bank of England and the Chair of the Committee

Letter to the Chair of the Committee from the Deputy Governor for Prudential Regulation, Bank of England, and Chief Executive Officer of the Prudential Regulation Authority

I refer to the Committee's report of 20 July on Lessons from Greensill Capital. This notes that: *"In retrospect, the Bank, by not informing the Treasury sooner about its knowledge of Greensill's control problems, no matter how relatively unimportant they appeared, may have missed an opportunity. The Bank should review its approach to the disclosure of information on Greensill to the Treasury, to check that it is content with how its systems operated."*

In light of this recommendation from the Committee, we have now reviewed the approach we took to disclosure of information on Greensill to the Treasury, and how our systems operated. We did of course also consider our approach to sharing information we received through our supervision of Wyelands with the Treasury carefully at the time, alongside the approach we took to sharing a range of material information with a number of other authorities, often on a proactive basis. Nonetheless, it is often useful to re-examine these things ex post. Having done this, we are content with our approach and how our systems operated in relation to sharing information on this matter with other authorities, including HM Treasury, and that when it was shared, information was shared sufficiently promptly.

The PRA supervised two entities within the GFG "Alliance": Wyelands Bank and the Commonwealth Trade Bank. It did not supervise any other GFG entities and it did not have any supervisory role in relation to any Greensill entities. The PRA's visibility over the activities and position of Greensill was therefore limited, gleaned from references to Greensill entities in Wyelands' documentation that the PRA reviewed, and, in relation to Greensill Bank AG, such information as supervisers received from BaFin.

Accordingly, as I mentioned in my letter to the Committee of 2 July, we kept HM Treasury informed about the situation with Wyelands Bank plc but our view of Greensill entities was limited. The potentially serious nature of the financial difficulties at Greensill began to become apparent to the PRA in October 2020 when speaking to BaFin but was not evident from the information BaFin shared earlier in 2020. On 3 November, we updated HM Treasury on the information we had received from BaFin. As the problems intensified, we informed HM Treasury of the latest intelligence from BaFin on 27 January and 1 February 2021. Prior to October 2020, we did not pass on to HM Treasury the information we had received from BaFin about weaknesses in controls because it conveyed less serious concerns about Greensill than the October information. It also did not add materially to our pre-existing concerns about the position of Wyelands and its relationship with the GFG Alliance, which we were already sharing with HM Treasury.

Notwithstanding this assessment, this case and the Committee's recommendation do provide a useful reminder of the importance of managing our disclosures about firms to HM Treasury in a thoughtful way, and should help us ensure that we strike the right balance in future cases. There will always of course be an element of judgement in these sorts of matters, and although we are content with the judgements made in this case it does illustrate the importance of those judgements being made in a careful and considered way.

I hope this is helpful to the Committee.

Yours sincerely,

Sam Woods

Deputy Governor and CEO, Prudential Regulation Authority

25 August 2021

Letter from the Chair of the Treasury Committee to the Deputy Governor for Prudential Regulation, Bank of England, and Chief Executive Officer of the Prudential Regulation Authority

Many thanks for your letter of 25 August, in response to our report of 20 July on Lessons from Greensill Capital.

You have told us that the potentially serious nature of the financial difficulties at Greensill began to become apparent to the PRA in October 2020 when speaking to BaFin, but was not evident from the information BaFin shared earlier in 2020—which conveyed less serious information than the information you received in October.

My understanding is therefore that the information you received in March 2020 did not relate to the financial position of Greensill, and was solely related to control failings, and that these control failings did not prompt serious concerns at this time or make it apparent that Greensill would be likely to face financial difficulties in the future. I would appreciate if you could let me know whether this understanding is correct.

Your letter also notes that the PRA updated HM Treasury on the information received from BaFin on 3 November 2021. Please could you provide further clarity as to when exactly in October that information came in from BaFin, and therefore how long it took the Bank to pass on that information?

Finally, please could you tell the Committee at what level of seniority the decision to not pass on the March 2020 information, and the decision to pass on the information in November 2020, was made.

I would be grateful for a response by 20 September 2021.

Rt Hon. Mel Stride MP

Chair of the Treasury Committee

14 September 2021

Letter to the Chair of the Committee from the Deputy Governor for Prudential Regulation, Bank of England, and Chief Executive Officer of the Prudential Regulation Authority

Thank you for your letter of 14 September following up on my letter on 25 August. I am happy to be able to provide further assistance to the Committee in relation to this matter.

As I mentioned in my previous letter, the PRA supervised two entities within the GFG "Alliance": Wyelands Bank and the Commonwealth Trade Bank. It did not supervise any other GFG entities and it did not have any supervisory role in relation to any Greensill entities. The PRA's visibility over the activities and position of Greensill was therefore limited. Further, in relation to Greensill Bank AG, the PRA's information was limited to that which supervisors received from BaFin.

You asked firstly about the nature of the information the PRA received from BaFin in March 2020 in relation to Greensill. This information indicated that work by the Auditing Association of German Banks (*Prüfungsverband deutscher Banken e.V*) was underway at that time in Germany in relation to the level of concentration of Greensill Bank's exposures to GFG entities and the control and reduction of these exposures.

In May, BaFin provided further information to the PRA about Greensill Bank's exposures to GFG. This indicated that no material difficulties had been reported by Greensill Bank with regard to its exposures to GFG.

The PRA updated HMT about additional information received from BaFin on 3 November 2020. You asked when we received this additional information. We received it on 30 October.[15]

You asked about the seniority at which the decisions were taken not to share the March information and to share the October information. The information the PRA received from BaFin in March was preliminary in nature. Therefore, the director of UK Deposit Takers Supervision wrote to BaFin to make it clear that the PRA were keen to understand their view of the position. The information received in May in response to this request did not prompt serious concerns and therefore was not the type of information where the question of dissemination to HM Treasury would be explicitly considered by the PRA. The decision to share the information received in October was taken by the director of UK Deposit Takers Supervision.

I trust this information is of assistance. However, please do not hesitate to let me know if I can provide further clarification to the committee.

Sam Woods

Deputy Governor and CEO, Prudential Regulation Authority

17 September 2021

15 Note that HMT had also been contacted directly by the German Finance Ministry—see Charles Roxburgh's evidence to the Committee on 27 May at Q434.

Appendix 3: Response from the Financial Conduct Authority

Letter from the Chief Executive of the Financial Conduct Authority to the Chair of the Committee

Re: FCA response to the Committee's report on the Lessons from Greensill Capital

I am writing to you in response to the publication of the Committee's report Lessons from Greensill Capital on 20 July 2021 (the Report).

Following my letter of 4 May 2021, the FCA is still formally investigating matters relating to Greensill Capital UK (GCUK) and Greensill Capital Securities (GCSL) and the oversight of GCSL by its principal, Mirabella Advisers LLP (Mirabella). There remain, therefore, some aspects of the FCA's interactions with Greensill entities that I am not able to disclose so as not to prejudice these ongoing investigations.

I have set out below the recommendations relevant to the FCA as well as our response. The recommendations are numbered for ease of cross referencing.

Securitisation

1. The FCA and the Treasury should give serious consideration to revising the definition of "securitisation" within the Securitisation Regulation, given that it appears to have been too narrow. (Paragraph 22)

In the EU and the UK, a securitisation is defined as a transaction or scheme that has at least two stratified risk positions (or tranches) with different levels of seniority, also known as senior and subordinated structures and where the performance of the securitisation depends upon the performance of the underlying exposures. Its definition relies on the concept of "tranching", which creates different categories of credit risk to suit different investors' risk appetite. Investors in the lower tranches are exposed to more losses than those in higher tranches.

This definition is consistent across the Basel II and III frameworks (which were put in place after the 2008 Financial Crisis in which securitisation risks played a significant role), the EU/UK Capital Requirements Regulation (which implements Basel III in the EU/UK) and the EU/UK Securitisation Regulation (which came into force on 1 January 2019).

In comparison, factoring and reverse factoring typically involve the outright purchase of receivables (typically invoices) funded either on the balance sheet of the buyer, or through the issuance of notes in the market. Investors in such notes are typically pari-passu ranking, i.e. all noteholders have the same risk in the receivables. Although the notes are issued out of a Special Purpose Vehicle (SPV), to the extent that there is no tranching of the notes, such schemes do not fall within the definition of securitisation.

Factoring and reverse factoring are an important funding tool for SMEs and have been widely used for some time. Securitisation of trade receivables can be an alternative source of funding, but securitisation is often not economically viable for small SMEs as it is more complex and upfront costs are high.

The definition of securitisation was extensively debated when the Securitisation Regulation was introduced. Many stakeholders considered it very broad as it covers many private and bilateral transactions (so long as there is tranching). For programmes of factoring or reverse factoring to fall within the scope of the Securitisation Regulation, the definition of securitisation would need to be expanded even further and remove the concept of tranching. This would potentially bring in a wide range of new types of lending into the definition.

There are a number of arguments against such an approach:

- If the definition of "securitisation" were to be extended beyond the concept of tranching, it would capture all financing of a pool of exposures or any financing that is backed by a pool of receivables/collateral, and would therefore effectively widen the securitisation framework to cover large parts of the commercial lending market. The majority of commercial lending is currently unregulated. This reflects Government policy of recognising that businesses are considered to be better able to understand and manage risk than consumers, and ensuring that businesses have the greatest possible access to finance.

- A key objective of the Securitisation Regulation was to ensure that banks and insurance companies investing in securitised instruments hold sufficient capital against the risks of these instruments. The calibration of capital comes hand in hand with certain requirements on the structure, disclosure and alignment of interests. As outright purchase of receivables, factoring and reverse factoring already have a separate capital treatment under the capital rules. It is not clear that there is a strong case to change this treatment. The capital requirements in the Securitisation Regulation have not been designed for such transactions. Widening the definition in the UK Securitisation framework would also go beyond Basel III and recognised international frameworks, potentially running counter to Parliament's concerns, for example that we have regard to "*any relevant standards set by an international standard-setting body*" [FS Act 2021, s.143G (1)(a)].

- A second key risk addressed in the Securitisation Regulation was the leverage embedded in the subordinated tranches of securitisations, and the systemic issues arising from that—we have not seen evidence that supply chain finance presents the same degree of leverage or systemic risk.

There is a question, however, of whether some elements of the Securitisation Regulation could benefit commercial lending in general. Those would include, for example, standardised and enhanced disclosure to investors; better origination of risk; and risk retention to align interests and avoid the risks inherent in the "originate-to-distribute" model.

However, we note the public policy approach of focusing regulatory intervention where market participants cannot reasonably be expected to have the capability to understand, choose and manage the risks that they take on. There is an argument that commercial lenders to SMEs can use their commercial influence to obtain the appropriate degree of disclosure and assess the appropriate level of risk, as should fund managers investing in financing of this type through notes such as those described above (we note that the notes issued through the Greensill schemes were not directly sold to retail clients in the UK).

Appointed Representatives

2. The FCA and HM Treasury should consider reforms to the appointed representatives regime, with a view to limiting its scope and reducing opportunities for abuse of the system. (Paragraph 51)

The FCA welcomes the TSC's recommendation that the FCA and HM Treasury should consider reforms to the Appointed Representatives (AR) regime. In considering reforms, we will work with HM Treasury to determine the most effective ways to reduce opportunities for misuse of the regime, including whether limiting the scope of the AR regime is a necessary and effective way to achieve this.

Reviewing use of the AR regime is a priority for the FCA. We highlighted the importance of tackling harms associated with firms who use the AR regime in our 2021/22 Business Plan, published in July.

In recent years, we have focused on a number of risks and potential harms associated with the AR regime. This has included thematic supervisory reviews in the General Insurance and Investment Management sectors, which identified significant shortcomings in principal firms' oversight and understanding of their regulatory responsibilities for their ARs. We also highlighted the risks we see in this model in our 2019/20 Perimeter Report.

We want Principals and ARs to demonstrate appropriate oversight and control of their activities, their financial stability, and that they ensure fair outcomes for consumers when selling products or giving advice. As set out in my letter of 4 May 2021, we are carrying out further work at our gateway for authorisations to achieve this, as well as more targeted supervision to reduce the most significant risks from Principals and ARs. In the autumn, we will also consult on changes to our rules governing this regime to improve and strengthen it. This includes changes to require more timely information on principals and their ARs, and improve Principals' ongoing oversight and due diligence of current and prospective ARs. We will be charging principal firms an annual fee[16] to fund this work.

In the coming weeks we will send a data request to a number of principal firms requiring them to provide additional information on their ARs. The data collection will inform our policy development, support our supervisory work on ARs and inform discussions with HM Treasury on potential legislative changes.

We are also considering whether more fundamental changes are needed to the regime, including legislative change. Since the AR regime is governed by the Financial Services and Markets Act 2000 (FSMA), we have been engaging HM Treasury about such potential changes, including potentially limiting the scope of the regime and other ways to prevent abuse of the system. We will continue to work closely with HM Treasury to establish whether there is merit in legislative changes.

16 £250 per annum for each AR, and £75 per annum for each Introducer AR

Non-bank finance data

3. In addition to international work to intensify global co-operation and data-sharing on nonbank finance, the Treasury should work with the Bank of England and the FCA to consider which domestic data gaps could be addressed. Filling these gaps may require legislative or regulatory fixes. Where there is additional information which could be collected to assist the Bank of England in achieving its objective for financial stability, the Prudential Regulation Authority and Financial Conduct Authority should collect this information, and, if needed, the Government should put forward legislation to enable this. Any information required should be collected on a measured, proportionate basis, taking care not to impose a disproportionate burden either on firms to submit the data or on regulators to review it. (Paragraph 76)

We will continue to work closely with HM Treasury and the Bank of England to consider how best to address non-bank data gaps. We will also support the Bank of England if additional information is required to assist them in achieving its financial stability objective, and will work with HM Treasury if any additional powers are required. We will continue to consider the burden placed on firms for any new data collections that we introduce to ensure the balance of costs to value is appropriate.

Information requirements

4. While the nature of the next civil emergency is unknown, the Treasury should consider what information it needs, in the planning for, and provision of, public support for potential future emergencies. In doing so, it should liaise with the Cabinet Office to ensure that major emergency planning exercises involve consideration of the potential economic impacts and policy response. (Paragraph 216)

We recognise that HM Treasury (and Governments departments generally) may well have different data requirements than we do as a regulator.

I trust the Committee finds this response helpful.

Nikhil Rathi

Chief Executive

17 September 2021