Consultation Paper

Fees regime for financial market infrastructure supervision 2018/19

March 2018

BANK OF ENGLAND

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The Bank of England (the Bank) and HM Treasury (HMT) invites comments on this Consultation Paper. Comments should reach the Bank by 9 May 2018.

Comments may be sent by email to FMIFeedback@bankofengland.co.uk.

Alternatively, please send comments in writing to:
FMI Feedback
Financial Market Infrastructure Directorate
Bank of England
20 Moorgate
London EC2R 6DA

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If you would like the information that you provide to be treated as confidential, please mark this clearly in your response. Under the FOIA, there is a Statutory Code of Practice with which public authorities must comply and which deals, among other things, with obligations of confidence. In view of this, it would be helpful if you could explain why you regard the information you provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances.

In the case of electronic responses, general confidentiality disclaimers that often appear at the bottom of emails will be disregarded unless an explicit request for confidentiality is made in the body of the response.

Copies of this consultation paper are available to download from the Bank's website at www.bankofengland.co.uk.

Purpose

The purpose of this Consultation Paper (CP) relates to the development of the Bank of England's (the Bank) proposal to introduce a new funding structure for the supervision of financial market infrastructures[(1)] and service providers to recognised payment systems (hereafter referred to collectively as 'FMIs'). This consultation is conducted jointly with HM Treasury (HMT) who are also consulting on a statutory instrument (SI). In order for the Bank to levy fees on payment system operators and service providers, HMT must lay an SI approving the scale of fees the Bank can levy.

The Bank initially consulted in August 2017 on the broad approach to levying fees for the supervision of FMIs (the 2017 CP).[(2)] Following the 2017 CP and consideration of the responses received, the Bank has decided to progress with developing a fee-charging regime.

This publication is formed of three parts. Part 1 presents the Bank's feedback to the 2017 CP responses. Part 2 consults on the detail of the proposed fee levying regime, building on the proposals contained in the 2017 CP. Part 3 covers a consultation on HMT's SI which will set out the scale of fees to which fees levied on recognised payment systems and specified service providers must relate.

Parts 2 and 3 of this CP seeks views on:

- The fee ratio between different categories of FMI;
- Estimated fees for 2018/19;
- Fees for operators of multiple recognised payment systems;
- Fee levels for applications;
- The process for levying fees; and
- The SI allowing payment systems and service providers to be levied (on behalf of HMT).

Since the 2017 CP on levying fees on FMIs was published, the Bank's regulatory perimeter has been expanded to include the supervision of specified service providers to recognised payment systems. This CP therefore covers the approach to specified service providers and the Bank seeks views on this approach.

This CP is mainly of interest to FMIs currently supervised by the Bank. It is also of interest to any FMIs who may seek to make certain applications to the Bank, such as for authorisation under the European Market Infrastructure Regulation (EMIR) in accordance with the Financial Services and Markets Act 2000 (FSMA), or for designation under the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (SFR).

This consultation closes on 9 May 2018. The Bank and HMT invite feedback on the proposals set out in this CP. Full responses from recognised payment systems and specified service providers sent to the Bank will be shared with HMT, unless otherwise specified by the respondent. Full responses from any other interested parties that cover the SI will also be shared with HMT, unless otherwise specified by the respondent. Please address any comments or enquiries to FMIfeedback@bankofengland.co.uk.

The Bank will consider the feedback received and will issue a policy statement in due course. The regime is expected to come into force after the HMT SI has taken effect. The Bank currently expects this to be in 2018 Q3.

Background

As set out in its published approach to FMI supervision the Bank supervises FMIs with a forward looking, risk-based approach, '*…prioritis[ing] its supervisory effort based on its assessment of where risks to financial stability are greatest*'.[(3)]

Within the Bank, the Financial Market Infrastructure Directorate (FMID) has responsibility for supervising FMIs. In order to undertake its supervisory activities effectively, FMID draws in specialist resource and expertise when required from other areas of the Bank including the Prudential Regulation Authority (PRA). The Bank currently funds its supervision of FMIs through cash ratio deposit (CRD) revenue.[(4)]

In February 2017, the Bank's Independent Evaluation Office (IEO) published its evaluation of the Bank's approach to FMI supervision.[(5)] The IEO report recommended that the Bank reviews its approach to funding FMI supervision and to consider whether levying fees on supervised FMIs would be appropriate.

The Bank consulted on the broad approach to levying fees on FMIs in the 2017 CP. The 2017 CP covered the overall approach to levying fees based on the categorisation of FMIs, the legal powers that the Bank has to do so, the population of FMIs affected and an estimation of what annual fees may be, based on the 2017/18 budget and population of supervised FMIs.

Following this consultation and considering the feedback received, the Bank has decided to progress developing a fee

(1) Central counterparties (CCPs), central securities depositories (CSDs) and payment systems.
(2) See www.bankofengland.co.uk/-/media/boe/files/paper/2017/levying-fees-for-financial-market-infrastructure-supervision.pdf.
(3) See www.bankofengland.co.uk/-/media/boe/files/financial-stability/financial-market-infrastructure-supervision/the-boe-approach-to-the-supervision-of-fmi.pdf.
(4) Cash ratio deposits (CRDs) are non-interest bearing deposits lodged with the Bank by eligible institutions. The interest earned from the deposits is used by the Bank towards funding its operations. The CRD scheme is being reviewed in 2018. This funding model was set out in the Bank's published approach to supervision when it assumed its new responsibilities for FMI supervision in 2013, see www.bankofengland.co.uk/financialstability/Documents/fmi/fmisupervision.pdf.
(5) See www.bankofengland.co.uk/independent-evaluation-office/fmi-supervision-february-2017.

levying regime. The Bank has concluded that levying fees on supervised FMIs is a more proportionate allocation of costs as it better reflects the recipients of the Bank's supervision. The FMI fee regime would align the Bank's FMI supervisory funding approach with that of the PRA. It will also provide greater transparency and accountability in the delivery of the Bank's FMI supervision functions.

HMT issued a consultation on the renewed CRD in February. That paper proposes that the fees for FMI supervision would no longer be funded from the CRD.(6)

Part 1: feedback to consultation responses

The Bank received eight responses to the 2017 CP on the broad approach to levying fees for the supervision of FMIs. Respondents were broadly supportive of the proposals but did raise a number of specific issues and questions on the details of the approach. These are discussed below by topic with the Bank's response and any action proposed to take.

Definition of 'special project'

The 2017 CP set out that fees charged to FMIs could include work on special projects that fall under the Bank's supervisory remit for FMIs and are in the scope of the Bank's fee-levying powers. While FMIs could see the advantage in levying fees in this way they wanted more clarity on how such projects were defined and how FMIs could plan for them.

As a general principle the Bank considers special projects to be one-off or significant activities that may be time limited and require additional supervisory resource. This could apply to a specific FMI or a group of FMIs. An example that triggers a special project fee could potentially be a change within an individual FMI such as a large scale restructure that requires additional specific supervisory work and analysis. The Bank expects to levy this fee infrequently and will engage with the FMI or FMIs in the relevant circumstances.

Volatility in levy

As outlined in the 2017 CP the Bank consulted on working on a cost recovery basis in its fee regime. Some respondents mentioned that this approach could create some budget uncertainty as the Bank could recover additional costs at the end of the fee year that were unplanned for by an FMI.

The Bank acknowledges FMIs' concerns and will endeavour to set fees at an appropriate level for the year, therefore minimising this risk. If the Bank becomes aware of exceptional circumstances that will trigger the need to recoup further costs at the end of the year, we will endeavour to give FMIs early notice of this fact, where possible. The Bank believes the current approach of charging on a year by year basis, including the possibility of recovering additional costs, is proportionate but will keep this approach under review.

Scrutiny

A small number of respondents asked about how the Bank was going to ensure that the fees levied were subject to appropriate scrutiny.

The Bank will consult every year on the fees for FMI supervision which will provide the industry with the opportunity to respond. The Bank also publishes an Annual Report on its FMI supervisory work which sets out the work delivered for the year; this enables those interested to understand how the Bank is making use of its resources.

In addition, FMI supervision fees will be included as a separate line in the Bank's annual accounts which are published as part of the Bank's *Annual Report*. This will mean the FMI fee will be subject to scrutiny by the Bank's external auditors.

Impact on participants

A number of respondents questioned how FMI fees would impact their participants and what guidance the Bank was going to give around passing fees on to participants.

The Bank supervises, and has powers in relation to, the operators of market infrastructure and service providers to payment systems rather than participants in the system. The Bank therefore only has the power to levy fees on the operator or service provider. FMIs should consider their own payment structures and tax obligations in regard to fees.

Role of the Bank of England

Respondents to the 2017 CP raised questions relating to the Bank in its role both as a participant in payment systems and as an operator.

The 2017 CP was clear that the high value payment system (HVPS) being brought in-house would not lead to their regulatory costs being passed on to other recognised payment systems. The Bank, as operator of the HVPS, will pay a proportionate share of the cost of supervision on a non-statutory basis which will be recovered alongside other running costs.

Separately, where the Bank is a direct participant in an FMI, it will contribute its proportionate share for the purposes of any fees arising from the Bank's supervision of FMIs.

Co-ordination with Payment Systems Regulator (PSR)

A number of the payment system operators raised the need for co-ordination with the PSR.

Some payment systems are dual regulated by both the Bank and the PSR. The Bank has a duty to co-ordinate with the PSR,

(6) See www.gov.uk/government/consultations/review-of-the-cash-ratio-deposit-scheme-consultation-on-proposed-changes.

and the Bank, PRA, Financial Conduct Authority (FCA) and PSR have a Memorandum of Understanding (MOU) to cover how this co-ordination works. The MOU is reviewed every year at a senior level, and in the reviews undertaken to date, co-operation has been found to be working well.[7] The Bank is seeking to align the operational side of the fees regime with the PSR's timeline for levying fees and this should help FMIs manage the administrative burden. The Bank will continue to discuss common ways of working with the PSR.

Part 2: detail on the proposed fee-charging regime

Background

The 2017 CP proposed to introduce 'fee blocks' for each type of FMI (ie separate fee blocks for: payment systems; CCPs; and CSDs). The purpose of this approach is to minimise cross-subsidisation between FMI type. It also set out that FMIs would be charged based on their category, which reflects their potential capacity for disruption to the financial system, linking fees to the Bank's mission to promote the good of the people of the United Kingdom by maintaining monetary and financial stability. No respondent disagreed with these broad principles and following the last consultation the Bank is continuing with this approach.

This CP is seeking views on more granular details of the proposed fee levying regime on FMIs, namely the fee ratio between different categories of FMI, the fees for the 2018/19 fee year, fees for operators of multiple recognised payment systems, the level of application fees and the process for levying fees. It also sets out how specified service providers could be charged fees.

Fee blocks

As service providers to a recognised payment system are now within the Bank's regulatory perimeter, as detailed above, we propose to include any specified service providers within the payment system fee block, as outlined in **Table 1**.

Table 1 The FMIs supervised by the Bank and their respective fee blocks

Central counterparties (CCPs)	Central security depository (CSD)	Payment systems and specified service providers
ICE Clear Europe Limited	Euroclear UK & Ireland Limited (EUI)	Bacs
LCH Limited		CLS
LME Clear Limited		FasterPayments Service (FPS)
		LINK
		Visa Europe

The fee ratio between different categories of FMI

As explained in the 2017 CP, the Bank's supervision of FMIs and use of its supervisory resources is based on the risks presented by each type of FMI, the systemic importance of each individual FMI and therefore the potential impact that each FMI may present to the stability of the financial system. All FMIs supervised by the Bank are categorised into one of three categories for CSDs and CCPs or one of two categories for payment systems and service providers,[8] according to their potential capacity to cause disruption to the financial system. These categories will be the basis for their respective fees. The Bank is now consulting on how fees will be allocated across the categories within each fee block. The proposed ratios below reflect the different challenges posed in supervising the different FMI types. Supervisory effort has been used as one of the proxies for determining the respective systemic importance of the FMIs.

- For CCPs the proposed ratio between category one, category two and category three firms is 1.75:1:0.57.
- For CSDs the proposed ratio between category one, category two and category three firms is 1.5:1:0.67.
- For payment systems and specified service providers the proposed ratio between category one and category two firms is 1.5:1.

Table 2 shows these ratios applied to the budget for 2018/19.

Table 2 Fees broken down by fee block and category of FMI[(a)]

	Central counterparties (CCPs)	Central security depository (CSD)	Payment systems and service providers
Category 1	£1.95 million	£1.05 million	£495,000
Category 2	£1.12 million		£330,000
Category 3			

Note: This encompasses the costs of supervision and the cost of any central services that directly support supervision.

(a) Category rows have been left blank for which there are no currently recognised firms.

Estimated fees for 2018/19

The fees charged for FMI supervision over the 2018/19 fee year are expected to be as follows.

2018/19 is expected to be a shortened fee period as the Bank is waiting on the SI to take effect, which will set out the scale of fees to which fees levied on recognised payment systems

(7) See www.bankofengland.co.uk/-/media/boe/files/annual-report/2018/supervision-of-financial-market-infrastructures-annual-report-2018.pdf?la=en&hash=58A07611A193B1C549E4A443DF3D0E7D19B23A95.
(8) Payment systems and service providers to payment systems are not authorised by the Bank under FSMA. Due to the threshold for recognition or specification by HMT, a recognised payment system or specified service provider would not be categorised as category 3 by the Bank.

and specified service providers must relate, before it can commence the full regime. The exact date is dependent on Parliament, but the Bank currently expects, following the passing of the required SI, the regime to go live in 2018 Q3. Accordingly the fees for all FMIs will be prorated based on the number of months remaining until the end of February 2019.

The FMI supervision fee regime is expected to work on a cost recovery basis, as noted in the 2017 CP, therefore there is the potential for the amount billed to FMIs to be greater or less than the amount stated above.

Fees for operators of multiple recognised payment systems

Under the Banking Act, HMT recognises payment systems, rather than the operator of the system. This means that there can be two or more recognised payment systems operated by a single legal entity. In these cases the Bank will consider the appropriate fee on a case by case basis. However the minimum the Bank will charge is the fee for the lowest category payment system (eg category one if at least one scheme is in this category) and the maximum is the fee for all systems combined (ie if a firm operates a category one payment system and a category two payment system, the maximum the operator will pay is the category one fee plus the category two fee). The decision on the level of fees will reflect the overall importance of the operator, the supervisory work required and the resources allocated to the supervision of this type of operator. It also reflects the benefits gained from some economies of scale. Because the efficiency gains will be case specific they will be discussed separately with each operator, however an operator of more than one system will be able to ascertain the maximum fee they could expect to pay.

Fee levels for applications

As noted in the 2017 CP, the Bank has powers to charge fees in relation to certain specific applications. The firms to which these fees could apply is broader than the current population of Bank supervised FMIs, and could include non-supervised FMIs or bodies seeking authorisation, as well as currently supervised FMIs. No FMI will be charged for an authorisation it already holds or for an application it has already made.

The level of the proposed application fees has also been determined based on the principle of cost recovery and the Bank's expected work effort in handling each type of application. There is expected to be one fee rate for each application type. The amount of each application fee will be kept under review to determine whether they are set at an appropriate amount. At the time of publication, the application fees are intended to be the following, set out in **Table 3**.

All application fees are payable at the time of application. If the cost of work required is greater or lesser than the fee charged the Bank will recover the difference or refund, where it is proportionate to do so.

Table 3 Application fees

Application fee payer	Fee payable (£)
• Fees for UK-based CCPs seeking authorisation under EMIR in accordance with FSMA.	300,000
• Fees for UK-based CSDs seeking authorisation under the Central Securities Depositories Regulation (CSDR) in accordance with FSMA.	250,000
• Fees for FMIs seeking designation under the SFR, where the Bank is the relevant designating authority.	5,000
• Fees for overseas CCPs applying under section 170B of the Companies Act 1989 for an order of the Bank recognising that the relevant provisions of that CCP's default rules satisfy the relevant requirements.	5,000

In the 2017 CP the Bank proposed charging an application fee for persons seeking approval as operators of relevant systems under the Uncertificated Securities Regulations 2001 (USRs). However, as part of the CSDR implementation in the UK, HMT have proposed amendments to the USRs removing the power that permits the Bank to levy fees for these applications,(9) therefore the Bank has not set a fee level for this type of application.

Process for levying fees

The Bank's fee year is 12 months from 1 March to the end of February. New fee rates are intended to take effect from 1 March in each year. The Bank intends to consult annually on fee rates. The Back acknowledges that FMIs may need sufficient time to plan for the payment of fees. The intention, therefore, is to follow a set annual process starting from the fee year 2019/20. From that budget year and for each subsequent year, it is expected that the Bank will publish a public consultation in Q1 setting out the expected fee rates for that year. This will give industry an opportunity to respond to our consultation on annual fee rates as they are set.

Following that public consultation, it is expected that the Bank will publish a policy statement in Q2 of each budget year which confirms the fee rates for that budget year, as well as feedback from the consultation and any agreed policy changes. Invoices will be issued to FMIs soon thereafter and it is expected to be no later than Q3 of that budget year. Invoices will be issued with 30 day payment terms.

Where significant policy changes are envisaged to the fee regime, for example a change in methodology, the Bank may consult on these separately. This could be expected to take place in the autumn preceding the start of the fee year in which they are intended to take effect.

(9) See www.gov.uk/government/consultations/consultation-on-the-implementation-of-the-central-securities-depositories-regulation-csdr/consultation-on-implementing-csdr.

For the 2018/19 fee year the regime (including application fees and fees for supervision) will not come into effect until after the SI has taken effect, therefore, the start date of the regime is currently dependent on Parliamentary procedure. Our expectation is that for 2018/19 invoices for supervision fees should be sent out within three months of the regime coming into force.

If it appears to the Bank, in relation to any fee, that in the exceptional circumstances of a particular case it would be inequitable to require payment or to retain sums previously paid, it may at its discretion:

- waive the payment;
- reduce the amount payable; or
- offer a whole or partial refund of sums already paid.

Part 3: statutory instrument allowing payment systems and service providers to be levied

As previously noted, in order for the Bank to levy fees on Payment System Operators, HM Treasury must lay an SI approving the scale of fees the Bank can levy.

HMT has agreed in principle that the Bank may levy fees on recognised payment systems and service providers to payment systems of no greater than £760,000 and no less than £200,000 per firm per annum.

The proposed upper bound is based on the Bank's estimation of the potential maximum cost to the Bank of supervision of a payment system or service provider per annum over the next five years.

The proposed lower bound is based on the Bank's estimation of the minimum cost to the Bank of oversight of a payment system or service provider per annum over the next five years.

The Bank may also face costs for 'special projects'. Therefore in addition HMT intends to approve a limit on special project fees of £500,000 per firm per annum.

The intended SI will only provide for the Bank to recoup the costs related to supervision, and not other functions performed by the FMI Directorate, for example research. It will not enable the Bank to levy fees that exceed those costs. As noted elsewhere in the consultation, the Bank currently recoups the cost of oversight from the CRD. Therefore, the fees that the Bank will be able to levy as a result of the SI will result in an equivalent fall in the income required through the CRD scheme over the 2018–23 period, making the net cost to the financial sector of the fee scheme zero.

The total costs of supervision to the Bank include the expenditure on resources required to conduct an annual assessment of each overseen institution, to ensure that their practices are in line with internationally agreed requirements; and the expenditure on resources required to carry out the Bank's core assurance programme, which ensures that firms are appropriately mitigating the risks they face.

As with other fees the Bank levies on supervised firms, the Bank will consult on the fees it intends to levy for the following year, and will take account of representations made. For special projects the Bank will liaise with the firm or firms in the relevant circumstances.

To note, responses should be sent to the Bank of England, rather than HMT. The Bank will share responses received in respect of this draft SI with HMT.

Other matters

Having had regard to the public sector equality duty under the Equality Act 2010, the Bank does not consider this proposal to have any implications for equality matters. The aims behind the proposed funding arrangements include greater transparency and accountability in the delivery of the Bank's FMI supervision functions.

Feedback to this consultation

This consultation closes on 9 May 2018. Please send comments to FMIfeedback@bankofengland.co.uk by this date. Full responses from payment systems and service providers will be shared with HMT for the purposes of their SI, unless otherwise specified by the respondent. Full responses from any other interested parties that cover the SI will also be shared with HMT, unless otherwise specified by the respondent.

The Bank will consider the feedback received and will issue a policy statement in due course. The regime is expected to come into force once the SI has taken effect. The Bank currently expects this to be in 2018 Q3.