



DIRECTORATE-GENERAL FOR INTERNAL POLICIES

POLICY DEPARTMENT **A**
ECONOMIC AND SCIENTIFIC POLICY



Potential Concepts for the Future EU-UK Relationship in Financial Services

Economic and Monetary Affairs

Employment and Social Affairs

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Industry, Research and Energy

Internal Market and Consumer Protection

Potential Concepts for the Future EU-UK Relationship in Financial Services

Study for the ECON Committee



DIRECTORATE GENERAL FOR INTERNAL POLICIES
POLICY DEPARTMENT A: ECONOMIC AND SCIENTIFIC POLICY

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STUDY

Abstract

This study assesses the key impacts of the United Kingdom's exit from the European Union on the financial system and its infrastructures, on financial firms and financial services under three alternative concepts for the future EU-UK relationship. In addition to the impact on the 'passporting rights' of financial firms, particular emphasis is given to the impact on the regulatory framework governing i.a. credit institutions under a 'third-country status' scenario for the UK, the impact on payment systems and market infrastructures, as well as to certain aspects of the EU institutional framework governing the monetary and the financial system could be affected.

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LIST OF ABBREVIATIONS

| | |
|---------------|--|
| BIS | Bank for International Settlements |
| BoE | Bank of England |
| BRRD | Bank Recovery and Resolution Directive (2014/59/EU) |
| CRD IV | Capital Requirements Directive (2013/36/EU) |
| CRR | Capital Requirements Regulation (575/2013) |
| DGS | Deposit Guarantee Scheme |
| EBA | European Banking Authority |
| EBC | European Banking Committee |
| ECB | European Central Bank |
| EEA | European Economic Area |
| EFTA | European Free Trade Association |
| EIB | European Investment Bank |
| EIOPA | European Insurance and Occupational Pensions Authority |
| EMIR | European Market Infrastructure Regulation (648/2012) |
| EMU | Economic and Monetary Union |
| ESAs | European Supervisory Authorities |
| ESCB | European System of Central Banks |
| ESFS | European System of Financial Supervision |
| ESMA | European Securities and Markets Authority |
| ESRB | European Systemic Risk Board |

| | |
|-----------------|---|
| EU | European Union |
| FCA | Financial Conduct Authority |
| FSB | Financial Stability Board |
| G20 | Group of twenty |
| GATS | General Agreement on Trade in Services |
| MFN | Most Favoured Nation |
| MIFID II | Markets in Financial Instruments Directive (2014/65/EU) |
| MREL | Minimum Requirement for (own funds and) Eligible Liabilities |
| MTFs | Multilateral Trading Facilities |
| OJ | Official Journal of the European Union |
| PRA | Prudential Regulation Authority |
| SEPA | Single Euro Payments Area |
| SRM | Single Resolution Mechanism |
| SSM | Single Supervisory Mechanism |
| TARGET2 | Trans - European Automated Real - time Gross settlement Express Transfer system |
| TEU | Treaty on European Union |
| TFEU | Treaty on the Functioning of the European Union |
| UCITS | Undertakings for Collective Investment in Transferable Securities |
| UK | United Kingdom |
| WTO | World Trade Organisation |

EXECUTIVE SUMMARY

The study assesses the key impacts of the United Kingdom's (UK) exit from the European Union (EU) on the financial system and its infrastructures, on financial firms and on financial services under alternative potential concepts for the future relationship between the EU and the UK. Moreover, it explores the impact of the UK's exit from the EU on the EU institutional framework governing the monetary and the financial system.

The main alternative options which could govern both, the UK financial firms operating in the EU and the EU financial firms operating in the UK are explored (application of GATS; bilateral trade agreements; and membership of the European Economic Area (EEA)). The difference between financial firms established in the form of subsidiaries and established in the form of branches is explained because the EU single passport and hence the EU freedoms of establishment and to provide services are important to the branches or the provision of services cross-border without establishment. The passporting issues are a very important aspect, but not the only legal issue arising from the UK's exit from the EU. For this reason, the study is not confined to passporting issues, but also assesses the impact of the UK's exit from the EU on regulatory aspects in regard to credit institutions, such as micro-prudential supervision, reorganisation, resolution and winding-up, as well as participation in deposit guarantee schemes. The impact on payment systems and market infrastructures under a 'third country' regime is also examined.

Chapter 1 ('The conceptual framework') lays the building blocks of the study. In that respect, it firstly reviews the main modes of supplying financial services at international level. Then it draws attention to the wide perimeter of financial firms and trading venues to be affected by the future EU-UK relationship in the field of financial services, since such services are currently provided by a wide range of financial firms under the conditions laid down in EU law. Finally, it presents the position of the Bank of England and other UK administrative financial authorities within the international institutional framework governing the financial system as well as their importance, taking into account that several legal acts of EU financial law are based on the work of these international fora, hence it can be expected that the UK will continue, after its exit from the EU, to comply with their main provisions.

The first section of **Chapter 2** explores three main concepts for the future relationship between the EU and the UK:

- the global regime of a third country under the General Agreement on Trade in Services (GATS) of the World Trade Organization (WTO);
- bilateral trade agreements; and
- membership of the European Economic Area (EEA).

The analysis then turns to the impact on financial firms, markets and infrastructures under the alternative concepts. Undoubtedly, the main issue is the impact on the 'passporting rights' of UK and EU financial firms, i.e., the continuation or discontinuation of UK financial firms' right to have access, through branches and provision of services without (permanent) establishment, to the EU single market by virtue of the single passport under the different concepts which could govern the future EU-UK relationship. The same applies also to EU financial firms as to their activities in the UK financial marketplace. An aspect of legal (and strategic) importance is that this impact does not significantly affect the legal position of subsidiaries established by UK financial firms in the EU and the subsidiaries established by EU financial firms in the UK (apart from business considerations which are beyond the scope of this study), since in both cases subsidiaries remain to be subject to the national legislation of the country in which they are established.

The emphasis in **Chapter 3** is given to two equally important issues:

- the first is the impact on the regulatory framework governing UK and EU credit institutions under a ‘third-country status’ scenario for the UK, including their micro-prudential supervision, reorganisation, winding-up and resolution, as well as their participation in deposit guarantee schemes, and
- the impact on payment systems and market infrastructures.

In this respect, the framework governing the micro-prudential supervision of the EU branches of UK financial firms and the UK branches of EU financial firms, their reorganisation, resolution and winding-up, as well as the participation of credit institutions’ branches in deposit guarantee schemes and the participation of credit institutions’ and investment firms’ branches in investor compensation schemes will also be affected, almost to the same extent as their ‘passporting rights’. To a much lesser extent implications will also be evident for the subsidiaries of these financial firms.

In addition, under the scenario of the third-country regime, another significant aspect under examination is the impact on payment systems and market infrastructures, including the EU large-value payment system ‘TARGET2’, the ‘Single Euro Payments Area’ (SEPA), and the financial infrastructures for clearing and reporting transactions, taking into account the huge volume of transactions settled through payment systems, the crucial role of market infrastructures for the smooth operation of financial systems, and the significance of the interconnectedness between payment systems and market infrastructures.

Chapter 4 (‘Institutional aspects’) explores the aspects of the EU institutional framework governing the monetary and the financial system to be affected by the future EU-UK relationship in financial services. After a brief review of the implications concerning the European Investment Bank (EIB) and the four ‘Comitology Committees’, the study focuses on the impact of the UK’s exit from the EU:

- on the capital of the European Central Bank (ECB) and decision-making within its General Council, and
- the two pillars of the European System of Financial Supervision (ESFS), i.e., the European Systemic Risk Board (ESRB) and the European Supervisory Authorities (ESAs).

The impact of the UK’s exit from the EU is expected to be of substantial significance for the financial system, its infrastructures, financial firms and financial services both in the UK and in the (other) EU Member States. This study does not cover the entire diversified range of implications of the UK’s exit from the EU. Aspects not dealt with include, e.g. the impact on consumer protection in the field of financial services, on anti-money laundering arrangements, and on data protection.

In addition, the focus of the analysis in **Chapters 2 and 3** is mainly on passporting and the regulatory impacts on credit institutions (and to a certain extent on investment firms). Nevertheless, it is expected that it lays the groundwork for further research into passporting and the regulatory impact on insurance and re-insurance companies, as well as the regulatory impact on investment firms and other regulated financial firms in capital markets.

1. THE CONCEPTUAL FRAMEWORK

KEY FINDINGS

- The legal status of subsidiaries and branches of financial firms is different.
- The perimeter of financial firms and trading venues to be affected by the future EU-UK relationship in the field of financial services is wide.
- The UK government, the Bank of England (BoE) and other administrative financial authorities are fully embedded in the international institutional framework governing the financial system. This is important for the future EU-UK relationship in financial services, even if the UK were to become a 'third-country' under WTO rules.

1.1. The four modes of supplying services at international level

According to a widely used categorisation in trade negotiations, there are four modes of supplying services between countries:

- **Mode 1 ('cross-border supply')** refers to the supply of a service from the territory of one WTO Member to another;
- **Mode 2 ('consumption abroad')** occurs when a service consumer of one WTO Member consumes a service while in the territory of another;
- **Mode 3 ('commercial presence' or 'establishment')**, involves a service supplier of one WTO Member doing business in another WTO Member through commercial presence in the latter; and
- **Mode 4 ('presence of natural persons')** occurs when a service supplier from one WTO Member sends individuals to another WTO Member to supply services to consumers in that territory.

However, this **terminology is not uniform**. In a number of EU Preferential Trade Agreements, the term 'cross-border supply' is used to cover both of Modes 1 and 2.

Importantly, the category of Mode 3 services trade covers forms of economic activity which are also commonly understood as **foreign investment**, leading to an **overlap between rules on trade in services and rule relating to the treatment of foreign investors**¹.

Within the European Single Market – being more than an area with trade agreements – activities across Member States are based on the exercise of the four Treaty freedoms and covered by the relevant directives, regulations (the *aquis*), etc. In the field of financial services² 'commercial presence' may take two forms³:

- The first form is the establishment in the 'host' country of a **subsidiary** which is a **separate legal entity** owned or controlled by a parent company (established in the 'home' country). A subsidiary needs to get a license from the competent authorities

¹ See on this Zacharias, p. 48-53, analysing Article I, paragraph 2, of the General Agreement on Trade in Services (GATS) of the World Trade Organisation, and Lang, Conyers, p. 12.

² The term '**financial services**' is used in this section as a generic term covering all types of financial services, as laid down in the First Annex of the General Agreement on Trade in Services (see paragraph 5, point (a) GATS); see Von Bogdandy, Windsor, p. 632.

³ Mode 2 and 4, i.e. the 'consumption abroad' and the '(temporary) presence of natural persons' are of lesser importance to this study.

of the host country in order to be able to operate, and is considered as a 'national' of that country⁴.

- The second form is the opening of **branches**. Branches do **not have a legal personality**; they are defined as a *place* of business (other than the head office) which are a part of the financial firm and provide financial services for which the financial firm has been authorised.

1.2. The impact on financial firms and services before and after the UK's exit

1.2.1. Foreign subsidiaries of financial firms within the EU

The status quo: UK financial firms⁵ with an establishment in other EU Member States in the form of a subsidiary are treated there as nationals of the Member State in which they have been granted authorisation by the competent (supervisory) authorities and where the subsidiary must have its registered *and* head office ('home Member State')⁶. This implies that they are subject to the regulatory and supervisory framework of that Member State, while the UK competent authorities can only impose additional requirements for the purpose of *consolidation* (e.g. consolidated financial statements, consolidated micro-prudential supervision). These subsidiaries can provide cross-border services in other Member States, can establish branches in other Member States ('host Member States'), and can participate in the payments and market infrastructures without any further restrictions. *Mutatis mutandis*, the above applies equally to **EU financial firms** established in the UK in the form of a subsidiary.

The situation after the UK's exit: This situation for **UK financial firms** established through **subsidiaries** in EU Member States will basically not change after the UK's exit from the EU (with the exception of the rules on consolidation in accordance with the provisions of various sources of EU financial services law⁷). Accordingly, any UK financial firm having established a subsidiary in an EU Member State will continue to be treated as a company of the Member State in which the subsidiary is established and incorporated. Through this subsidiary it will continue to be able to establish branches in host Member States, to provide services and to participate in the payments and market infrastructures – all of this under the EU rules governing the right of establishment and the freedom to provide services. In this respect, it should be (strongly) expected that several UK financial firms which currently either do not have a subsidiary in other EU Member States or are only present through branches or by virtue of the freedom to provide services cross-border under their 'EU single passport', will decide (depending on the progress and the direction of the discussions on the model for the future EU-UK relationship in financial services, and duly taking into account the high costs involved and the overall impact on their business model⁸) resort to a 'subsidiary strategy' as the preferred one for their new positioning in the EU financial market⁹. Any **EU financial firm** established in the UK in the form of a

⁴ See the Barcelona Traction Case of the International Court of Justice (ICJ Reports 1970, 4, Belgium vs. Spain). For details see Stein – von Buttlar; and Herdegen, pp. 59-60.

⁵ The term '**financial firm**' is used in this section as a generic term covering all types of institutions providing financial services. In section 1.2 it is further specified with reference to the types of financial firms authorised under EU financial services law.

⁶ For instance, the requirement imposed on credit institutions to have their head office in the same Member State as their registered office is laid down in Article 13(2) Directive 2013/36/EU 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 [...] (CRD IV), OJ L 176, 27.6.2013, pp. 338-436.

⁷ See indicatively section 3.2.1.

⁸ On the implications for the UK's financial businesses (on the basis of five case studies) see Reynolds, pp. 31-36.

⁹ See section 2.2.2.

subsidiary will continue to be treated as a UK company and will continue to have the right to provide services in the UK and participate in the established UK payment systems and the market infrastructures.

1.2.2. Branches of foreign financial firms and the freedom to provide services

The status quo: A key principle of EU law which will not be applicable to the UK after its exit is the '*principle of mutual recognition*'. This principle was introduced by the European Court of Justice's (ECJ) jurisprudence and was gradually used, already since the late 1980s, in several of the legal acts which constitute the sources of EU financial services law, and played a catalytic role in the establishment and deepening of the internal market in financial services¹⁰.

According to its application to licensing by competent supervisory authorities laid down in the relevant legal framework for most categories of EU regulated financial firms¹¹, such financial firms may open branches in other EU Member States or provide services cross-border on the basis of authorisations granted by their *home* Member State's competent (supervisory) authorities (the 'single passport'). Apart from some administrative arrangements between the competent authorities of the home and the host Member States' competent authorities, and without prejudice to the limited host Member States' powers, no additional requirements may be imposed on the branches or the cross-border provision of services of EU financial firms by the host Member States' competent authorities. This applies, however, to the extent that the services to be provided directly or through a branch in the host country are covered by the (extensive) list of services which, under the relevant sources of EU financial services law, are subject to mutual recognition¹².

So the principle of mutual recognition also applies to the provision of financial services in the 'modes' of supplying services presented above¹³ by EU financial firms, making use of their single passport in host Member States under similar conditions to those governing the right of establishment through branches¹⁴. Nevertheless, the application of the principle of mutual recognition is broader when it comes to the branches of several types of EU financial firms established in other Member States. In accordance with the provisions of several EU legal acts, it applies also to the **prudential supervision** of such branches, their reorganisation, resolution and winding up, as well as to their participation in deposit guarantee, resolution and investor compensation schemes, where appropriate. All these aspects fall under the remit of the competent (supervisory, resolution, other administrative or judicial, depending on each aspect) authorities of the *home* Member State and its established schemes.

The situation after the UK's exit from the EU: The **branches of UK financial firms in EU Member States** and **cross-border services provision** will no longer benefit from the EU framework governing the freedom to operate in an EU Member State through branches or cross-border under authorisation granted by the UK competent authorities. Their position, including prudential supervision etc., will depend on the future EU-UK relationship in the field of financial services and/or domestic rules in the relevant Member State. *Mutatis mutandis*, the same will apply to **branches of EU financial firms in the UK**.

¹⁰ On this principle see Sousi-Roubi, pp. 126-127; and Vigneron, Smith.

¹¹ See section 1.2.

¹² As regards e.g. credit institutions see Articles 17 and 33 CRD IV. See also section 2.2.2.

¹³ See section 1.1.

¹⁴ Article 33 CRD IV.

1.3. Financial service providers affected by the future EU-UK relationship

EU financial law¹⁵ contains detailed provisions for the authorisation, the operating conditions, the micro-prudential supervision, the prudential regulation (in principle at micro-level and in some cases also at macro-level) and (partially) the reorganisation and the resolution of several types of financial firms incorporated in EU Member States. In certain cases, it also establishes requirements in relation to the provision of financial services by branches of 'third-country'¹⁶ financial firms. The types of financial firms are usually divided according to the activities of banking, securities (trading and markets) and insurance (and re-insurance)¹⁷.

1.3.1. The UK position within the international financial architecture

Certain inter-governmental fora, along with several international fora and a limited number of international organisations constitute the international institutional framework governing the financial system (international/financial architecture) and are the main actors in the process of making the rules of public international financial standards. The making of the rules of public international financial standards into (national) law takes place in different stages: political decision-making, writing the standards of international financial (services), implementation on national level, and – to the extent possible - 'indirect enforcement' of the international financial (services) standards¹⁸.

1.3.2. The current position of the UK and the Bank of England (BoE)

The UK, the Bank of England (**BoE**) and other UK administrative authorities are part of the international institutional framework. In particular, the UK is a member of the **G20** which sets the global political agenda with regard to policy objectives. At the Finance Ministers and Central Bank Governors level, the UK is represented by its Finance Minister and the BoE's Governor, whereas at the level of the Heads of State or Government by its Prime Minister.

The UK is also a member of all international organisations which are part of this international institutional framework, notably the International Monetary Fund (**IMF**) which is involved in the process of (indirect) 'enforcement' of the international financial standards¹⁹, the World Trade Organization (**WTO**) which is the main international institution dealing with issues pertaining to global trade in financial services under the rules of the General Agreement on Trade in Services (**GATS**)²⁰, and the Organisation for Economic Cooperation and Development (**OECD**) which elaborates international standards with regard to the corporate governance of companies listed in regulated markets, provides the aegis for international cooperation in the fields of consumer protection and financial literacy and hosts one of the international fora governing the financial system (the Financial Action Task Force).

¹⁵ The term '**EU financial law**' is defined for the purpose of this study as the set of provisions of secondary EU law aimed at the achievement of the EU's negative financial integration, i.e. the creation of a single financial area in the single market, whereas positive financial integration relates to the achievement at EU level of specific financial policy objectives.

¹⁶ The term '**third-country financial firm**' is defined for the purpose of this study as a financial firm which is headquartered in a country which is not an EU Member State.

¹⁷ The **Annex** of this study contains a short (to the extent possible) **definition of the main categories of financial firms and of the categories of trading venues** regulated under EU financial services law. On the definition of these firms and trading venues see further details in Jung, Bischof, pp. 63-78.

¹⁸ See on this Giovanoli, and Gortsos (2012), pp. 131-132.

¹⁹ See on this Giovanoli, and Gortsos (2012), pp. 150-157.

²⁰ See in detail in section 2.1.2.

The BoE is as well a member of the Bank for International Settlements (**BIS**). In fulfilling its statutory tasks²¹, i.e. the promotion of cooperation between its member central banks, the BIS hosted nine committees and groups, which are part of the 'Basel Process'²². The UK is represented (mainly but not exclusively) by the BoE in all of them.

The UK is also represented in the Financial Stability Board (**FSB**) by the BoE, the Financial Conduct Authority (**FCA**), and the Treasury. The statutory objective of this international forum consists in coordinating the work of national financial authorities and international standard-setting bodies (hereinafter the '**international financial fora**') and adopting international financial standards, in order to develop and promote the implementation of effective regulatory, supervisory and other financial system policies²³.

Finally, the UK Government, the BoE and other UK administrative authorities are members of many other international financial fora²⁴. The majority of these fora, all of which have *not* been established by virtue of international treaties, are referred to as 'standard-setting bodies', or 'standard setters', because their main objective consists in the adoption of international financial standards²⁵:

- The BoE and the Prudential Regulation Authority (**PRA**, which is a BoE subsidiary) are members of the **Basel Committee on Banking Supervision**, active in the subject-areas of micro- and macro-prudential banking regulation and micro-prudential banking supervision.
- The FCA is a member of the **International Organisation of Securities Commissions (IOSCO)**, which is active in the subject-areas of micro- and macro-prudential regulation and micro-prudential supervision of investment firms.
- The PRA and the FCA are members of the **International Association of Insurance Supervisors (IAIS)**, which is active in the subject-area of micro- and macro-prudential regulation and micro-prudential supervision of insurance and re-insurance undertakings, and of the **Joint Forum**, which deals with issues common to the banking, securities and insurance sectors, including the prudential regulation of financial conglomerates.
- The BoE is a member of the **Committee on Payments and Markets Infrastructures (CPMI)**, which is active in the subject-area of payment and settlement systems' oversight²⁶.
- In the **Financial Action Task Force on Money Laundering (FATF)**, which is active in the subject-area of combating money laundering and terrorist financing, the UK is represented by its Government.

²¹ Article 3 BIS Statutes (2005), as further specified in Articles 19-25; see Nobel, pp. 183-188.

²² The '**Basel Process**' refers to the role of the BIS in hosting and supporting the work of the international secretariats engaged in standard-setting and the pursuit of financial stability; http://www.bis.org/about/basel_process.htm.

²³ Article 1 FSB Charter (2012). For further details on the FSB see Giovanoli, pp. 19-25, Nobel, pp. 173-183; Gortsos (2012), pp. 143-150, and Thiele, pp. 541-545.

²⁴ On these fora see Giovanoli, pp. 20-29; Nobel, pp. 189-226; Gortsos (2012), pp. 160-195; Thiele, pp. 552-554; Wandel, pp. 30-44; and Lastra, pp. 501-507.

²⁵ On this term, see Giovanoli, p. 8; and Norton, p. 14.

²⁶ The BoE is also a member of three other international financial Committees, which are not standard-setting bodies: the **Committee on the Global Financial System** which is the only international forum that is not a standard-setter, but still very important in terms of research, the **Markets Committee**, which deals with structural developments that can have an impact on short-term market dynamics, and the **Irving Fisher Committee on Central Bank Statistics**, active in the issue-area of statistical issues in central banks.

- The Financial Services Compensation Scheme is a member of the **International Association of Deposit Insurers (IADI)**, which deals with issues pertaining to the operation of deposit guarantee and investor compensation schemes.
- Finally, the UK participates in the **Global Partnership on Financial Inclusion (GPFI)**²⁷ which is an inclusive platform for G-20 Member States, carrying forward its work on financial inclusion matters, including the implementation of the '*G-20 Action Plan on financial inclusion*'.

1.3.3. An assessment

The following conclusions can be drawn:

- Firstly, The UK's participation in the WTO allows it in principal to resort to the rules of the GATS as one of potential models with regard to the future EU-UK relationship in financial services. This aspect is discussed in detail in **Chapter 2**.
- The participation of the UK, the BoE and other UK administrative authorities in the international organisations and financial fora is a guarantee that the UK financial system and UK financial law will continue both to influence and be influenced and shaped by international regulatory developments with regard to safeguarding financial stability and attaining other policy objectives concerning financial regulation, supervision and oversight²⁸.

This may prove a safe haven for the shaping of the future EU-UK relationship in financial services, to the extent that the financial system and the financial law of the EU Member States are also influenced by these international regulatory developments, either as a result of their participation in the above-mentioned international organisations and financial fora or through the transposition of the international soft law elaborated by these international fora into EU law. In this sense, the convergence of a significant part of the main aspects of the substantive rules governing financial regulation, supervision and oversight through the impact of (public) international financial law will facilitate a high level of approximation of the regimes to be developed in the UK and in the EU, even if the right of establishment and the freedom to provide services between them were to be 'distorted', depending on the concept with regard to the future EU-UK relationship in financial services which will finally prevail. At the same time, it will provide the UK legislators with a higher degree of flexibility as to the concrete implementation of these rules, since they will not be bound by EU Directives and *a fortiori* EU Regulations which transpose the international rules into EU law.

²⁷ See <http://www.gpfi.org/>.

²⁸ See on this also Moloney, p. 76, arguing that the UK's ability to influence and impose its preferences on these international standards will be severely diminished.

Table 1: UK membership in international standard-setting bodies

| Forum | Objective | UK membership |
|--|---|--|
| Financial Stability Board (FSB) | Overall coordination Resolution of financial firms | BoE, FCA and Treasury |
| Basel Committee on Banking Supervision (BCBS) | Banking regulation and supervision | PRA |
| International Organisation of Securities Commissions (IOSCO) | Capital markets' regulation and supervision | FCA |
| International Association of Insurance Supervisors (IAIS) | Insurance sector regulation and supervision | PRA and FCA |
| Joint Forum | Regulation and supervision of financial conglomerates | PRA and FCA |
| Committee on Payments and Market Infrastructures (CPMI) | Oversight of payments and market infrastructures | BoE |
| Financial Action Task Force on Money Laundering (FATF) | Combating money laundering and terrorist financing | Government |
| International Association of Deposit Insurers (IADI) | Operation of deposit guarantee systems | Financial Services Compensation Scheme |
| International Federation of Accountants (IFAC) | International auditing standards | Several Associations and Institutes |

2. FUTURE EU-UK RELATIONSHIP CONCEPTS AND THEIR IMPACT ON FINANCIAL FIRMS

KEY FINDINGS

- The three potential concepts under examination lead in general to different conclusions with regard to the future EU-UK relationship in financial services:
- If the UK were to become a member of the European Economic Area (**EEA**), the current situation would not be significantly affected; under the other two options (**WTO** or **bilateral trade agreements**), the UK would have a third-country status.
- If the UK were to have a third-country status, the 'passporting rights' of the of UK financial firms operating cross-border or via branches in the EU and of EU financial firms operating in the UK would cease to operate. In contrast, in such a case, the position of their subsidiaries would not be affected.

Situation before the UK exits from the EU: The UK will continue to be a Member State of the EU, subject to EU legislation and relevant commitments, throughout the time period ending with the completion of the procedure laid down in **Article 50** of the Treaty on European Union (**TEU**). Thus, the EU regulatory framework provides for a favourable regime for the establishment and prudential supervision of branches of financial firms established in an EU Member State. More specifically, based on the principle of the EU passport, a financial firm having its head office in a Member State may establish a branch and/or provide cross-border banking services in another Member State of the EU, provided that the supervisory authority of the country of origin deems that the conditions laid down in EU law are fulfilled. Consequently, the establishment of a branch in or the cross-border provision into another Member State does not necessitate an authorisation by the supervisory authority of the host Member State.

Under this framework, one issue has to be kept in mind with regard to secondary EU law in the form of regulations. **Regulations**, pursuant to **Article 288** of the Treaty on the Functioning of the European Union (**TFEU**), have general application and are **directly applicable** in all Member States. Given that regulations do not require an act of transposition into national law, their application in the jurisdiction of the UK will automatically cease upon the completion of the procedure for the UK's exit from the EU, unless the UK government adopts their content as UK law by means of a bill, or the UK were to become a member of the EEA, and the EEA-relevant regulations are incorporated into the EEA Agreement²⁹. The same may apply for implementing and delegated acts. In any event, given that several provisions of UK law refer to Regulations or copy provisions that have been laid down in Regulations, it is clear that a solution must be found that will safeguard continuity and legal certainty in the UK legal order³⁰.

For the time being, the UK has not indicated that it would like to deviate from the (currently) applicable legislative framework governing financial services after it has left the EU which makes sense as this reflects in essence international practices adopted by the international financial fora which the UK has helped to shape³¹. In this respect, on 24 June

²⁹ See Council Regulation (EC) No 2894/94 concerning arrangements for implementing the EEA Agreement.

³⁰ See Taylor Wessing.

³¹ See also Brown, Waitzman, pp. 2-4.

2016, the FCA stated that UK financial firms must continue to abide by EU law until the completion of the UK's exit from the EU and the adoption of UK law of a different content³². Throughout this period, the transposition of (applicable) EU law into UK law will continue as normal. On the basis of this announcement, the conclusion may be drawn that at least for the coming years and up until the withdrawal of the UK from the EU becomes effective, the regulatory framework governing the provision of financial services in the UK will remain in line with the EU regulatory framework³³.

The main options: The future relationship including possibly the UK's access to the EU single market will be determined by the concept that will be negotiated in the agreement of the UK's exit from the EU and/or in subsequent agreements. In the event of failure to reach an agreement and complete the exit procedure by the expiry of the deadline starting when the UK makes a notification under **Article 50 TEU** (or after an extended deadline), the UK would have the status of a third country, fully lacking access to the EU single market. In any event, the alternative options for the UK's status vis-à-vis the EU could take for instance the following three forms which are explored in more detail:

- **third-country status** under the provisions of the GATS of the WTO;
- special status through a **bilateral agreement** with the EU; and
- membership of the **EEA**³⁴.

The rationale underlying the choice of this sequence is that the main elements of the GATS are crucial for the analysis of bilateral agreements. However, the first option is the one with the fewest ties and may be regarded as an 'option of last resort'.

2.1. Third country regime: application of the General Agreement on Trade in Services (GATS)

The **GATS** was the first multilateral framework of rules and principles by which the members of the World Trade Organisation (**WTO**)³⁵ undertook **general obligations** and **specific commitments** with regard to the liberalisation of international trade in services³⁶. However, negotiations on financial services were not completed when the Uruguay Round came to a close, even though the specific provisions which govern trade in financial services were finalised at that time with the signing of the (First) '**Annex on Financial Services**', and the 'Understanding on Commitments in Financial Services (hereinafter the '**GATS Understanding**')³⁷. Their outcome is included in the '**Fifth Protocol to the General Agreement on Trade in Services**'³⁸ which came into force on 1 March 1999³⁹.

³² Financial Conduct Authority (2016): Statement on European Union referendum result; <https://www.fca.org.uk/news/statements/statement-european-union-referendum-result>.

³³ See Taylor Wessing.

³⁴ With a specific note on the membership of the EFTA without membership of the EEA (the case of Switzerland).

³⁵ The Treaty establishing the WTO was signed in Marrakesh (Morocco) on 15 April 1994 and its provisions came into force on 1 January 1995. It replaced the General Agreement on Tariffs and Trade (GATT) of 1948.

³⁶ On the GATS see indicatively Van den Bossche, the various contributions in Wolfrum, Stoll and Feinäugle (ed.), Lowenfeld, pp. 117-128, and Lang, Conyers.

³⁷ See von Bogdandy, Windsor, pp. 618-639 and 647-666.

³⁸ Bogdandy, Windsor, pp. 643-646.

³⁹ The present study does not cover the multilateral Trade in Services Agreement (TiSA), which is still being negotiated among 23 WTO Members (counting the EU as one) since March 2013 in order to further liberalise trade in services; <http://ec.europa.eu/trade/policy/in-focus/tisa>.

2.1.1. Scope of application: main provisions of GATS on financial services

The GATS applies to all *'measures by [its] Members affecting trade in services'*⁴⁰. This phrase covers measures relating to the purchase, payment or use of services, access to and use of services in order to make them available to the broader public, and the (temporary) presence of natural persons from a Member country for the provision of services in the territory of another Member country. The term **'trade in services'** is defined to mean the supply of a service in any of the four modes laid down in **Article I(2) GATS**⁴¹.

The GATS provisions do *not* apply to services supplied in the exercise of governmental authority⁴². In the context of financial services, the latter means activities conducted by a central bank or monetary authority or by any other public entity in pursuit of monetary or exchange rate policies and specific other activities⁴³. The Annex on Financial Services contains a **'carve-out clause'** for *'measures for prudential reasons'*, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. Nevertheless, non-conforming prudential measures may not be used as a means of avoiding the WTO Member's commitments or obligations under the GATS⁴⁴.

2.1.2. The general obligation

The GATS contains a **'most favoured nation' (MFN) general obligation** according to which each WTO Member must extend immediately and unconditionally to services and service suppliers of any other WTO Member treatment no less favourable than that it accords to like services and service suppliers of any other country⁴⁵. This is subject to the three cases of 'permanent exemptions' provided for in the GATS⁴⁶ and the WTO Members' right to maintain measures inconsistent with the general obligation, provided that they are listed in, and meet the conditions of, the **Annex on Article II Exemptions**⁴⁷.

2.1.3. The specific commitments

The *'specific commitments'* undertaken by the WTO Members are laid down in Schedules⁴⁸ and form an integral part of the GATS. They include market access, **national treatment** and additional commitments and apply in sectors in which they are undertaken and to all modes of service supply. As the UK is currently covered by the EU's Schedules, it is likely that the EU and the UK would have to (re-)negotiate their Schedules when the UK leaves the EU.

Under the specific commitment on **market access** and according to the provisions of the GATS, each WTO member must accord services and service suppliers of any other WTO Member treatment no less favourable than that provided for under the terms, limitations and conditions agreed and specified in its Schedule. If a WTO Member undertakes a market-access commitment in relation to the supply of a service through the cross-border

⁴⁰ GATS, Article I(1).

⁴¹ Article XXVIII, point (c) GATS. The term **'measure'** is defined in point (a) of that Article and the term **'measures by Members'** in Article I(3), point (a).

⁴² Article I(3), point (b) GATS.

⁴³ GATS Annex on Financial Services, paragraph 1, points (b) and (c).

⁴⁴ GATS Annex on Financial Services, paragraph 2, point (a).

⁴⁵ Article II(1) GATS.

⁴⁶ Articles II(3), V and VII GATS.

⁴⁷ Article II(2) GATS.

⁴⁸ Article XX GATS. Schedules; https://www.wto.org/english/tratop_e/serv_e/serv_commitments_e.htm.

mode of supply, and if the cross-border movement of capital is an essential part of the service itself, that member is thereby committed to allow such movement of capital⁴⁹.

Making such a commitment in financial services (as in any services sector) does not entail an obligation to remove all restrictions on market access. It only requires the removal of specific measures, such as limitations on the number of service suppliers, on the total value of service transactions or assets, on the total number of service operations or on the total quantity of service output, measures which restrict or require specific types of legal entity or joint venture through which a service supplier may supply a service, or limitations on the participation of foreign capital in terms of maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment⁵⁰.

But under the GATS, the **national treatment** obligation ensures that in the sectors inscribed in its Schedule, and subject to any conditions and qualifications set out therein, each WTO Member must accord to services and service suppliers of any other WTO Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers⁵¹. This requirement may be met by a WTO Member by according to services and service suppliers of any other WTO Member, either 'formally identical treatment' or 'formally different treatment' to that it accords to its own like services and service suppliers⁵².

2.2. Bilateral trade agreements

An option for the UK within the framework of negotiations could be the establishment of bilateral trade agreements, which could also cover financial services, containing obligations and commitments which go beyond those of the GATS⁵³. Contrary to the UK, the EU has significant experience with such trade agreements, developed within an established legal and institutional framework based on the strategic direction of EU trade policy, initially by providing leadership in multilateral trade negotiations (2000-2006) and then by negotiating 'preferential trade agreements' (**PTAs**) as a complement to the multilateral track from the *Global Europe* strategy in 2006, which identified liberalisation of trade in services as central to the next generation of European trade agreements⁵⁴.

The financial services sector has emerged as a key priority for these trade negotiations, which include the EU-**Chile** Association Agreement (includes principles relating to services liberalisation similar to GATS), the EU-**Korea** agreement which contains a 'new template' for financial services rules, the EU-**Singapore** FTA, as well as the EU-**Central America**, EU-**Colombia/Peru** and EU-**CARIFORUM** agreements⁵⁵. Of particular importance is also the Comprehensive Economic and Trade Agreement (**CETA**) with Canada of 30 October 2016⁵⁶ which covers virtually all sectors and aspects of Canada-EU trade in order to eliminate or reduce relevant barriers⁵⁷.

⁴⁹ Article XVI(1) GATS.

⁵⁰ Article XVI(2) GATS. The GATS Understanding contains specific provisions on market access in financial services relating to the cross-border mode of supply, the commercial presence mode of supply and the temporary presence of natural persons for business in the financial services sector (Section B, paragraphs 3-4, 5-6, and 9, respectively).

⁵¹ Article XVII(1) GATS.

⁵² Article XVII(2)-(3) GATS. Section C GATS Understanding contains also specific provisions in that respect.

⁵³ The study does not cover the **Customs Union** (e.g. between the EU and Turkey). Customs unions are not a useful alternative, since they usually only provide for free movement of goods and not free trade in services.

⁵⁴ Lang, Conyers, pp. 9-10, with further references.

⁵⁵ For further details on these Agreements see <http://ec.europa.eu/trade/policy/countries-and-regions>.

⁵⁶ See <http://ec.europa.eu/trade/policy/in-focus/ceta>.

⁵⁷ On all these agreements see Lang, Conyers, pp. 10-11, with further references.

2.2.1. Commitments pertaining to the financial system

Commitments on the services supplied in the three sectors of the financial system (*i.e.* banking, capital markets and insurance) typically include market access and national treatment (non-discrimination) with regard to all modes of their supply. Their main purposes are the freezing of existing levels of market access, ensuring enhanced rights of establishment, the automatic liberalisation of new financial services and the liberalisation of cross-border data flows. Some agreements also contain 'standstill' clauses, which at a minimum bind the *status quo*. These apply in respect of market access and/or national treatment, usually by limiting the conditions, limitations and qualifications which parties may inscribe in their schedules. Finally, in support to the liberalisation commitments, most agreements contain requirements on both parties to ensure freedom of payments on the current account, as well as freedom of capital movements directly relating to the transactions liberalised.

The provisions governing the **right of establishment** (commercial presence) and the **removal of related discriminatory measures** may include limitations:

- of financial firms' right to determine the juridical form of a business presence, by imposing on foreign firms to have their registered office in the host country, or to be incorporated therein in order to provide certain financial services, mainly in the fields of retail banking, internet banking and asset management;
- on the ownership rights of foreign investors in domestic firms (over a certain threshold) or on the participation of foreign investors in banks under privatisation; and
- on the permissible proportion of senior managers who may not have permanent residence within the EU.

Finally, commitments on cross-border supply **usually cover only a small number of sub-sectors of financial services**, such as insurance (and reinsurance) of risks relating to maritime shipping, space launching and freight (including satellites), as well as international trade, services auxiliary to insurance (such as consultancy, actuarial, risk assessment and claim settlement services), and provision and transfer of financial information and financial data processing. In the banking sector they are confined to auxiliary services⁵⁸.

2.2.2. Prudential 'carve-outs'

A final element which is common to all bilateral agreements are the provisions containing standard form carve-outs, governing the prudential regulation and supervision of financial firms entering the host country under the terms of the liberalisation regime. Such provisions, usually based on those of GATS, include:

- the application (to financial services) of general investment protection provisions akin to those found in bilateral investment treaties;
- an explicit 'right to regulate';
- guidance notes on the interpretation of the prudential carve-out (CETA);
- protection for services supplied in the exercise of governmental authority;
- inclusion of comprehensive advance notice and comment obligations for proposed financial regulation;

⁵⁸ See Lang, Conyers (2014), pp. 16-17.

- a necessity test for prudential regulation; and
- encouraging the implementation and application of specified international standards for financial regulation⁵⁹.

2.3. Membership of the European Economic Area (EEA)

The third concept examined for the future UK-EU relationship in financial services is membership in the EEA and to join the three members of the European Free Trade Agreement (EFTA), namely Iceland, Liechtenstein and Norway, in accordance with the **EEA Agreement** of 1994⁶⁰. By this Agreement, these three countries have access to the EU single market and enjoy the four fundamental freedoms (the free movement of goods, persons, services and capital) which they have to grant reciprocally to EU Member States⁶¹.

New EU Member States must, and the Swiss Confederation *or* new EFTA members may, apply to become a party to the EEA Agreement by submitting an application to the EEA Council⁶². The terms and conditions for such participation are subject to an agreement between the Contracting Parties and the applicant state, which must be submitted for ratification or approval by all Contracting Parties in accordance with their own procedures. Thus, opting for this model would require approval of the UK's application to become an EFTA member (including approval from Switzerland) and an EEA member by the other 27 EU Member States, as well as by Iceland, Liechtenstein and Norway.

2.3.1. Right of establishment

In accordance with the EEA Agreement, the four freedoms apply, i.e. there are no restrictions on the freedom of establishment of nationals of an EU Member State or an EEA State in the territory of any other, including the setting up of agencies, branches or subsidiaries by nationals of any of these States established in their territory. In order to facilitate the taking up and pursuit of activities as self-employed persons, the Contracting Parties must take the necessary measures, as contained in Annex VII, concerning the mutual recognition of diplomas, certificates and other evidence of formal qualifications, and the coordination of the legal, regulatory or administrative provisions therein concerning the taking up and pursuit of activities by such persons⁶³. Specific provisions on the right of establishment are laid down in **Annexes VIII-XI**⁶⁴; **Annex IX** of the EEA Agreement applies to financial services.

2.3.2. Provision of services

There are also no restrictions on the freedom to provide services⁶⁵ within the territory of the Contracting Parties⁶⁶. Specific provisions on the freedom to provide services are laid down in **Annexes IX-XI** EEA Agreement⁶⁷.

⁵⁹ Lang, Conyers, pp. 17-19.

⁶⁰ OJ L 1, 3.1.1994, pp. 3-522.

⁶¹ Cooperation in fields outside these freedoms is governed by **Articles 78-88** EEA Agreement. However, agriculture and fishery is not part of the EEA Agreement. And for instance Norway is not part of the Customs union.

⁶² Article 128 EEA Agreement. The EEA Council, which is governed by Articles 89-91 EEA Agreement, consists of the members of the EU Council, members of the EU Commission, and of one member of the Government of each of the EFTA States (Article 90(1), first sentence EEA Agreement).

⁶³ Article 35 with reference to Article 30 EEA Agreement.

⁶⁴ Article 31(2) EEA Agreement.

⁶⁵ The term '**services**' is defined as meaning, *inter alia*, activities of a commercial character such as *financial services* (Article 37, second sub-paragraph EEA Agreement).

⁶⁶ Article 37, first sub-paragraph EEA Agreement.

2.3.3. Membership of the EFTA but not of the EEA – the case of Switzerland

Switzerland is not a member of the EEA, but is a member of the EFTA⁶⁸. Its cooperation with the EU is limited to specific sectors under more than 100 bilateral agreements⁶⁹. In any case, with some exceptions for life assurance activities, Switzerland's bilateral agreements with the EU **do not cover financial services**⁷⁰. Thus, Swiss financial firms currently do *not* have 'passporting rights' enabling them to provide services in the single market on the basis of the license they have obtained from the Swiss financial supervisory authority (FINMA). Notwithstanding that, however, Switzerland is keeping track with developments in EU financial, and in particular EU capital markets law⁷¹. Opting for such a solution, if it ultimately were to become an option for the UK, implies a cumbersome and time-consuming negotiating process.

2.4. The impact on financial firms under the alternative concepts

The exit of the UK from the EU will definitively have implications for the financial system, the services provided and financial firms established both in the UK and in other EU Member States. The EU budget will also be affected, irrespective of the future EU-UK relationship, more importantly so if the concept to be adopted is not EEA membership (the latter would further entail the continuation of the UK's contribution to the EU budget under the principle of proportionality⁷²).

An aspect of primary importance is the continuation or discontinuation of UK financial firms' right to have access, through branches and cross-border provision of services in the EU single market by virtue of the single passport under the different concepts which will govern the future EU-UK relationship. The same applies also to EU financial firms as to their activities in the UK financial marketplace.

2.4.1. Application of the GATS

The position of UK financial firms in the EU: If the UK were not to become a member of the EEA or to conclude any bilateral agreement for its participation in specific areas of the EU single market, it will have no access to the latter. Given that the UK is already a member of the WTO, applicable in this case would be the provisions of the GATS. The UK would be subject to the general obligation of the MFN clause and would have to negotiate a new Schedule on specific commitments⁷³.

EU Directives which have already been transposed into UK law would continue to apply, unless this national legislation would be repealed or amended (a very unlikely development in the case of legal acts reflecting international financial standards⁷⁴). **EU Regulations** would cease to apply from the date of the UK's withdrawal from the EU. This is of particular importance to the extent that a significant part of EU financial law now consists of Regulations and the UK will have to legislate *de novo* on the subject-areas⁷⁵. New EU

⁶⁷ Article 36 and 39 EEA Agreement, respectively. This freedom is also governed by **Articles 30 and 32-34** EEA Agreement.

⁶⁸ See on this; <http://www.efta.int/about-efta/european-free-trade-association>. Switzerland is also not part of the EU customs union.

⁶⁹ See on this Lehmann, Zetzsche, p. 3.

⁷⁰ See on this University of Kent Centre for Swiss Politics; and Kaddous, Matthey (ed.).

⁷¹ On this aspect see the various contributions in Bovet (ed.).

⁷² See on this the provisions laid down in Article 5(4) TEU, as well those of Protocol (No. 2) 'on the Application of the Principles of Subsidiarity and Proportionality' attached to the European Treaties.

⁷³ On this see details in Lang.

⁷⁴ See Lang; and section 3.2.3.

⁷⁵ Moloney, p. 81, highlights the threat of a 'regulatory vacuum' if the UK would decide not to replace EU Regulations by national legislation.

directives, regulations, delegated and implementing acts, etc., would not be binding upon the UK either.

The impact on subsidiaries

The procedure for establishing a subsidiary of a financial firm would be based on the licensing conditions laid down in EU law (as implemented in the national legal order). Accordingly⁷⁶, the UK's exit from the EU would not affect the legal status of subsidiaries. However, the financial group's *set-up of operations* - for instance if the London head office provides certain EU-wide services - could necessitate major changes. The application of a '**subsidiarisation strategy**' would allow the group to make use, via the establishment of a EU subsidiary, of the single passport to establish branches and provide services without (permanent) establishment in other Member States⁷⁷.

The impact on branches

The EU right of establishment of branches (and all other related aspects)⁷⁸ would cease to apply. The operation of UK financial firms through branches would be governed by the EU's GATS Schedule on specific commitments in financial services⁷⁹, the provisions of EU financial law on third-country financial firms/branches, and national GATS Schedules and laws.

Taking the case of **credit institutions** as an example, if the UK would have third country status only, the establishment of branches of UK credit institutions in a Member State would be subject to the provisions of **Article 47 CRD IV** which prohibits Member States to apply to branches of third country credit institutions a more favourable treatment than that accorded to branches of EU credit institutions. The EU may also conclude agreements with third countries providing for the application of provisions which accord to third country originating branches identical treatment throughout the EU⁸⁰. The establishment and operation of branches of third-country credit institutions is authorised by the competent authorities of the (host) Member State under the provisions of its domestic law.

Similar provisions would apply in the future to the branches of UK **investment firms** in a Member State by virtue of Article 34-35 **Directive 2014/65/EU (MiFID II)**⁸¹. The MiFID II governs several aspects pertaining to the provision of investment services and the performance of investment activities in Member States (such as trading in securities and derivatives, carrying out customer orders, portfolio custody and management) and also provides credit institutions and investment firms with the right to do business across the EU through branches. MiFID also provides for access of investment firms to regulated markets by setting up branches or becoming remote members or having remote access to a regulated market, as well as for the access to central counterparties⁸² and to clearing and

⁷⁶ See above section 1.1.2.

⁷⁷ See by way of mere indication, Moloney, p. 79, and Proctor, pp. 3-4. On the consolidated micro-prudential supervision of these subsidiaries see section 3.2.1.

⁷⁸ See section 1.1.2.

⁷⁹ For these Schedules see https://www.wto.org/english/tratop_e/serv_e/serv_commitments_e.htm.

⁸⁰ Articles 47(1) and 47(3) CRD IV. See also recital (23) according to which the rules governing branches of credit institutions having their head office in a third country should be analogous in all Member States.

⁸¹ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (...), OJ L 173, 12.6.2014, pp. 349-496. On this Directive see the various contributions in Busch, Ferrarini (eds.). The MiFID II will most probably begin to be applied before the completion of negotiations with the EU, given that the date for the entry into force of its provisions is 1 January 2018.

⁸² Central counterparties are governed by Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on over-the-counter (OTC) derivatives, central counterparties and trade repositories, OJ L 201, 27.7.2012, pp. 1-59, '**EMIR**'.

settlement systems (for the purpose of finalising or arranging the finalisation of transactions in financial instruments) and the right to designate a settlement system⁸³.

In relation to third-country investment firms, the MiFID II, unlike the CRD IV, establishes two different regimes. In particular:

- In principle, a credit institution or an investment firm having its head office in a third country may, at the discretion of national legislation in each Member State, be required to establish a branch in a Member State if it intends to provide investment services and/or perform investment activities in that Member State to retail or professional clients (as defined in Section II of Annex II) upon fulfilment of specific conditions⁸⁴.
- Nevertheless, if a retail or professional client established or situated in the EU initiates at its own exclusive initiative the provision of an investment service or the performance of an investment activity by a third-country firm, the above-mentioned requirement for authorisation by branching does not apply to the provision of that service or the performance of that activity by the third-country firm to that person⁸⁵.

In addition, in accordance with the provisions of **Regulation (EU) No 600/2014 (MiFIR)**⁸⁶, third-country investment firms may provide investment services and/or perform investment activities to eligible counterparties and to professional clients throughout the EU without the establishment of a branch, if they are registered in the 'register of third-country firms' kept by the European Securities and Markets Authority (**ESMA**)⁸⁷ by way of an 'equivalence check'⁸⁸.

A direct impact on rights and obligations of **alternative investment fund managers** and **UCITS managers** should also be expected if the UK is to have third-country status. Their ability to market and provide management services for investment capital (including investment advice, portfolio management and custody and management of assets) would potentially be limited with regard to access to private and professional customers in Member States and might necessitate further licensing or the establishment of specific provisions⁸⁹.

Finally, the right to provide financial services without (permanent) establishment in host Member States by UK financial firms (under the EU single passport) would also not be granted because the provision of financial services would be subject to the relevant provisions of the EU GATS Schedule on specific commitments in financial services, since EU financial law is silent on this. Nevertheless, it should be noted that demand for cross-border financial services is not so important in certain areas of financial activity, such as retail

⁸³ Articles 36-38 MiFID II.

⁸⁴ Article 39(1)-(2) MiFID II. See also recitals (109) and (111).

⁸⁵ Article 42, first sentence, MiFID.

⁸⁶ Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (...), OJ L 173, 12.6.2014, pp. 84-148.

⁸⁷ On the ESMA, see also below in section 3.2.1 and in section 4.1.1.

⁸⁸ Articles 46(1) and 47(1) MiFIR. The ESMA keeps a register of the third-country firms allowed to provide investment services or perform investment activities in the EU in accordance with Article 46 and 48 MiFIR. See on this Ferran, p. 10. On the 'equivalence model' concerning access to the EU single market in general by third-country financial firms see Ferran, pp. 8-9, Moloney, pp. 78-79, and Reynolds, pp. 20-26 and 39-88 (Annexes A-C).

⁸⁹ The framework governing alternative investment fund managers is laid down in Articles 34-42 of Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers (...), OJ L 174, 1.7.2011, pp. 1-73; and that pertaining to UCITS managers in Article 9 (with further reference to MiFID II) of Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), OJ L 302, 17.11.2009, pp. 32-96. On this aspect see Ferran, pp. 15-17.

banking services. According to the European Commission, *'The current level of direct cross-border transactions in retail financial services is limited, with consumers largely purchasing these products in their domestic market and firms overwhelmingly serving markets in which they are physically established. Recent studies suggest that the share of consumers who have already purchased banking products from another Member State was less than 3% for credit cards, current accounts and mortgages. In consumer credit only 5% of loans had been obtained cross-border. Cross-border loans within the euro area account for less than 1% of the total household loans in the area.'*⁹⁰. The same holds true for insurance and re-insurance services, albeit not for wholesale banking services and certain wholesale investment services.

The position of EU financial firms in the UK: The position of EU financial firms in the UK would also be affected. The passporting provisions will not apply to EU financial firms having (or intending to establish) branches and providing (or intending to provide) services without permanent establishment in the UK. These aspects would be governed by the UK GATS Schedule on specific commitments in financial services and national UK law. On the other hand, the establishment of subsidiaries of EU financial firms in the UK would be governed by the provisions of the relevant UK law and those of the UK GATS Schedule on specific commitments in financial services. Depending on the set-up of operations, financial services firms in the EU will have to adapt their model of providing services.

2.4.2. Bilateral agreements

The conclusion of bilateral agreements would not provide for participation in the EU single market as a whole either. Depending on the content of the agreement, the treatment of UK financial firms in the EU could be more favourable than in the case of the application of the GATS. In this context it is reminded that according to EU financial law the EU may conclude agreements with third countries providing for the application of provisions which accord to branches of credit institutions or investment firms having their head office in a third country identical treatment throughout the territory of the EU. It is to be expected that these provisions would be taken into account when drafting an EU-UK bilateral agreement.

Mutatis mutandis, the same considerations would apply to EU financial firms in the UK, if an EU-UK bilateral agreement were to be concluded.

2.4.3. EEA Membership

The position of UK financial firms in the EU: Opting for this concept (also called the 'Norwegian model') would ensure that the basic EU freedoms and hence the principle of mutual recognition would be granted. The EU Regulations on *EU financial law* would continue to apply, while EU financial law Directives are either already incorporated into UK law (unless they were to be repealed or amended), while new ones would apply to the UK as long as they are of relevance for the EEA. However, with the right of these freedoms comes the obligation to contribute (partially) to the EU budget, be bound to EU (financial services) legislation, and accept EFTA Court jurisdiction and the free movement of persons.

If the UK could establish a seamless transition from EU Membership to EEA Membership, under the EEA concept, the UK's exit from the EU would not affect either the operation of UK financial firms' branches in other Member States or the provision by these firms of services without (permanent) establishment in other Member States⁹¹. The establishment

⁹⁰ See European Commission (2015) 'Green Paper on retail financial services: better products, more choice, and greater opportunities for consumers and businesses'; <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2015:630:FIN>.

⁹¹ See e.g. Articles 33-46 CRD IV for credit institutions, and Articles 34-38 MiFID II, for investment firms.

of subsidiaries of UK financial firms in the UK would be governed by the provisions of the UK legal acts transposing the relevant sources of EU financial law into the UK legal order⁹².

The position of EU financial firms in the UK: The position of EU financial firms in the UK would also not be affected. The passporting provisions will apply to EU financial firms having (or intending to establish) branches and providing (or intending to provide) services without (permanent) establishment in the UK.

Table 2: Matrix of possible Brexit options – soft or hard Brexit

| Have / can do | EU Member | non-EU EEA Members ⁹³ | Non EEA EFTA Member ⁹⁴ | Customs Union ⁹⁵ | FTA ⁹⁶ | WTO Rules |
|----------------------------|-----------|----------------------------------|---------------------------------------|-----------------------------|-------------------|-----------|
| Single Market Access | Yes | Yes (with exceptions) | Partial | No | No | No |
| Market Access for Services | Yes | Yes | Partial | No | Partial | No |
| Duty Free Trade in Goods | Yes | Yes | Yes | Yes | Yes | No |
| Free Movement of People | Yes | Yes | Yes ⁹⁷ | No | No | No |
| Implementation of EU Rules | Yes | Yes | No (but similar rules ⁹⁸) | No | No | No |
| EU Budget Contributions | Yes | Yes (reduced) | Yes (reduced) | No | No | No |
| ECJ Jurisdiction | Yes | No (but EFTA Court) | No (but EFTA Court) | No | No | No |
| Trade Agreements | No | Yes | Yes | No | Yes | Yes |

Source: Doris Kolassa, Rudolf Maier, ECON Secretariat.

⁹² See e.g. CRD IV, Articles 8-16 for credit institutions and MiFID II, Articles 5-10 and 14-20 for investment firms (and partially also for credit institutions providing investment services and/or performing investment activities).

⁹³ According to Article 126 [Agreement on the EEA](#), the EEA Agreement only applies to the territories of the EU, in addition to **Iceland, Liechtenstein and Norway**. Under the present wording of the EEA Agreement, only a member of either the EU or EFTA can be a party to the EEA Agreement. The EEA was established by the EEA Agreement which entered into force in 1994. Its objective is to **extend the Internal Market of the EU** to the *three* participating EFTA States.

⁹⁴ Currently the only EFTA Member which is not in the EEA is Switzerland.

⁹⁵ As currently for Turkey.

⁹⁶ Like with Canada.

⁹⁷ The EEA Agreement is based on economic freedoms. Therefore, it is independent from the issues covered in the provisions of the [Schengen Acquis](#). However, all of the four EFTA States participate in Schengen through **bilateral agreements** and they all apply the provisions of the relevant *acquis*. Since 2001, the EFTA Convention has been updated on a continuous basis in order to align its content with the Swiss-EU bilateral agreements and the EEA Agreement. This includes, for example, provisions on the free movement of persons between all of the EFTA States.

⁹⁸ Switzerland's economic and trade relations with the EU are mainly governed through a series of bilateral agreements where Switzerland has agreed to take on certain aspects of EU legislation in exchange for accessing the EU's single market, see <http://ec.europa.eu/trade/policy/countries-and-regions/countries/switzerland/>.

3. REGULATORY ASPECTS FOR BANKS AND IMPACT ON PAYMENT SYSTEMS AND MARKET INFRASTRUCTURES IN THE WTO SCENARIO

KEY FINDINGS

- Under a ‘**third-country** status’ scenario for the UK, the framework governing the micro-prudential supervision of the EU branches of UK credit institutions and the UK branches of EU financial firms, their reorganisation, resolution and winding-up, as well as their participation in deposit guarantee schemes would be affected significantly.
- For the subsidiaries of these financial firms the implications would be less significant to the extent that the principle of mutual recognition does not apply to them.
- Under the same scenario, the impact on the large-value payment system ‘TARGET2’, the SEPA, and the financial infrastructures for clearing and reporting transactions would be less significant.

This Chapter focuses on the WTO third country model only. Almost to the same extent as their ‘passporting rights’, the framework governing the micro-prudential supervision of the EU branches of UK banks and the UK branches of EU banks, their reorganisation, resolution and winding-up, as well as the participation of credit institutions’ branches in deposit guarantee schemes and the participation of credit institutions’ branches in investor compensation schemes will also be affected. To a much lesser extent, implications will also be evident for the subsidiaries of these financial firms. Another important aspect to be explored is the impact on payment systems and market infrastructures, including the EU large-value payment system ‘TARGET2’, the ‘Single Euro Payments Area’, and the financial infrastructures for clearing and reporting transactions.

3.1. The impact on the regulatory framework governing credit institutions

3.1.1. Micro-prudential supervision of branches of foreign credit institutions

Under the CRD IV, EU credit institutions are being supervised on a solo basis by the competent authorities of their home Member State⁹⁹ or by the European Central Bank (**ECB**) if they are considered to be significant and their head office is located in a Member State whose currency is the euro within the context of the (European) Banking Union¹⁰⁰. This micro-prudential supervision also covers (with some exceptions) their branches which are established in other Member States, by application of the principle of mutual recognition¹⁰¹.

If the UK became a third-country, this regime would be altered. The conduct of micro-prudential supervision of UK credit institutions would hence continue to be the responsibility

⁹⁹ Articles 49-110 CRD IV.

¹⁰⁰ Article 4(1), point (b) Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, OJ L 287, 29.10.2013, pp. 63-89. On the Banking Union see section 4.1.1.

¹⁰¹ Article 49(1) CRD IV. The powers of the competent authorities of the host Member State are laid down in Articles 40-46 CRD IV.

of the UK PRA in accordance with the provisions of UK law (which currently, and unless amended, is based on the CRD IV)¹⁰². Nevertheless, the branches of these credit institutions in the EU would then have to be (authorised and) supervised by the competent authorities of the host Member State. The branches of EU credit institutions in the UK would become subject to micro-prudential supervision by the UK PRA in accordance with UK law.

Consolidated micro-prudential supervision

EU credit institutions are also subject to micro-prudential supervision on a consolidated basis (including at least all their banking subsidiaries) in principle by the competent authorities of the Member State where the parent company's head office is situated,¹⁰³ or by the ECB, respectively. If the UK were to become a third country, **Article 127 CRD IV** would be applicable to consolidated supervision. This would mean that if a credit institution, the parent undertaking of which is a credit institution, (an investment firm, a financial holding company or a mixed financial holding company) with its head office in a third country, is not subject to consolidated supervision under **Article 111**, the competent authorities must assess whether this credit institution is subject to consolidated supervision by a third-country supervisory authority which is 'equivalent' to that governed by the principles set out in the CRD IV and the relevant requirements of **Regulation (EU) No 575/2013 (CRR)**¹⁰⁴. In the absence of such equivalent supervision, Member States must apply the CRD IV and the CRR to the credit institution *mutatis mutandis* or allow their competent authorities to apply other appropriate supervisory techniques which achieve the objectives of credit institutions' consolidated supervision¹⁰⁵.

According to **Article 48 CRD IV**, the Commission may submit proposals to the Council for the negotiation of agreements with a third country regarding the means of exercising supervision on a consolidated basis over credit institutions the parent undertakings of which have their head offices in a third country and credit institutions situated in third countries the parent undertakings of which have their head offices in the EU, in order to ensure that specific conditions laid down in the Directive are met¹⁰⁶.

3.1.2. Reorganisation and winding-up

Credit institutions' reorganisation measures and winding-up proceedings in the EU are governed by **Directive 2001/24/EC**¹⁰⁷ (**CIWUD**, as amended by **Directive 2014/59/EU BRRD**¹⁰⁸). CIWUD is the only act of EU financial law which does not provide for a minimum harmonisation of national rules and introduced the principle of mutual recognition, whereby the administrative or judicial authorities of the home Member State responsible for reorganisation and/or winding-up are solely competent to decide on the application of such

¹⁰² Member States and the European Banking Authority (EBA), in accordance with Article 33 EBA Regulation (EU) No 1093/2010, may conclude cooperation agreements, providing for the exchange of information with the supervisory authorities of third countries in accordance with Articles 56 and 57(1) CRD IV for the purpose of performing the supervisory tasks of those authorities or bodies (Article 55, first sub-paragraph CRD IV).

¹⁰³ Articles 111-126 CRD IV.

¹⁰⁴ Regulation (EU) 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms (...), OJ L 176, 27.6.2013, pp. 3-339. The provisions of this legal act apply equally to credit institutions and to investment firms.

¹⁰⁵ Articles 127(1) and 127(3) CRD IV. See on this Ferran (2016), pp. 7-8.

¹⁰⁶ Article 48(1)-(2) CRD IV. See also recital (24) CRD IV pursuant to which an agreement must be reached between the EU and third countries with regard to the practical exercise of consolidated supervision over the largest possible geographical area.

¹⁰⁷ Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding-up of credit institutions, OJ L 125, 5.5.2001, pp. 15-23.

¹⁰⁸ Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms (...), OJ L 173, 12.6.2014, pp. 190-348.

measures and the initiation of such proceedings concerning a credit institution, including its branches in other Member States¹⁰⁹.

If the UK were to be granted third-country status, this regime would be altered in the following way:

- On the one hand, the application of reorganisation measures and the opening of winding-up proceedings with regard to UK credit institutions would continue to be the responsibility of the national competent administrative or judicial authorities (in accordance then with the provisions of UK law). The branches of these credit institutions established in Member States, nevertheless, would be reorganised and wound-up by the competent administrative or judicial authorities of the host Member State¹¹⁰.
- On the other hand, the branches of EU credit institutions established in the UK would be subject to the reorganisation measures applied and the winding-up proceedings initiated in accordance with the provisions of relevant UK law by the UK competent administrative or judicial authorities.

3.1.3. Resolution

The BRRD provides the EU regulatory framework governing the recovery and resolution of credit institutions (and investment firms)¹¹¹. It is interesting to note that in the amended **Article 2 of CIWUD** the term 'reorganisation measures' is defined (point 7) to contain the application of resolution tools and the exercise of resolution powers under the BRRD, meaning that the principle of mutual recognition with regard to branches of credit institutions from other Member States applies to those as well.

The UK's exit from the EU in the form of a third-country status raises several issues. The first issue is whether this will lead to a substantial modification of the UK's legislation (BRRD implementation). The BRRD follows and introduces into the EU legal order the international FSB standard '*Key Attributes of Effective Resolution Regimes for Financial Institution*'¹¹². This standard sets out the main axes for the efficient resolution of a bank in an organised manner, without taxpayers incurring the costs of an insolvent bank's losses and concurrently ensuring that key banking services continue to be provided. This standard was approved in November 2011 by the heads of state at the G20 Cannes summit. The UK is a member of both, the G20 and the FSB, and was one of the states that significantly contributed to both, the elaboration of this framework and its approval at international political level. Furthermore, the UK was one of the first EU Member States that adopted a special regulatory framework for the resolution of credit institutions before any such efforts officially started at European level¹¹³. Particularly with regard to one BRRD element, i.e. raising the minimum requirement for own funds and eligible liabilities (**MREL**)¹¹⁴, the Bank of England (BoE) announced on 8 November 2016 that the relevant rules will be implemented fully by 2022¹¹⁵.

In addition, the BRRD's provisions on third countries, which refer to the conclusion of agreements with third countries, the recognition and enforcement of third-country

¹⁰⁹ Articles 3-7 and 9-18 CIWUD 2001/24/EC, respectively.

¹¹⁰ Applicable in this case would be **Articles 8 and 19 CIWUD**, respectively, see Wessels, pp. 63-65 and 80-81.

¹¹¹ The Single Resolution Mechanism (SRM) only applies to credit institutions covered by the Banking Union, i.e. relevant banks in the euro area (and participating Member States).

¹¹² FSB, '*Key Attributes of Effective Resolution Regimes for Financial Institutions*'. See also recitals (67) and (101) BRRD.

¹¹³ See Brierley.

¹¹⁴ Article 45 BRRD. See Maragopoulos.

¹¹⁵ See Bank of England.

resolution proceedings, the right to refuse recognition or enforcement of third-country resolution proceedings, the cooperation with third-country authorities and the exchange of confidential information will be applicable¹¹⁶. The BRRD also provides that the resolution of a branch of a third-country credit institution operating in a Member State may be carried out, under specific conditions, by the Member State's resolution authorities¹¹⁷.

3.1.4. Participation in deposit guarantee schemes

The rules and procedures relating to the establishment and the functioning of deposit guarantee schemes (DGSs) are laid down in **Directive 2014/49/EU**¹¹⁸ (DGSD). Membership of EU credit institutions in the DGS(s) operating in their home Member State constitutes a *sine qua non* condition for their right to be authorised and to accept deposits from the public¹¹⁹. According to the principle of mutual recognition, deposits which EU credit institutions accept through their branches established in host Member States, are covered by the DGS operating in their home Member State¹²⁰.

For the UK as third-country, this regime would be altered: UK credit institutions would continue to be members of the UK deposit guarantee scheme. The guarantee of deposits at UK banks' branches established in EU Member States would continue to be governed by **Article 15** DGSD which requires Member States to check whether the branches established in their territory by third-country credit institutions have protection 'equivalent' to that prescribed in the DGSD, and at least that depositors benefit from the same coverage level and scope of protection as provided for in the DGSD¹²¹. Accordingly, if (UK) protection would not be considered to be equivalent, these branches would be obliged to join a DGS(s) within the territory of the Member State. Member States must respect the above-mentioned provision of **Article 47(1) CRD IV**¹²² according to which Member States are not permitted to apply to branches of non-EU credit institutions provisions which result in more favourable treatment than that accorded to branches of EU credit institutions¹²³.

The branches of EU credit institutions in the UK would be required to participate in the UK deposit guarantee scheme in accordance with the provisions of UK law on the treatment of foreign branches.

3.2. Impact on payment systems and market infrastructures

3.2.1. The EU large-value payment system 'TARGET2'

As regards large-value payment systems, in the case that the UK would become a third country, the operation of the banking system of the EU Member States might be affected with regard to the clearing and settlement of transactions taking place through the Trans-European Automated Real-time Gross settlement Express Transfer system (**TARGET2**)¹²⁴.

¹¹⁶ Articles 93-95 and 97-98 BRRD.

¹¹⁷ Articles 96 BRRD.

¹¹⁸ Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes (recast), OJ L 173, 12.6.2014, pp. 149-178. See details in Gortsos (2014).

¹¹⁹ Article 4(3) DGSD.

¹²⁰ Article 14(1) DGSD.

¹²¹ Article 15(1), first and third sub-paragraphs DGSD.

¹²² See section 2.2.2.

¹²³ Article 15(1), second sub-paragraph DGSD.

¹²⁴ Additional information on the structure and operation of TARGET2: <http://www.ecb.europa.eu/paym/t2/html/index.en.html>. For a detailed overview of that system see Geva, pp. 113-123, and Kokkola pp. 243-259.

The main component of this payment system is owned and operated by the Eurosystem. TARGET2 has expanded the benefits offered by national real-time gross settlement systems beyond national borders and, at the same time, enabled participants to be credited or debited on a continuous basis, in central bank money with immediate finality of the transaction. TARGET2 functions on the basis of a single shared IT platform interlinking, on the one hand and on a mandatory basis, the ECB and the central banks of the 19 Member States which have adopted the euro, and, on the other hand, on an optional basis, the central banks of one Member State, Denmark, which has opted out of the single currency (as the UK did, too) and four Member States which (still) have a derogation¹²⁵. The payment services that may be used by system members are credit transfers, direct debits and transfers namely the sending (or movement) of funds or securities, or of rights relating to funds or securities, from one party to another party.

Given that, TARGET2 services are provided into Member States which (national central banks) are not participating in TARGET2 (including the UK) and, in view of the total daily average value of processed euro-denominated payments (amounting to trillions¹²⁶), the impact for credit institutions from Member States operating in the UK may be significant as far as the services provided by them are concerned if and to the extent that they participate as users in the above payments system.

3.2.2. The Single Euro Payments Area (SEPA)

With regard to retail payment systems, one of the key initiatives at European level is the establishment as of 1 August 2014 of the SEPA. Its geographical scope covers 34 countries (i.e., the EU Member States, Norway, Lichtenstein, Iceland, Switzerland, the Principality of Monaco and the Republic of San Marino).

The establishment of the SEPA enables the conduct of payment transactions in euro between payment accounts kept with payment service providers established in SEPA countries, in the same manner as payment transactions carried out at national level. Its characteristic is that the payment users (natural persons and legal entities) may use payment accounts to carry out payment transactions in all 34 SEPA's members¹²⁷.

Given that the geographical scope of the SEPA is (as mentioned above) broader than that of the EU single market and that SEPA is, to a large extent, a product of market self-regulation, **no significant impact** on the banking system of the (other remaining) Member States should be expected from the UK's exit from the EU¹²⁸.

3.2.3. Financial infrastructures for clearing and reporting transactions

Financial infrastructures for clearing and reporting transactions (such as trade repositories¹²⁹ and central counterparties¹³⁰) have been created to facilitate the implementation of decisions and obligations undertaken at international level. In the event

¹²⁵ As of February 2016, 25 central banks participating in, or connected to, TARGET2: The 19 euro area central banks plus the ECB, and five central banks from non-euro area countries: Bulgaria, Croatia, Denmark, Poland and Romania, see <https://www.ecb.europa.eu/paym/t2/about/countries/html/index.en.html>.

¹²⁶ Decision 2014/533/EU of the European Central Bank of 13 August 2014 on the identification of TARGET2 as a systemically important payment system pursuant to Regulation (EU) No 795/2014 on oversight requirements for systemically important payment systems (ECB/2014/35), OJ L 245, 20.8.2014 pp. 5-8, Annex, point (b)(i). In 2015, the daily average value of TARGET2 amounted to EUR 1 835 trillion.

¹²⁷ For the SEPA structure see http://ec.europa.eu/finance/payments/sepa/index_en.htm.

¹²⁸ According to a presentation by Payments UK, the competent collective representation of 44 payment service providers in the UK: *'The outcome of the EU referendum has no immediate effect on retail payments or payments policy and regulation. It remains "business as usual"'*.

¹²⁹ On trade repositories see also section 3.2.1.

¹³⁰ On central counterparties see also section 2.2.2.

that the UK would be subject to third-country status, the users of such infrastructures established in the UK would lose their regulated status and hence the EU passport, unless they would continue to operate as eligible trading or clearing organisations, having ensured the recognition of their operational status as equivalent to that of the EU¹³¹.

It is reasonably expected that the provisions governing the operation of these financial infrastructures would continue to apply and are likely to become UK law. Nevertheless, it is possible that credit institutions, trading venues and clearing houses established in EU Member States **would not be allowed to conduct transactions with UK infrastructure organisations** until the latter were deemed to be equivalent, which would likely require (time consuming) further adjustments. In addition, in the case of limited access to the EU single market by UK credit institutions, UK trading venues and UK clearing organisations being users of European infrastructures, it is likely that the volume of data and information processed by EU Member States' supervisory authorities would be considerably reduced.

Table 3: The impact of alternative concepts for the future EU-UK relationship regarding UK financial firms

| Concept | Single passport | Other impact |
|-------------------------|-----------------|--|
| Application of the GATS | - | Lack of access to the EU single market Restricted movement of services The micro-prudential supervision, reorganisation and winding-up, as well as the resolution of branches of UK credit institutions in the Member States, and their participation in deposit guarantee schemes would be governed by the provisions of EU law applying to third-country credit institutions |
| Bilateral agreements | - | Limited access to the EU single market (under specific conditions and in specific sectors, including those on financial services, upon the agreement) Potentially similar results as in the case of application of the GATS with regard to the regulatory aspects applying to UK credit institutions |
| EEA membership | ✓ | Access to the EU single market Application of EU legislation |

¹³¹ See on this Ferran, pp. 14-15.

4. THE IMPACT ON THE MONETARY AND FINANCIAL EU INSTITUTIONAL FRAMEWORK

KEY FINDINGS

- Irrespective of the future EU-UK relationship, the functioning of the European System of Central Banks (ESCB) and the European Central Bank (ECB) will not be substantially affected by the UK's exit from the EU. The only exceptions are the ECB's capital and the decision-making process in its General Council.
- The operation of the European System of Financial Supervision (ESFS) will, in principle, also not be affected, with some exceptions as well.
- Arrangements will also have to be made with regard to the UK's share in the European Investment Bank's (EIB) subscribed capital and its paid-up capital.
- There will be no impact on the two main pillars of the Banking Union (i.e., the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM)).
- It is likely that the European Banking Authority (EBA), currently located in London, will be moved to another Member State.

4.1. European System of Central Banks (ESCB) – European Central Bank (ECB)

The EU institutional framework governing the monetary system in the context of the EU Monetary Union, the first and only genuinely Europeanised element of the EU Economic and Monetary Union (EMU) is governed by the TFEU¹³², the Statute of the European System of Central Banks (ESCB) and the ECB ('Statute')¹³³, and several legal acts of the ECB. The specific position of the UK and the BoE within the EMU is governed by Protocol (No 15) attached to the EU Treaties '*on certain provisions relating to the United Kingdom (...)*'¹³⁴ which established the UK's right to opt out of the third stage of EMU¹³⁵.

The **non-euro area national central banks**, including the BoE, are **members of the ESCB** along with those of Member States whose currency is the euro¹³⁶. However, due to the fact that Member States outside the euro area are not bound by the policies carried out by the ESCB, the position of their central banks within the ESCB is significantly different to that of the central banks of Member States whose currency is the euro. The ultimate indication of this differentiation is that the fundamental provision of **Article 14.3 Statute**, stipulating that '*the national central banks are an integral part of the ESCB and shall act in accordance with the guidelines and instructions of the ECB*', does not apply to these national central banks.

The functioning of the ESCB and the ECB will, in principle, not be affected by the UK's exit from the EU. Nevertheless, there are two aspects on which there will be an impact: the capital of the ECB and the decision-making process in its General Council.

¹³² Articles 127-144, 219 and 282-284 TFEU.

¹³³ Protocol (No 4) attached to the EU Treaties on the Statute of the European System of Central Banks and of the European Central Bank, OJ C 202, 7.7.2016, pp. 230-250.

¹³⁴ OJ C 202, 7.7.2016, pp. 284-286.

¹³⁵ Protocol (No 15), paragraphs 1 and 2, respectively. On the position of the UK and the BoE within the EMU see Smits, pp. 138-139, and Louis, pp. 81-83.

¹³⁶ Article 282(1), first sentence TFEU, and Article 1, first subparagraph, first sentence Statute.

4.1.1. Impact on the ECB capital

Taking into account the *sui generis* position of the non-euro area national central banks (including the BoE) within the ESCB, the TFEU and the Statute established a series of derogations for the entire duration of the derogation and/or the opt out status¹³⁷. *Inter alia*, not applicable are certain Statute's Articles relating to the financial provisions of the ESCB, namely those on the annual accounts of the ECB, the auditing of the accounts of national central banks, the allocation of monetary income of national central banks and the allocation of net profits and losses of the ECB¹³⁸. By contrast, the provisions of the Statute on subscription to the ECB's capital are applicable to the non-euro area national central banks, which may also be called upon to pay up a minimal percentage of their subscription to the capital of the ECB.

4.1.2. The ECB's capital and capital subscription

In order to ensure the ECB's financial independence, it was decided that the ECB should have its own capital, with resources coming exclusively from the national central banks-members of the ESCB. The initial capital of the ECB, the amount of which was set to EUR 5 billion¹³⁹ was operational upon its establishment, on 1 June 1998 and all national central banks-members of the ESCB subscribed to it, as the sole subscribers to and holders of the capital¹⁴⁰. In December 2010, due to the emergency circumstances arising from the need to prop up the European banking system following the recent (2007-2009) international financial crisis and the respective fiscal crisis in several Member States, the ECB proceeded to a first increase (duplication) of its capital, which as from 1 January 2014 amounts to **EUR 10,825,007,069.61**¹⁴¹.

The subscription to the ECB's capital is established in accordance with the key referred to in **Article 29 Statute**¹⁴². The weighting assigned to each national central bank based on this capital key is equal to the sum of 50 % of the respective Member State's share in the population of the EU in the penultimate year preceding the establishment of the ESCB (*i.e.* 1996) and 50% of the share of the respective Member State in the gross domestic product of the EU at market prices, as recorded in the last five years preceding the penultimate year before the establishment of the ESCB¹⁴³. The weightings assigned to each national central bank are being adjusted every five years, by analogy with the provisions of the initial weighting¹⁴⁴. On the basis of the above and taking into account the (most recent) capital key weightings laid down in ECB Decision of 29 August 2013 (**ECB/2013/28**)¹⁴⁵, the **share of the BoE** in the ECB's subscribed capital as from 1 January 2014 amounts to **EUR 1,480,243,941.72** (with a weighting of 13.6743 %).

4.1.3. Payment of the subscribed capital by non-euro area national central banks

The Statute provides that the non-euro area national central banks have in principle no obligation to pay up their subscribed capital by way of derogation from **Article 28.3**

¹³⁷ The provisions of primary monetary law which do not apply to central banks of non-euro area Member States are listed in Article 139(2) TFEU and in Article 42 Statute.

¹³⁸ Articles 26.2, 27 and 32-33 Statute, respectively.

¹³⁹ Article 28.1, first sentence Statute.

¹⁴⁰ Article 28.2, first sentence Statute.

¹⁴¹ Decision of the Governing Council of the ECB of 13 December 2010 (ECB/2010/26), adopted on the basis of Article 28.1, second sentence of the Statute and Council Regulation (EC) 1009/2000 (OJ L 115, 16.5.2000, p. 1).

¹⁴² Article 28.2, second sentence Statute.

¹⁴³ Article 29.1, first subparagraph (and Article 47, first sentence) Statute.

¹⁴⁴ Article 29.3, first sentence Statute.

¹⁴⁵ OJ L 16, 21.1.2014, pp. 53-54.

Statute¹⁴⁶. The General Council of the ECB may, nevertheless, impose on them the obligation to pay up a 'minimal' percentage of their subscription to the ECB's capital '*as a contribution to the operational costs of the ECB*'¹⁴⁷. According to the most recent **ECB Decision** of the General Council of 30 August 2013 (**ECB/2013/31**)¹⁴⁸ on this score, each non-euro area national central bank must pay up 3.75 % of its share in the ECB's subscribed capital with effect from 1 January 2014. Hence, from 1 January 2014 the paid-up capital of the BoE amounts to **EUR 55,509,147.81**¹⁴⁹.

4.1.4. Arrangements in view of the UK's exit from the EU

When the UK leaves the EU, and irrespective of the future EU-UK relationship, the BoE will cease to be a member of the ESCB. Accordingly, arrangements will have to be made with regard to its share in the ECB's subscribed capital and its paid-up capital. Under the Statute, the shares of national central banks in the subscribed capital of the ECB may in principle not be transferred (pledged or attached)¹⁵⁰. It is only when there is an adjustment of the weightings assigned to national central banks in the key for capital subscription that these may transfer among themselves capital shares to the extent necessary to ensure that the distribution of capital shares corresponds to the adjusted key, under the terms and conditions determined by the Governing Council¹⁵¹.

Thus, in view of the fact that the BoE will cease to be a member of the ESCB and taking into account the fact that there are no provisions on reducing the ECB's capital, the **Governing Council will have to take a Decision assigning new weightings to the other national central banks in the key for subscription to the ECB's capital**, to the effect that the BoE's capital shares will be transferred to the latter. Otherwise, an amendment to the Statute is required, providing for a decrease in the ECB's capital¹⁵².

It is not clear whether the BoE will have a **right to retrieve** its already paid-up capital worth EUR 55.5 million. In the absence of any relevant provision in the Statute and unless there is an amendment thereof to resolve the issue by introducing a general clause (which the author hardly believes will be the case), it is strongly expected that **the resolution of this issue will be part of the political agreement to be reached between the EU and the UK**.

4.1.5. Impact on decision-making within the General Council of the ECB

As a non-euro area national central bank, the BoE only participates in the ECB's third decision-making body, the General Council¹⁵³. The operation of this body is governed by **Article 45 Statute** and (mainly) by the **ECB Decision** of 17 June 2004 (ECB/2004/12) '*adopting the Rules of Procedure of the General Council of the ECB*'¹⁵⁴. For the adoption of a Decision by the General Council imposing on non-euro area national central banks to pay

¹⁴⁶ Article 47, second sentence Statute.

¹⁴⁷ Such a Decision of the General Council is also binding on the BoE by virtue of Article 8, point (c) of Protocol (No 15).

¹⁴⁸ OJ L 16, 21.1.2014, pp. 63-64.

¹⁴⁹ Article 32 of the Statute on the allocation of monetary income to the national central banks does not apply to the BoE (nor to any other non-euro area central bank).

¹⁵⁰ Article 28.4 Statute.

¹⁵¹ Article 28.5 Statute. See e.g. the most recent ECB Decision of the Governing Council of 29 August 2013 (ECB/2013/29), OJ L 16, 21.1.2014, pp. 55-60.

¹⁵² Articles 28-29 Statute do not belong to those that (due to the technical nature of their content) can be amended in accordance with the 'simplified amendment procedure' laid down in Article 129(3) TFEU and in Article 40.1 of the Statute.

¹⁵³ Article 141(1) TFEU, and Article 44.1-44.2 Statute.

¹⁵⁴ OJ L 230, 30.6.2004, pp. 61-63.

up a minimal percentage of their share in the subscribed ECB's capital as a contribution to the operational costs of the ECB¹⁵⁵; **Article 47 Statute** (exceptionally¹⁵⁶) requires a qualified majority of at least 2/3 of the subscribed capital (and half of the shareholders).

Since the weighting assigned to the BoE in the key for subscription to the ECB's capital is considerably high (13.6743 %) and taking into account the readjustment of the weightings assigned to the other national central banks which will take place after the UK's exit from the EU, irrespective of the future EU-UK relationship, **the ability to reach a qualified majority might be affected**. Of minor importance is the fact that the quorum of two-thirds of members required for voting in the General Council¹⁵⁷ will have, after the UK's exit from the EU, to be met by a number of members reduced by one.

4.2. The European System of Financial Supervision

The European System of Financial Supervision (**ESFS**), which entered into operation on 1 January 2011 and consists of two elements, the three European Supervisory Authorities (**ESAs**) and the European Systemic Risk Board (**ESRB**), and is relevant to *all* EU Member States¹⁵⁸. The ESAs were established by Regulations of the European Parliament and of the Council of 24 November 2010:

- the European Banking Authority (**EBA**) by Regulation (EU) No 1093/2010;¹⁵⁹
- the European Insurance and Occupational Pensions Authority (**EIOPA**) by Regulation (EU) No 1094/2010;¹⁶⁰ and
- the European Securities and Markets Authority (**ESMA**) by Regulation (EU) No 1095/2010¹⁶¹.

In principle, the ESAs are regulatory authorities with some specifically designated and explicitly stipulated supervisory powers¹⁶².

The ESRB was established under Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board¹⁶³. As regards the operation of the ESRB, specific tasks have been conferred on the ECB under Council Regulation (EU) No 1096/2010 of 17 November 2010¹⁶⁴. Each Member State also designated an authority entrusted with the conduct of macro-prudential policy in national legislation, as set out in Recommendation B, paragraph 1 of the Recommendation of the European Systemic Risk Board of 22 December 2011 on the macroprudential mandate of national authorities (**ESRB/2011/3**)¹⁶⁵.

The operation of the ESFS will also not be affected. The three ESAs and the ESRB will continue to operate with the participation of the remaining Member States. However, an impact, to variable degree, will become evident on the composition of the ESRB's governing

¹⁵⁵ See section 4.2.1.

¹⁵⁶ See Decision ECB/2004/12, Article 4(2).

¹⁵⁷ Article 4(1), first sentence Decision ECB/2004/12.

¹⁵⁸ On the ESFS, see Louis; Tridimas, pp. 801-803; Wymeersch; Thiele, pp. 494-519.

¹⁵⁹ OJ L 331, 15.12.2010, pp. 12-47.

¹⁶⁰ OJ L 331, 15.12.2010, pp. 48-83.

¹⁶¹ OJ L 331, 15.12.2010, pp. 84-119.

¹⁶² For the only genuine supervisory powers of the ESMA see section 3.2.1.

¹⁶³ OJ L 331, 15.12.2010, pp. 1-11.

¹⁶⁴ OJ L 331, 15.12.2010, pp. 162-164. On both Regulations, which lay down the EU framework on macro-prudential (financial) oversight, see Ferran, Alexander, as well as Papathanassiou, Zarouras, with extensive further references.

¹⁶⁵ OJ C 41, 14.2.2012, pp. 1-4.

bodies, on the seat of the EBA (which is currently located in London), on the composition of the ESAs' governing bodies (the only impact which will depend on the model to be adopted for the future EU-UK relationship), and on the budget of the ESAs.

4.2.1. Impact on the European Systemic Risk Board (ESRB)

In accordance with **Regulation (EU) No 1092/2010**, the ESRB is governed by a General Board and has also a Steering Committee, a Secretariat, an Advisory Scientific Committee¹⁶⁶ and an Advisory Technical Committee¹⁶⁷. The **General Board** consists of the following members with voting rights: the President and the Vice-President of the ECB, the Governors of the central banks-members of the ESCB, a member of the Commission, the Chairpersons of the three ESAs and the Chairperson of the Advisory Technical Committee. Furthermore, a high-level representative of the national supervisory authority of each Member State and the President of the EU's Economic and Financial Committee are members without voting rights¹⁶⁸. The **Steering Committee** is assisting the General Board and consists, among others, of the Chair and the Vice-Chair of the ESRB and five other members of the General Board who are also members of the ECB's General Council¹⁶⁹, and Members of the **Advisory Technical Committee**, which provides advice and assistance on technical issues, are representatives of the institutions and bodies represented in the General Board and the Steering Committee¹⁷⁰.

After the UK's exit from the EU, and irrespective of the future EU-UK relationship, the Governor of the BoE will cease to participate in the General Board (he currently serves as its Vice-Chair) and will not be eligible for participating in the Steering Committee either (he currently participates in his capacity as Vice-Chair). The high-level representatives of the UK PRA and/or¹⁷¹ the UK FCA will also cease to be members of the General Board without voting rights, while BoE representatives will not be eligible any more for participation in the Advisory Technical Committee either.

In accordance with **Regulation (EU) No 1096/2010**, the Secretariat of the ESRB is provided by the ECB¹⁷². Since the ESRB does not have its own budget and the financial (and human) resources necessary for fulfilling the task of ensuring the Secretariat are also provided by the ECB¹⁷³ the UK's exit from the EU will have no impact on the ESRB's finances.

4.2.2. The European Supervisory Authorities (ESAs)

Termination of the UK-EBA Headquarters Agreement: In accordance with Article 7 Regulation (EU) No 1093/2010, the **EBA has its seat in London**. This decision was taken, *inter alia*, as a demonstration of the fact that the EBA (like all three ESAs and the ESRB) has been assigned tasks which refer to the entire EU single market. On the basis of that Article, the UK Government and the EBA signed a 'Headquarters Agreement' on 8 May 2012 (hereinafter '**UK-EBA Headquarters Agreement**')¹⁷⁴.

¹⁶⁶ This body is governed by Articles 12(1) and 12(3) EBA Regulation (EU) No 1092/2010.

¹⁶⁷ Article 4(1) EBA Regulation.

¹⁶⁸ Article 6(1)-(2) EBA Regulation.

¹⁶⁹ Article 11(1) EBA Regulation. Its full composition does not reflect the composition of the General Board, in which members from national central banks have a clear majority.

¹⁷⁰ Article 13(1) EBA Regulation.

¹⁷¹ Article 6(3) EBA Regulation.

¹⁷² Article 2 Regulation (EU) No 1096/2010.

¹⁷³ Article 3(1) Regulation (EU) No 1096/2010.

¹⁷⁴ Treaty Series No 29 (2012);

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/228541/8363.pdf.

In view of the UK's exit from the EU, and irrespective of the future EU-UK relationship, **Article 7 of the EBA Regulation** must be amended taking into account the fact that an EU agency/body may not be established in a third country. The decision on the EBA's new seat is an intra-EU political one and is not bound by any legal requirements.

The UK-EBA Headquarters Agreement may be terminated in accordance with **Article 20**, which requires an Exchange of Notes between the UK Government and the EBA¹⁷⁵. Given that the EBA's Headquarters will be relocated, it is provided that the Agreement will cease to be in force after the period *reasonably* required for such a transfer and for the disposal of the property of the EBA¹⁷⁶. Hence, preparations for the determination of a new location should not be postponed. In any event, the Headquarters Agreement will remain in force in respect of any events which occurred before its date of termination¹⁷⁷. Any dispute between the UK Government and the EBA concerning the Agreement's interpretation or application should be settled by negotiation or any other agreed method; otherwise, it must be referred for final decision, at the request of either contracting party, to a tribunal of three arbitrators¹⁷⁸. Following the determination of a new seat, a new Headquarters Agreement will have to be signed with the Government of the respective Member State.

Impact on the governing bodies of the ESAs: In accordance with their statutory Regulations, the governance structure of all three ESAs includes a Board of Supervisors, a Management Board, a Chairperson¹⁷⁹, and an Executive Director¹⁸⁰. The **Board of Supervisors** comprises the Chairperson (without a voting right), the head of the national (public) authority which is competent for the micro-prudential supervision of financial institutions in each Member State¹⁸¹, and some non-voting members representing various EU institutions and agencies¹⁸². From the UK point of view, the head of the UK PRA is a member in the Board of Supervisors of EBA and the EIOPA and the head of the UK FCA a member in the ESMA's Board of Supervisors. In addition, the Board of Directors may admit observers¹⁸³, a status which currently is granted to the head of the national (public) authority which is competent for the micro-prudential financial supervision in the EEA countries Norway, Liechtenstein and Iceland.

Members of the **Management Board** are the Chairperson and six other members of the Board of Supervisors, elected by and from the voting members¹⁸⁴. **Currently, no representative of the UK PRA or of the UK FCA is a member of this body in any ESA.**

After the UK's exit from the EU, and irrespective of the future EU-UK relationship, the heads of the UK PRA and of the UK FCA will cease to be members of the Board of Supervisors of the three ESAs¹⁸⁵ and they will also not be eligible for becoming members of

¹⁷⁵ Article 20(2) UK-EBA Headquarters Agreement (2012).

¹⁷⁶ Article 20(3) UK-EBA Headquarters Agreement (2012). See on this also Article 10 UK-EBA Headquarters Agreement (2012) on the resale of goods.

¹⁷⁷ Article 20(4) UK-EBA Headquarters Agreement (2012).

¹⁷⁸ Article 18 UK-EBA Headquarters Agreement (2012).

¹⁷⁹ Articles 48-50 Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010.

¹⁸⁰ Articles 51-53 Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010. This is without prejudice to the joint bodies of the ESAs, i.e. the Joint Committee (governed by Articles 54-57 Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010) and the Board of Appeal (governed by Articles 58-59 Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010). For more on all these bodies, see Wymeersch, pp. 288-308.

¹⁸¹ These authorities are defined, differently, in Article 4, point (1) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010.

¹⁸² Article 40(1) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010. The operation of this body is governed by Articles 40-44.

¹⁸³ Article 40(7) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010, first sub-paragraph.

¹⁸⁴ Article 45(1) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010, first subparagraph. The operation of this body is governed by Articles 45-47 Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010.

¹⁸⁵ See also Moloney, p. 79.

their Management Board. Nevertheless, if the UK were to remain a member of the EEA, they could potentially be admitted as observers.

Impact on the budget of the ESAs: The ESAs have their own budget, which is being adopted by their Board of Supervisors and then transmitted to the Commission for inclusion in the General Budget of the EU¹⁸⁶. Implementation of the budget is a task assigned to their Executive Director (who is functioning as ‘authorising officer’)¹⁸⁷ and its control is governed by **Article 64(2)-(9)** ESAs Regulations. Budget revenues consist of three sources:

- The first being obligatory contributions from the national authorities which are competent for the micro-prudential supervision of financial institutions¹⁸⁸. These contributions must be made in accordance with a formula based on the weighting of votes as set out in **Article 3(3)** of **Protocol (No 36)** ‘on transitional provisions’ attached to the Treaties¹⁸⁹, which for this purpose continue to apply (beyond the established deadline)¹⁹⁰. The UK’s weighting of votes under this Article is 29 votes out of 352 votes in total, ranking first along with that of Germany, France and Italy (8.49 % each)¹⁹¹.
- The second source is a subsidy from the EU, entered in its General Budget (Commission Section).
- The third source are any fees paid to the Authorities in the cases specified in the relevant instruments of EU law (Article 62(1), points (b)-(c) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010).

In that sense, the ESAs are not financially independent. It is evident that, since the UK PRA and the UK FCA will cease to be members of the ESAs after the UK’s exit from the EU, and irrespective of the future EU-UK relationship, the obligatory contributions to be paid by other national authorities-members will increase significantly. The distribution of this additional burden will depend:

- on the outcome of the re-adjustment of the weightings set out in **Article 3(3) of Protocol (No 36)**, if this were to be maintained (which may not be the case, since in general weightings should not continue to apply); or
- on the weightings under any new formula to be adopted ad hoc; or
- on whether the EU would also be willing (a very unlikely scenario) to increase its subsidy accordingly in order to absorb part of the difference¹⁹².

4.2.3. The four ‘Comitology Committees’ in the financial system

Finally, for the sake of completeness, also noteworthy is a minor institutional change of horizontal nature, which will have an impact on the making of EU financial law. After the entry into force of the Treaty of Lisbon, the ‘Comitology procedure’ applies only to implementing acts adopted in accordance with **Article 291 TFEU**¹⁹³. It is governed by

¹⁸⁶ Article 63(5) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010.

¹⁸⁷ Article 64(1) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010.

¹⁸⁸ Article 62(1), point (a) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010.

¹⁸⁹ OJ C 202, 7.7.2016, pp. 321-326.

¹⁹⁰ Article 62(1), point (a) Regulations (EU) No 1093/2010, 1094/2010 and 1095/2010.

¹⁹¹ On the ESAs budget see Wymeersch, pp. 311-313.

¹⁹² According to Wymeersch, p. 311 (at 9.292), burden-sharing between national authorities and the subsidy from the General Budget has been agreed (in the absence of an explicit provision in the respective Regulations) at a 40/60 ratio.

¹⁹³ On these acts see Craig, pp. 57-66 and 260-282, and Schoo, pp. 2337-2344.

Regulation (EU) No 182/2011 laying down the rules and general principles concerning mechanisms for control by Member States of the Commission's exercise of implementing powers¹⁹⁴, and lays down rules and general principles governing the mechanisms that apply if a legally binding EU act (a 'basic legal act') identifies the need for uniform conditions of implementation and subjects the adoption of implementing acts by the Commission to the control of Member States¹⁹⁵. Under this Regulation, when adopting implementing acts under **Article 291 TFEU**, the Commission is assisted by a 'Comitology Committee' set up by virtue of a basic legal act.

This procedure is of particular importance to EU financial services law, since several of the legislative acts (within the meaning of **Article 289 TFEU**) which constitute its sources empower the Commission to adopt (delegated and) implementing acts. In the financial sector, there are four such Committees:

- the European Securities Committee (**ESC**), which entered into operation on 7 June 2001¹⁹⁶;
- the Financial Conglomerates Committee, which started operating in 2003¹⁹⁷;
- the European Banking Committee (**EBC**)¹⁹⁸; and
- the European Insurance and Occupational Pensions Committee (**EIOPC**), which entered into operation on 13 April 2005¹⁹⁹.

The institutional change consists in the fact that after the UK's exit from the EU these Committees will be reduced in size, which may affect decision-making in cases where simple majority is required.

4.2.4. The Banking Union

The creation of the Banking Union establishing a Single Supervisory Mechanism (**SSM**) for credit institutions²⁰⁰ and a Single Resolution Mechanism (**SRM**)²⁰¹, and a Single Resolution Fund (**SRF**) which is governed by the SRM Regulation and by the Intergovernmental Agreement (No 8457/14) between 26 EU Member States ('SRF Agreement')²⁰² for Member States in the euro area and participating Member States. Sweden and the UK are the only Member States which are not signatories to the SRF Agreement²⁰³. **As the UK is not participating in the Banking Union, this set-up will not be affected.**

¹⁹⁴ OJ L 55, 28.2.2011, pp. 13-18. This Regulation repealed Council Decision 1999/468/EC of 28 June 1999, OJ L 184, 17.7.1999, pp. 23-26, as amended by Council Decision 2006/512/EC of 17 July 2006, OJ L 200, 22.7.2006, pp. 11-13.

¹⁹⁵ Article 1 Regulation (EU) No 182/2011. For details on this Regulation see Gortsos (2016).

¹⁹⁶ Commission Decision 2001/528/EC of 6 June 2001 establishing the European Securities Committee, OJ L 191, 13.7.2001, pp. 45-46.

¹⁹⁷ Article 21 Directive 2002/87/EC of the European Parliament and of the Council on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate (...), OJ L 35, 11.2.2003, pp. 1-27.

¹⁹⁸ Commission Decision 2004/10/EC of 5 November 2003 establishing the European Banking Committee, OJ L 3, 7.1.2004, pp. 36-37.

¹⁹⁹ Commission Decision 2004/9/EC of 5 November 2003 establishing the European Insurance and Occupational Pensions Committee, OJ L 3, 7.1.2004, pp. 34-35.

²⁰⁰ Governed by Council Regulation (EU) No 1024/2013.

²⁰¹ Governed by Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund (...), OJ L 225, 30.7.2014, pp. 1-90.

²⁰² Intergovernmental Agreement;
http://register.consilium.europa.eu/content/out?lang=EN&typ=ENTRY&i=SMPL&DOC_ID=ST%208457%202014%20COR%201.

²⁰³ For a Compendium of the legal acts governing the Banking Union (as of summer 2015) see Binder, Gortsos.

The third main pillar of the Banking Union, i.e. the European Deposit Insurance Scheme (**EDIS**) proposed by the European Commission²⁰⁴, is still negotiated in Council and Parliament (November 2016). As this proposal spans the whole EU there could be effects.

N.B. The UK's exit from the EU will neither have an impact on the Direct Recapitalisation Instrument of the European Stability Mechanism (**ESM**).

4.3. The European Investment Bank

The operation of the European Investment Bank (**EIB**) regarding the financing of investment projects, in order to contribute to the balanced and smooth development of the single market in the interest of the EU will, in principle, remain unaffected by the UK's exit from the EU. Nevertheless, there are three aspects on which there will be an impact: its capital, the composition and the decision-making process of its governing bodies.

In this respect, it should be noted that the share of the UK in the EIB's capital as from 1 July 2013 amounts to EUR 39,195,022 (16.11 % of its total capital). The UK thereby constitutes, alongside with Germany, France and Italy, **one of the EIB's main shareholders**. It also participates in the composition of its governing bodies, namely the **Board of Governors**, which lays down the guiding principles and the high-level policies of the financing operations of the EIB, the **Board of Directors**, which is mainly responsible for the approval of financing operations of investment projects, and the **Management Committee**, which is liable for the day-to-day management of the EIB under the authority of its President and the supervision of the Board of Directors.

Upon its exit from the EU, and irrespective of the future EU-UK relationship, the UK will cease to be a member of the EIB; accordingly, arrangements will have to be made with regard to its share in the EIB's subscribed capital and its paid-up capital²⁰⁵. Furthermore, it will cease to participate in the above-mentioned governing bodies²⁰⁶ of the EIB and the relevant decision making-process will have to be amended accordingly²⁰⁷.

²⁰⁴ COM(2015) 586 final of 24.11.2015.

²⁰⁵ Detailed provisions regarding the EIB's capital are laid down in Articles 4-5 of Protocol (No 5) on the Statute of the European Investment Bank, OJ C 202, 7.6.2016, pp. 251-264.

²⁰⁶ As of December 2016, the UK is represented by its Finance Minister in the Board of Governors; in the Board of Directors by one appointed Director and two alternates; and in the Management Committee by one member appointed by the Board of Governors acting upon a proposal from the Board of Directors; <http://www.eib.org/about/governance-and-structure/index.htm>.

²⁰⁷ Articles 6-12 Protocol (No 5) on the Statute of the European Investment Bank.

5. CONCLUSIONS

The first main conclusion is that the EU regulatory framework provides for a favourable regime in relation to trade in services within its territory, including financial services. More specifically, based on the principle of the EU passport, a regulated financial firm having its head office in a Member State may establish branches and/or provide cross-border banking services in any other EU Member State, provided that the home Member State's competent authorities deem that the conditions laid down in EU law are fulfilled. The EU passport is one of the key benefits arising from access to the integrated EU single market, which the UK would lose if it were to be granted third-country status. In such a case, UK financial firms intending to provide investment services in the EU will need to:

- either choose to establish themselves through a subsidiary in a Member State and operate across the EU making use of the EU passport through this subsidiary; or
- comply with the different legislative framework of each Member State, given that the relevant legislation does not provide for the application of a uniform legislative framework for third-country enterprises.

A second main conclusion of this study is that the participation of the UK government, the BoE and other UK administrative authorities in international organisations and international financial fora, which constitute the international institutional framework governing the financial system, is a guarantee that the UK financial system and UK financial law will continue both to influence and be influenced and shaped by international regulatory developments with regard to safeguarding financial stability and attaining other policy objectives concerning financial regulation, supervision and oversight. This may prove a safe haven for the shaping of the future EU-UK relationship in financial services, to the extent that the financial system and the financial law of the (other) EU Member States are also influenced by these international regulatory developments (either directly as a result of their participation in the above-mentioned international organisations and financial fora or through the transposition of the (international) soft law elaborated by these international financial fora into EU law).

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ANNEX

Main categories of regulated financial firms and categories of trading venues under EU financial law

| 1. Financial firms in the banking sector and in payments | |
|--|---|
| Category | Definition |
| 'credit institution' | an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account |
| 'financial institution' | <p>an undertaking, other than a credit institution (or an investment firm), the principal activity of which is to acquire holdings or to pursue any of the activities listed in points (2) to (12) and (15) of Annex I to the CRD IV:</p> <ul style="list-style-type: none"> • including a financial holding company, a mixed financial holding company, a payment institution, and an asset management company, but • excluding 'insurance holding companies' and 'mixed-activity insurance holding companies' as defined in Directive 2009/138/EC (Solvency II) |
| 'payment institution' | a legal person that has been granted authorisation to provide and execute payment services throughout the EU |
| 'electronic money institution' | a legal person that has been granted authorisation to issue electronic money; 'electronic money' means electronically, including magnetically, stored monetary value as represented by a claim on the issuer which is issued on receipt of funds for the purpose of making payment transactions as defined in point 5 of Article 4 of Directive 2007/64/EC, and which is accepted by a natural or legal person other than the electronic money issuer |

| 2. Financial firms in capital markets | |
|--|---|
| Category | Definition |
| 'investment firm' | (in principle) any legal person whose regular occupation or business is the provision of one or more 'investment services' to third parties, and/or the performance of one or more 'investment activities' on a professional basis; 'investment services and activities' are defined as meaning any of the services and activities listed in Section A of Annex I relating to any of the instruments listed in Section C of Annex I Directive 2014/65/EU (MiFID II) |
| 'UCITS' | an undertaking the sole object of which is collective investment in transferable securities or in other liquid financial assets of capital raised from the public and which operates on the principle of risk-spreading, with units which are, at the request of holders, repurchased or redeemed, directly or indirectly, out of those undertakings' assets |
| 'management company' | a company, the regular business of which is the management of UCITS in the form of common funds or of investment companies (collective portfolio management of UCITS) |
| 'alternative investment fund managers' | legal persons whose regular business is managing one or more alternative investment funds, i.e. collective investment undertakings, including investment compartments thereof, which raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors, and do not require authorisation pursuant to Article 5 of Directive 2009/65/EC (UCITS IV) |
| 'central counterparty' | 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 |
| 'credit rating agency' | a legal person whose occupation includes the issuing of credit ratings on a professional basis; 'credit rating' means an opinion regarding the creditworthiness of an entity, a financial instrument, or an issuer of a financial instrument, issued using an established and defined ranking system of rating categories – <i>directly supervised by the ESMA</i> |
| 'data reporting services providers' | (1) 'approved publication arrangements': a person authorised under Directive 2014/65/EU (MiFID II) to provide the service of publishing trade reports on behalf of investment firms pursuant to Articles 20-21 of Regulation (EU) No 600/2014 (2) 'consolidated tape providers: a person authorised under Directive 2014/65/EU (MiFID II) to provide the service of collecting trade reports for financial instruments listed in Articles 6, 7, 10, 12- 13, and 20-21 of Regulation (EU) No 600/2014 from regulated markets, multilateral trading facilities (MTFs), organised trading facilities (OTFs) and approved publication arrangements and consolidating them into a continuous electronic live data stream providing price and volume data per financial instrument (3) 'approved reporting mechanisms': a person authorised under Directive 2014/65/EU (MiFID II) to provide the service of reporting details of transactions to competent authorities or to ESMA on behalf of investment firms |
| 'central securities depository' (CSD) | a legal person operating a securities settlement system and providing at least one other core service listed in Section A of the Annex of Regulation (EU) No 909/2014 |
| 'trade repository' | a legal person that centrally collects and maintains the records of derivatives (under the EMIR), and a legal person that centrally collects and maintains the records of SFTs (under Regulation (EU) 2015/2365) – <i>directly supervised by the ESMA</i> |

| 3. Financial firms in the insurance and re-insurance sector | |
|--|--|
| Category | Definition |
| 'insurance undertaking' | a direct life or non-life insurance undertaking which has received authorisation |
| 'reinsurance undertaking' | an undertaking which has received authorisation to pursue reinsurance activities, whereby 'reinsurance' means either of the following: <ul style="list-style-type: none"> • the activity consisting in accepting risks ceded by an insurance undertaking or third-country insurance undertaking, or by another reinsurance undertaking or third-country reinsurance undertaking, or • in the case of the association of underwriters known as Lloyd's, the activity consisting in accepting risks, ceded by any member of Lloyd's, by an insurance or reinsurance undertaking other than the association of underwriters |
| 4. Financial firms operating horizontally | |
| 'financial conglomerate' | a group or subgroup, where: <ul style="list-style-type: none"> • a regulated entity is at the head of the group or subgroup, or • at least one of the subsidiaries in that group or subgroup is a regulated entity (i.e. a credit institution, an insurance undertaking, a reinsurance undertaking, an investment firm, an asset management company or an alternative investment fund manager), which meets two additional specific criteria |
| 'financial holding company' | a financial institution: <ul style="list-style-type: none"> • the subsidiaries of which are exclusively or mainly credit institutions, investment firms or financial institutions, at least one of such subsidiaries being a credit institution or an investment firm, and • which is not a mixed financial holding company |
| 'mixed financial holding company' | a parent undertaking, other than a regulated entity, which, together with its subsidiaries – at least one of which is a regulated entity which has its registered office in the EU – and other entities, constitutes a financial conglomerate |
| 'mixed-activity holding company' | a parent undertaking, other than a financial holding company, a credit institution or a mixed financial holding company, the subsidiaries of which include at least one credit institution or investment firm |
| 5. Trading venues | |
| 'regulated markets' | multilateral systems operated and/or managed by a market operator, which bring together or facilitate the bringing together of multiple third-party buying and selling interests in financial instruments – in the system and in accordance with non-discretionary rules – in a way that results in a contract, in respect of the financial instruments admitted to trading under their rules and/or systems, and which are authorised and function regularly in accordance with Articles 44-56 of Directive 2014/65/EU (MiFID II) |
| 'multilateral trading facilities' ('MTFs') | multilateral systems, operated by an investment firm or a market operator, which bring together multiple third-party buying and selling interests in financial instruments – in the system and in accordance with non-discretionary rules – in a way that results in a contract in accordance with the provisions of Articles 5-43 2014/65/EU (MiFID II) |
| 'organised trading facilities' ('OTFs') | multilateral systems which are not a regulated market or an MTF and in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in a way that results in a contract also in accordance with the same above-mentioned provisions |
| 'market operator' | a person or persons managing and/or operating the business of a regulated market and may be the regulated market itself |

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