

12 August 2020

Joanne Thambyrajah
Ministry of Justice
102 Petty France
London SW1H 9AJ



Dear Ms Thambyrajah

Consultation on the departure from retained E.U. case law by U.K. courts and tribunals

The role of the Financial Markets Law Committee (the "FMLC" or the "Committee") is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.

According to the European Union (Withdrawal) Act 2018 (the "**2018 Withdrawal Act**"), as amended by the European Union (Withdrawal Agreement) Act 2020 ("**2020 Withdrawal Act**"), on 31 December 2020, when the Transition Period between the U.K. and E.U. ends, U.K. courts and tribunals will cease to be bound by the principles laid down by the Court of Justice of the European Union ("**CJEU**"). The 2018 Withdrawal Act created a new category of law in the U.K.: "retained E.U. law".¹ Retained E.U. law, as far as it is unmodified at the end of the Transition Period, is to be interpreted in line with retained case law, which comprises retained domestic case law and retained E.U. case law.² Sections 6(4) of the 2018 Withdrawal Act states that the U.K. Supreme Court and the High Court of Justiciary in Scotland have jurisdiction to depart from retained E.U. case law, and, as per section 6(5), in so doing the courts must apply the rules they respectively exercise in departing from their own previous case law.

Section 26(1) of the 2020 Withdrawal Act empowers HM Government to designate additional courts and tribunals (over and above those already mentioned above) as having the ability to depart from retained E.U. case law. The Ministry of Justice is now consulting on whether to extend the power to other courts and tribunals and, if so, which test should be applied and factors considered in any decision by a court or tribunal to depart from retained E.U. case law.

Courts

The Consultation sets out two options: (1) to extend the ability to depart from retained E.U. case law to the Court of Appeal and equivalent courts; or (2) in addition to the Court of Appeal and equivalent courts, to extend the ability to depart from retained E.U. case law to the High Court of Justice and its equivalent courts.³ The FMLC would urge HM Government not to extend the ability to diverge from retained E.U. case law as set out in either option. The FMLC has drawn attention in past publications to the complexities which will arise if the U.K. diverges in haste from E.U. law. Brexit already presents immense legal and operational uncertainty. The possibility that U.K. courts may deviate unexpectedly on established issues presents legal uncertainty with significant market impact, supplementing the operational challenges caused by the increased likelihood of inconsistent first-instance judgments and the lengthier-than-usual waiting times for hearings at the Court of Appeal and Supreme Court.

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Further, U.K. courts will still be bound by the text of retained E.U. law. The ability to depart from retained EU case law will not allow courts to re-write that text but only to depart from interpretative decisions of the Court of Justice of the European Union. While the U.K. should be able to resolve any cases in which retained E.U. case law is shown to be inappropriate or wrong satisfactorily on (final) appeal, a governmental policy of allowing other courts and tribunals to depart from retained EU case law will introduce unnecessary uncertainty into UK law. It may also create difficulties in establishing similarity with the E.U.'s financial markets framework for the purposes of equivalence assessments for access to the E.U. markets. Should it become necessary to deviate from retained E.U. law, the onus should fall upon Parliament to consider this carefully in terms of a policy change.

The Consultation expresses concerns about the practical impact of permitting only the Supreme Court and the Court of the Judiciary to deviate from retained case law: access to these courts is subject to a restrictive test for permission to appeal and the courts may be overburdened or overwhelmed by the volume of cases and U.K. law may become less agile in reacting to changes. If these concerns seem to HM Government inevitable and damaging, it could consider electing for Option 1 and extend the ability to depart from retained E.U. case law to the Court of Appeal and equivalent courts but, in such circumstance, the test to be applied becomes even more important, as discussed below.

The test and other considerations

With regards the test to be applied in the course of any consideration about departing from retained E.U. law, the FMLC has previously urged HM Government to consider offering principles to the judiciary by which it can evaluate consistently whether consideration should be given to post-Brexit CJEU judgments.⁴ In a similar vein, if the ability to depart from retained E.U. case law is extended to the lower courts, the FMLC would recommend that a stricter test is imposed that that which is applied by the Supreme Court currently. This may be that the court must be satisfied that the retained E.U. case law is wrong or otherwise inappropriate in the light of the U.K.'s withdrawal from the E.U. The Committee would also urge HM Government to include provisions which confer upon judges the ability to request from relevant bodies, such as the FCA, *amicus briefs* which provide judges with the necessary background.⁵

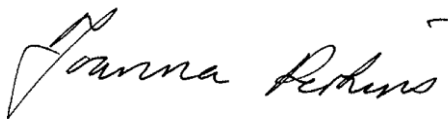
It might be helpful to reflect on an example of a case in which the interpretation of key E.U. regulatory concepts by the CJEU has had the ability significantly to affect the financial markets. The definition of “derivative” (and, correlatively, the definition of “spot”, since “spot” contracts are not “derivative” contracts) under the regulatory regime for markets in financial instruments.⁶ Foreign exchange derivatives such as forwards are regulated under this regime but spot foreign exchange contracts are not. The settlement cycle, however, means that spot contracts are settled forward of the parties entering into the contract. Thus, the boundary between “spot” and “forward” is a nuanced one with a penumbra of uncertainty. The U.K. Financial Services Authority (“FSA”)—and subsequently the Financial Conduct Authority (“FCA”)—developed a practice of using the concept of “commercial purposes” as the basis for distinguishing the two contracts but other E.U. Member States took a different approach. Owing to the substantial uncertainty to which this divergence gave rise, the European Commission was asked for guidance by the European Securities Markets Authority (“ESMA”) and issued a retrospective opinion under Directive 2004/39/EC on markets in financial instruments (“MiFID I”). A legislative definition was then introduced for the purposes of Directive 2014/65/E.U. on markets in financial instruments (“MiFID II”). It is possible, however, that given the importance of the issue and the impact of such divergent approaches, this issue would have become a question for the CJEU to address in the absence of a legislative definition.

It is also possible that the CJEU would have adopted an interpretation with which the FCA would, questions of comity aside, not have been inclined to concur. Post-Brexit, such divergence could well see the question on the meaning of “spot contract” referred to the U.K. judiciary. The risks which the courts’ approach might pose for the markets would be the alternate risks of inadvertently regulating an unregulated and thriving foreign exchange spot market, which is essential to commercial activity of all kinds, or deregulating certain foreign exchange derivatives markets and potentially jeopardising an equivalence decision. Given the significance of the question to the financial markets, its evident impact on the conduct and nature of foreign exchange business, the size of the foreign exchange markets in London and the highly technical material which would be necessary to reach an informed decision on the point, the U.K. courts would likely find it helpful to receive guidance not only on the technical issues but also on the degree to which their decision should “track” or even “reflect” the decision of the E.U.

A separate issue arises with respect to new decisions of the CJEU, which will not be retained E.U. case law under the Withdrawal Act, concerning terms in E.U. legislative measures which were retained by the U.K. and incorporated in domestic law as “retained E.U. law”. These decisions will not have any special status under the Withdrawal Act and the FMLC notes that, in the absence of statutory direction, U.K. courts customarily treat foreign court judgments on identical laws as persuasive but short of binding. HM Government may wish to consider further, in light of the comments above, the impact that divergence between E.U. and U.K. case law in respect of identical or very similar legislative measures may have in certain sectors and to consider further whether guidance to judges on the matters to be taken into account could usefully be developed in collaboration with the judiciary as a whole.

I and Members of the Committee would be delighted to meet you to discuss the issues raised in this letter. Please do not hesitate to contact me should you wish to arrange a meeting or if you have any questions.

Yours sincerely,

A handwritten signature in black ink that reads "Joanna Perkins". The signature is written in a cursive, flowing style.

Joanna Perkins
FMLC Chief Executive

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- ¹ Section 2 (*Saving for E.U.-derived domestic legislation*) provides that any E.U.-derived domestic legislation—i.e., any enactment made by HM Government under section 2(2) of the European Communities Act 1972 (the “**ECA**”) to facilitate the application in the U.K. of an E.U. regulation—that has effect in domestic law immediately before Exit Day will continue to have effect on and after Exit Day. Section 3 of the Withdrawal Act provides for the incorporation of “direct E.U. legislation”, which includes, per Section 3(2), any E.U. regulation, decision or tertiary legislation which has effect immediately before Exit Day. Section 4 of the Withdrawal Act makes provisions to make available, post-Brexit, rights, powers, liabilities, obligations, restrictions, remedies and procedures which are recognised and available immediately before Exit Day. Section 6(7) of the 2018 Withdrawal Act provides that “retained law” is “anything which, on or after exit day, continues to be, or forms part of, domestic law by virtue of section 2, 3 or 4 or subsection (3) or (6) above (as that body of law is added to or otherwise modified by or under this Act or by other domestic law from time to time)”
- ² See section 6(7) of the 2018 Withdrawal Act.
- ³ See pp. 17-18 of the Consultation.
- ⁴ FMLC, *Letter to Ministry of Justice: Clause 6 of the Withdrawal Bill* (19 March 2018), available at: <http://fmlc.org/letter-to-ministry-of-justice-u-k-withdrawal-from-the-e-u-19-march-2018/>
- ⁵ In view of the fact that this solution would require the cooperation of the U.K. regulatory authorities, Karen Levinge and Rob Price took no part in the preparation of this letter and the views expressed should not be taken to be those of the FCA and the Bank of England.
- ⁶ The MiFID regulatory regime comprises Directive 2004/39/EC on markets in financial instruments (“**MiFID I**”), which has now been replaced by Directive 2014/65/E.U. on markets in financial instruments (“**MiFID II**”) and Regulation (E.U.) No 600/2014 on markets in financial instruments (“**MiFIR**”).