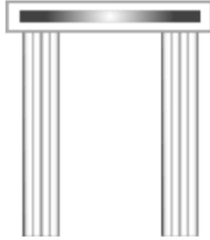
A Blueprint for Brexit

The Future of Global Financial Services and Markets in the UK

POLITEIA

A FORUM FOR SOCIAL AND ECONOMIC THINKING



POLITEIA

A Forum for Social and Economic Thinking

Politeia commissions and publishes discussions by specialists about social and economic ideas and policies. It aims to encourage public discussion on the relationship between the state and the people. Its aim is not to influence people to support any given political party, candidates for election, or position in a referendum, but to inform public discussion of policy.

The forum is independently funded, and the publications do not express a corporate opinion, but the views of their individual authors.

www.politeia.co.uk

A Blueprint for Brexit

The Future of Global Financial Services and Markets in the UK

Barnabas Reynolds

POLITEIA

2016

First published in 2016
by
Politeia
14a Eccleston Street
London SW1W 9LT
Tel. 0207 799 5034

E-mail: secretary@politeia.co.uk
Website: www.politeia.co.uk

© Politeia 2016

ISBN: 978-0-9926340-9-4

Cover design by John Marenbon

Politeia gratefully acknowledges support for this publication from

Foundation for Social and Economic Thinking (FSET)

Printed in the United Kingdom by:
Millnet Limited
6-7 Princes Court
11 Wapping Lane
London E1W 2DA

PREFACE*

As ministers prepare for the UK's departure from the EU, Britain's financial services will be at the centre of the Brexit stage. Many who lead the industry welcome the opportunities which Brexit will bring to build on their position as market leaders in the EU and globally. The Prime Minister, Theresa May, has made clear that her government will honour the people's mandate to leave the EU. "Brexit", as she has declared "means Brexit, and Britain will make a success of it." But what must now be decided is the best course from the many new options that the referendum has opened up.

These services cover a huge variety of different activities. They include businesses such as investment and fund management, international insurance, trading in foreign exchange and derivatives, with as much diversity in size as in function; they include the big banks; and they also include the legal and other professional services, from actuarial to accounting, which underpin the sector. Whether home-grown or of overseas origin, all in the sector benefit from the security which Britain's stable legal framework brings and the democratic and reliable political system under which the laws of this country are made. Brexit could bring further stability by removing the UK from potential uncertainties, political or economic, of the Eurozone; by encouraging greater legal certainty in place of what can be a tension in accommodating EU law to Britain's statute and common law tradition; and by further facilitating the competitive market system on which Britain's success and prosperity has evolved.

That stability will continue to matter to the important role financial services play in Britain's economy: they have a good trade surplus (although the precise figure is difficult to calculate, the surplus is around 7 per cent a year); they attract global and EU business; and for centuries London has been a global capital for financial services, rivalled only today by New York in world primacy. That position stretches back more than two centuries, existing before Britain joined the EU and before the "passport" was introduced in its full form in 2007. There are very good legal, economic and trade reasons to recognise that after Brexit it can be even stronger.

Many in financial services and the City have already welcomed the freedom Brexit will bring to the sector. Built on an ethic of free trade and competition over centuries under Britain's system of law, many consider that success has been constrained by the prescriptive nature of EU legislation, one in which EU lawmaking tends to impose a single "rule book", or one insensitive to the diversity of the sector. They want the government to move quickly and decisively to the new arrangements for access for our trade to global and EU markets, just as other successful systems (such as the US and Australia) now have.

Others in the sector recognise that if the country had voted to remain, there would be a period of further uncertainty as the Eurozone continues on the path towards political and monetary union and individual member states prepare for their national elections. Such difficulties, and the dangers of our businesses being exposed to

---

* This preface is written by Sheila Lawlor, Director of Politeia, to set the wider context of politics and policy for the specialist legal analysis that follows.

them, make Britain's extrication from the single market all the more important and timely.

There are, however, some in the City who want arrangements to stay as they are. They believe that the framework under which they now operate works reasonably well in facilitating cross-border trade. They want to remain in the single market or a similar set up, and they prioritise keeping the EU passport for financial services. Those priorities could even be at the cost of allowing the EU control over UK laws and regulation, as well as the supervision of UK services. For this group, if the City and the whole sector are to continue to flourish, there appears to be no alternative.

Such an approach is mistaken. Not only is it based on false assumptions, but it fails to respect the outcome of the referendum. There were similar fears when the UK stayed out of the single currency; the exodus from our shores did not take place in the 1990s, nor is it likely to happen now. Britain's economy has always been built on markets, freedom and flexibility. Leaving the single market will bring benefits to the financial markets. Some institutions may wish to reduce the size of their presence in the UK, uncertain about the transition to a more free market world. But most will accommodate themselves to the new arrangements and flourish.

The Prime Minister, having reassured the voters that Brexit will mean Brexit, is now, with her ministers, considering the options. The prospect of returning to the EU by the back door, when voters have decided to leave by the front, has been ruled out. But there are many good reasons to believe that, despite the concerns or even objections raised by some, the options for Britain's financial services out of the single market are in fact very good.

In the Paper that follows, Barnabas Reynolds, a UK and EU regulatory lawyer, working across the financial sector, analyses the current position as it now affects business and explains the options for the future. He addresses some of the (often mistaken) assumptions about the arrangements needed to continue trading freely whether with EU counterparties and customers, or globally.

He explores the future, both in terms of the advantages of leaving the single market and of the options for future trade, and presents two models under which that could be achieved. Equivalence arrangements now in place for US trade with the EU for some services are one option, though the gaps would need to be filled and an ancillary procedural deal agreed. This "Expanded Equivalence" model would permit some removal and reworking of EU laws (identified by Reynolds), although some constraints as to the UK's ability to determine its law and regulation would remain.

Alternatively, a "Financial Centre" model would allow the UK to establish a market-friendly regulatory framework, set in line with global standards and best practices now operating, and to welcome businesses that met these standards to the UK. This model would allow Britain to reshape its regulatory structures as well as moving away from what Reynolds sees as "the blanket of unnecessary processes introduced in EU laws" so as to "focus instead on outcomes".

Ministers should therefore consider these options as a far better alternative for the sector and the City than that proposed by those for whom continuing membership of the single market seems, mistakenly, to be preferred.

The financial sector can, as Barnabas Reynolds shows, welcome the opportunities created by our break with the EU, to continue trading even more successfully on a new basis, both with the EU and globally. The new world that will emerge, as Reynolds explains:

> … is not to be feared. It allows the UK to regain the prominence it enjoyed under the global regulatory framework of the early 1990s and before, reinforced with a modern understanding of the importance of systemic risk mitigation and consumer protection, and enhanced by a more radical re-think for which Brexit provides an opportunity. These are areas in which the UK has rightly taken the lead at an international level and which must find a place in post-Brexit laws… it is not simply a matter of "more" or "less" regulation, but rather better regulation to which the UK should aspire.

Sheila Lawlor

Director, Politeia
3 November 2016

THE AUTHOR

Barnabas Reynolds is a partner at Shearman & Sterling LLP, where he is head of the global financial institutions advisory practice. He practises in UK and EU regulation and advises all types of financial markets participants on their legal and regulatory situations, difficulties and opportunities, and their legal risk profiles.

After graduating in law from Downing College, Cambridge he took an LLM at Queens' College, Cambridge. He lives in London.

Reynolds co-edits Sweet & Maxwell's *Journal of International Banking Law and Regulation* and is the co-author of *Shipowners' Limitation of Liability*, Kluwer Law, 2012. He writes regularly on financial services regulatory matters including, recently, client money and assets, MiFID II, shadow banking, margin for uncleared swaps, derivatives clearing and senior management liability.

FOREWORD

On 23 June 2016, the UK voted to leave the EU. This Paper expresses no view on that outcome; it merely sets out a blueprint for the legal and regulatory landscape in the UK following Brexit, and the ways in which the UK's financial services sector and global markets can continue to flourish from outside the EU.

Since the referendum, there has been much discussion on the shape the UK's legal system should take after Brexit and the ways in which the UK's financial services sector will function in practice. Many have argued that the current passporting arrangements must be maintained, or that some kind of grand bilateral deal between the EU and the UK must be established to replace them.

In fact, a detailed analysis of the passporting system has revealed that it is far from indispensable. It is not critical for the provision of most services to EU customers. Maintaining the passporting system (or a similar system based on a grand bilateral agreement) would not only likely require concessions on sovereignty, free movement of persons and payments to the EU, but would also result in the UK's financial services sector being subject to rules which the UK had no hand in formulating. This would be problematic both from a democratic perspective and, as such rules are unlikely to have the success of the City as a priority, from a substantive and practical perspective.

This Paper provides a blueprint for the UK's global financial services sector after Brexit, and sets out two models under which the sector can succeed. The model selected will depend to a large extent on politics and the willingness of the EU to negotiate in its best economic interests.

Under either model, it will be possible for almost all parts of the financial sector in the UK to carry on providing services across Europe and the world without interruption, even without the passporting process. By building upon the UK's natural advantages – of time-zone, English law and language, and an established financial ecosystem and talent pool – the UK can create a highly competitive environment for the City outside the EU.

Barnabas Reynolds

Partner, Shearman & Sterling LLP
3 November 2016

Special thanks to Oliver Linch for his extensive help in writing this Paper. Many thanks also to Thomas Donegan, John Adams, Ellerina Teo, Aysuria Chang, Daniel Frost and Christopher Hobson for their help. All faults that remain, and the views expressed, are my own.

Table of Contents

FOREWORD I

1. The UK's Financial Services: Seizing the Brexit Opportunity to Re-Boot 3

Introduction: Brexit, the Financial Services and the Options for Policy 3
Passporting: An Unattractive Post-Brexit Solution 4
An Extensive EU/UK Bilateral "New Deal": Undesirable and Unlikely 5
Equivalence-Based Access: Desirable, Achievable and Realistic 5
A Practical Alternative: The Financial Centre Model 6
Trading and Clearing In Euros 8

2. The Policy: From Status Quo to Next Steps 9

Global Standards & Best Practices: Financial Regulation post-2008 9
The EU and its Regulations: Unfocussed and Burdensome 9
The Future of the EU: Unleashing the "Protectionist" Instinct 11
Maintaining the Passport: Politically and Practically Problematic 11
Minimal Request for Bilateral Deal 13
The UK as a Global Leader 14
Freedom to Trade and Clear in Reserve Currencies 14
Additional UK Domestic Reforms: Promoting Competitiveness and Preventing Systemic Risk 15

3. UK Open For Business: EU Access to the UK 16

4. UK Access to the EU 17

How Business Crosses Borders 17
Analysing "Cross-Border" Activities: A Closer Look 17
Reverse Solicitation Exemptions 18
Third-Country Equivalence 18

5. Expanded Equivalence Model 20

Equivalence in Practice: How it Operates 20
De-politicisation 21
Mutual Desirability 22
Legislative Process 22
Predictability: Tackling Uncertainty through a Procedural Deal 23
Opportunity to Rationalise UK Laws 24
How to Proceed: A Step-by-Step Practical Approach 25
An Appropriate Compromise 25
Detailed Analysis 26

6. Financial Centre Model 27

Financial Centre Model: Overview 27

Opportunity for a Comprehensive Re-Think 27

Precedent: the World's Oldest "New" Financial Centre where Counterparties and Customers Come to the City 28

The UK-EU Relationship: Attracting Business to the UK 29

The Need for a Clear Choice 30

7. The Implications for the UK's Financial Businesses: Case Studies 31

Case Study 1: Corporate and Investment Banking 31

Case Study 2: Retail Banking/Private Wealth Management 32

Case Study 3: Fund Management (Retail Funds) 33

Case Study 4: Fund Management (Non-Retail Funds) 34

Case Study 5: Insurance 35

8. The EU's Next Regulations: Avoiding Unnecessary New Measures 37

Annex A: Sectors with Existing Equivalence Regimes 39

Annex B: Sectors That Lack Existing Equivalence Regimes 68

Annex C: Summary of Equivalence Decisions 86

Annex D: Glossary of Terms Used 89

1. The UK's Financial Services: Seizing the Brexit Opportunity to Re-Boot

Introduction: Brexit, the Financial Services and the Options for Policy

As the UK prepares to leave the EU, the assumption in some parts of the financial services community persists that access to the EU's "passporting" regime should be preserved in the UK at any cost following Brexit. This proposition should be reassessed. It is based on an erroneous assumption about the benefits of EU financial services laws and ignores the significant advantages of moving the UK to better regulation based on achieving certain outcomes (rather than prescribing the minutiae of processes) outside the EU.

"The UK supports the most liquid and sophisticated markets in the European time-zones."

Following Brexit, the EU will continue to be an important political, social and economic partner. However, that does not mean that arrangements with the EU must be formalised at any price.

The City is a financial centre. Counterparties and customers have come together within the City over the centuries to do their financial business there with one another. The UK supports the most liquid and sophisticated markets in the European time-zones. Access to the EU's single market matters to the UK but, as this paper explains, access to EU financial services counterparties and customers in the single market (as for instance the US accesses them) and membership of the single market are not the same thing. Much business conducted in the City is not cross-border as a matter of law, or could, with minor adjustments, be made not to be cross-border. Counterparties and customers can, if necessary, come to the City as they have always done.

Passporting is a system that allows a firm authorised under one of the EEA's single market directives to carry on activities in another member state on the basis of its home state authorisation.

The "passport", which was rolled out in its full form relatively recently in 2007 for investment businesses, has enabled counterparties and customers located elsewhere within the EU to be dealt with directly and quite easily. This has reduced costs for EU counterparties and consumers and for UK-based financial institutions when dealing with EU counterparties and consumers.

However, there are numerous drawbacks associated with the EU framework under which the passport operates. For many years and in many sectors, there have been concerns in the UK about the direct and indirect costs imposed by ill-focussed and poorly drafted EU regulation. This has been a continuing theme of EU political wrangling. The existence of the passport has by no means been fundamental to the success or importance of the City. EU regulation has often been improperly focussed, has added unnecessary layers of processes and overheads. Most notably, it failed to prevent the 2008 financial crisis or to cater for or militate against the dramatic events currently unfolding in the Eurozone financial system. These shortcomings have already prompted concern amongst many businesses about the direction of EU legislation, its detrimental impact and the uncertainty or potential damage that will follow closer political and economic integration in the Eurozone.

Important benefits could be gained from the UK having fuller control over its rulemaking. This could, if managed properly, more than offset any costs of removing the passport, by making the UK a more attractive place to do business than the EU in light of the EU's increasingly cumbersome and protectionist regulatory regime.

The view that UK financial services regulation post-Brexit should be based on keeping the passport to "minimise disruption" misses the point. By definition, maintaining the status quo, or something close to it, would minimise disruption short-term. Such a solution, however, would raise significant sovereignty concerns, which are as relevant to the financial industry as to the UK itself, and would fail to capitalise on the considerable opportunities that Brexit presents. It would also prevent the UK from protecting the financial markets from any fall-out from future events. No-one can assess the level of disruption that will follow closer Eurozone integration or the likely instability to which the EU seems susceptible.

Following the referendum, the balance between the (relatively mild) reduction in friction costs for EU counterparties and consumers in accessing the City through the passport system on the one hand, and the (increasingly significant) anti-market regulatory instincts of many legislators and policy-makers in the EU on the other, has shifted.

"The UK is leaving the EU and — as with all aspects of government policy — the task now is to establish how to make a success of it."

The UK is leaving the EU and – as with all aspects of government policy – the task now is to establish how to make a success of it. This paper sets out some proposals as to how that can best be achieved.

Passporting: An Unattractive Post-Brexit Solution

There are three main concerns in maintaining the passport:

a. **Rule-taking of burdensome EU regulations**. In recent times, and in particular following the 2008 financial crisis, EU financial services legislation has become overly-prescriptive. A number of costly initiatives have been introduced which are seen by many as delivering few or no benefits to consumers or regulators. Maintaining the passport would require the UK to be a "rule-taker" as regards these already inflexible and burdensome standards. The UK would also be required to adopt legislation that in the future would be made without the UK's moderating influence. EU laws are likely to become even more protectionist and problematic for the UK once the UK loses its place on the Council and in the EP.[1]

b. **Supranational bodies**. Passporting would likely require the UK to sign up to the authority of EU supranational bodies such as the EBA and ESMA, and to be subject to interpretations issued by the CJEU.

c. **Free Movement and Financial Contributions**. Continued access to the single market based on passporting is likely to involve at least some kind of commitment to free movement of people and payment towards the EU budget.

The Prime Minister, Theresa May, has ruled out arrangements which do not involve controls over EU immigration and a return of sovereignty. In any event, given the vote, the UK should ensure it is able to regulate its own markets taking into account local conditions and needs, based on its traditionally key values of free and clean markets, systemic risk protection and consumer protection. The UK will face difficulty achieving these important goals if it maintains the passport.

The problems associated with the passport are set out in more detail in "Maintaining the Passport: Politically and Practically Problematic " in Part 2.

[1] Please see the Glossary at Annex D for these and other terms used in this Paper.

An Extensive EU/UK Bilateral "New Deal": Undesirable and Unlikely

A new, major bilateral deal for the UK or some new, associate or quasi-membership of the EU, as some have proposed, seems neither practicable nor desirable, whether for the EU or the UK.

From the UK's perspective, any such deal is likely to involve significant concessions on sovereignty issues, free movement of persons and budget contributions, which are politically undesirable. From the EU's perspective, there is no appetite to "reward" the UK for leaving the EU by granting it special privileges and the EU is keen not to set an attractive precedent, which might incentivise other member states to consider their position.

The problems associated with striking an acceptable bilateral deal are set out in more detail in "Minimal Request for Bilateral Deal" in Part 2.

Equivalence-Based Access: Desirable, Achievable and Realistic

An alternative and more feasible course of action is for the UK to seek an *equivalence-based* relationship with the EU in financial services. This does not import the "four freedoms" or other concessions on sovereignty. Many EU financial services laws allow financial institutions in third countries to access the single market if the third-country's laws are deemed "equivalent" to the EU's in a relevant area. Institutions from a number of other countries enjoy this status under various pieces of existing EU legislation, including companies incorporated in the US, Japan, Singapore, Switzerland, Canada, Mexico and others. Given the UK's close political, geographical and economic ties to the EU, it is likely that an equivalence regime will be even more successful and mutually beneficial than it is in other jurisdictions.

> "Given the UK's close political, geographical and economic ties to the EU, it is likely that an equivalence regime will be even more successful and mutually beneficial than it is in other jurisdictions."

As UK rules only need to be "equivalent", not identical, this would allow a certain amount of flexibility to remove some of the burdensome and unnecessary regulatory requirements from the UK's existing framework (see "Opportunity to Rationalise UK Laws" in Part 5).[2] The "Expanded Equivalence" model set out in Part 5 would therefore involve the UK:

- removing the most unnecessarily onerous requirements, provided that their absence would not affect necessary equivalence determinations;
- moving, so far as possible while maintaining equivalence, away from the EU's process-focussed approach, to an approach based on outcomes;
- re-drafting, so far as possible while maintaining equivalence, laws in common law style, which would bring with it far greater certainty. This would also remove the additional, more hidden blanket of laws imported by implication into the EU regime by the so-called "purposive" method of interpretation, in contrast with the more direct textual reading of the relevant provisions under the common law tradition;
- moving away from poor CJEU decision-making in the financial services context. CJEU reasoning often operates less straightforwardly than judicial practice in the UK, and in any event is too condensed and insufficiently

2 The Prime Minister has noted that, for the sake of expediency, there will be a grandfathering process for many laws at the point of exit, whereby the existing EU laws will be converted into UK law for a transitional period, until such time as the UK can fully and properly reset its own regulatory framework (Theresa May, "*Britain after Brexit: A Vision of a Global Britain*", 2 October 2016).

focussed on fact-based analysis to provide the clarity that the common law brings with it; and

- removing laws designed to provide for the EU single market and for regulating competition within the EU.

Under this approach, there would only be two key issues to resolve during the Brexit negotiations:

a. **Complete coverage of equivalence-based access**. The EU should expand the availability of "equivalence" regimes to cover certain "gaps" in the current framework, which largely result from historic reasons. These include lending, primary insurance, insurance mediation, mortgage credit, settlement finality and other matters.[3] Similarly, the UK should ensure that EU institutions can continue to access UK markets through the overseas person exclusion, expanded as necessary and by introducing a reciprocal equivalence regime for branches (see "UK Open For Business: EU Access to the UK" in Part 3).

b. **The EU and UK should treat each other fairly in assessing whether their respective rules are equivalent**. It should be recognised that "equivalent" laws are not the same as "identical" laws. The EU has not required third-country laws to be identical for equivalence determinations thus far, and a similar standard should be applied to the UK, without political interference. Even after making some of the changes discussed here, many of the UK's laws should be sufficiently similar to those of the EU on Brexit and thereafter that both the UK and the EU should be able to make reciprocal equivalence determinations, provided that they treat each other fairly and in a depoliticised manner.

Equivalence-based access on this basis would allow for reciprocity and mutual benefit between the UK and the EU. Mutual access between the EU and UK would be premised on equivalence between the two jurisdictions, providing for strong, open relations between the EU and the UK and delivering the advantages of access from the EU to the City, the main financial market in its time-zones.

Although a satisfactory resolution to the two issues noted above would deliver broad equivalence-based access to the EU, the UK and EU could go further than this to reflect the historical, geographical and cultural importance of the relationship between the two. An additional agreement could be sought between the UK and EU on a procedural framework for establishing, maintaining and withdrawing equivalence for the future. That would give certainty to both parties and to financial markets participants across Europe.

The Expanded Equivalence model is set out in Part 5.

A Practical Alternative: The Financial Centre Model

The UK must be prepared for the possibility that agreement on the Expanded Equivalence model will not be achievable. This could happen because plugging the gaps in existing equivalence regimes is not politically acceptable. Or it could occur because equivalence determinations are not forthcoming, or the EU requires such a high degree of conformity with EU laws in order to be deemed equivalent that

[3] The UK could vote on changes to relevant legislation, both in the Council and the EP, before exiting the EU.

the UK is in practice unable to make the significant and meaningful changes to its rules that the UK is likely to wish to make.[4]

The UK also needs to develop an alternative model in order to determine the extent to which the equivalence-based approach is attractive. It may be that in many areas, such as the regulation of alternative investment funds, the Expanded Equivalence model would not be as attractive as reverting to the traditional UK standalone approach straight away.

Under the "Financial Centre" model set out in Part 6, the UK would reconsider its entire regulatory framework. This would involve the following:

- removing not only those particularly burdensome rules that could be removed under the Expanded Equivalence model (see "Opportunity to Rationalise UK Laws" in Part 5) but also scrutinising and tailoring its regulatory requirements across the board;
- a complete shift from the EU's process-focussed approach to a more tailored approach based on outcomes;
- a comprehensive scrutiny and, as appropriate, re-draft of laws in common-law style. The benefits of the common-law style, as previously noted, are an increase in certainty and the removal of the additional, more hidden blanket of laws which are imported by implication into the EU regime by the so-called "purposive" method of interpretation rather than by a more direct reading of the relevant law; and
- a complete shift from poor CJEU decision-making in the financial services context, with reasoning that operates sometimes by omission and in any event is too condensed and insufficiently focussed on fact-based analysis to provide the clarity that the common law brings with it.

The effect would be the development of an attractive, market-friendly regulatory framework, allowing banks and financial institutions to improve returns on equity, free from unnecessarily burdensome EU regulation.

"The effect would be the development of an attractive, market-friendly regulatory framework, allowing banks and financial institutions to improve returns on equity, free from unnecessarily burdensome EU regulation."

This world is not to be feared. It allows the UK to regain the prominence it enjoyed under the global regulatory framework of the early 1990s and before, reinforced with a modern understanding of the importance of systemic risk mitigation and consumer protection and enhanced by a more radical re-think for which Brexit provides an opportunity. Systemic risk regulation is an area in which the UK has rightly taken the lead in formulating at an international level and which must find a place in post-Brexit laws.

The Financial Centre model recognises that it is not only that EU regulation goes beyond global standards and best practices (which it does), but that it does so in untargeted and inappropriate ways, driven by social policy and other extraneous interests. This has led not simply to *more* regulation, but to *worse* regulation. It has also created an incentive for some member states to disregard important regulatory requirements, creating informal regulatory arbitrage within the EU (which was one of the main underlying causes of the 2008 financial crisis). In rebalancing the UK's regulatory framework, it must be recognised that it is not simply a matter of "more" or "less" regulation, but rather *better* regulation to which the UK should aspire.

---

4 Such an outcome would effectively mean that the UK would essentially become a "rule-taker" in all but name, and would continue to be bound by (almost) all of what seems likely to become increasingly inflexible and burdensome EU standards.

By building on the UK's reputation as an attractive, market-friendly, well-respected place to do business, the incentive (far from moving business from the UK to the EU) would be for banks to continue to be established in the UK, and have their most significant customers come to the City to transact business. This should be welcomed, and the UK should facilitate customer access wherever possible, for example by structuring its tax laws to allow UK affiliates of EU companies to be established with tax transparency. This would allow businesses that currently are cross-border to be conducted through UK affiliates of EU counterparties and up-streamed to the EU parent without incurring an undue tax burden.

This more radical solution may prove better than the Expanded Equivalence model, depending on what the EU seeks for equivalence and how protectionist EU laws become going forward. Further, in some existing areas of law, such as AIFMD or Solvency II, it could well be that the Financial Centre model is preferable for the UK regardless of any equivalence offer.

The Financial Centre model is set out in Part 6.

Trading and Clearing In Euros

Whichever model is adopted, the UK must ensure it continues to be a key centre for the trading and clearing of instruments denominated in any globally important currency, including the euro, and should robustly resist any compromises or offers to cease trading or clearing euros within the City. There is no need to make any adjustments in this regard.

The importance of maintaining full trading and clearing in euros in the City and the reasons why the EU does not have the power to take control of this business are set out in more detail in "Freedom to Trade and Clear in Reserve Currencies" in Part 2.

2. The Policy: From Status Quo to Next Steps

This Part sets out the key policy considerations to be taken into account when formulating and drafting a post-Brexit vision. Several considerations are set out below: the importance of global standards and best practices; the problems with EU regulation now and in the future; the difficulties associated with the passport; the nature of the relationship between the EU and the UK; and the UK's role on the global stage. These considerations should act as touchstones in the political discussions surrounding Brexit, and will be drivers in designing a post-Brexit regulatory framework.

Global Standards & Best Practices: Financial Regulation post-2008

After the 2008 financial crisis, the international financial community, recognising the interconnectivity inherent in sophisticated financial systems, established global rules and guidelines in a range of areas, to ensure systemic stability, clean markets and consumer protection, while seeking to allow free markets to flourish and business to boom in a healthy and transparent manner.[5]

These international standards have been implemented within the G20 framework by the FSB, the Basel Committee and IOSCO. They have been carefully crafted with input from all major countries with financial centres, with the UK playing a very significant role. The standards, along with best practices developed by banks and other financial institutions implementing those standards worldwide, represent the financial community's bulwark against future instability and financial crises.

The EU and its Regulations: Unfocussed and Burdensome

The EU has introduced a raft of wide-ranging and extensive regulatory requirements following the 2008 financial crisis. Some of these requirements were designed to implement the G20 framework, but in many cases, they exceeded international standards and introduced inefficient, prescriptive regulation, including in areas that did not contribute to the crisis.

Legislators have acknowledged possible over-reach, but have stated that the cumulative impact of the post-crisis regulations was unknowable until after the rules were fully applied. Now, evidence of the negative effects of certain regulations is clear. They have led to a reduction in the effectiveness of the financial markets in providing funding and helping manage risks in the real economy.

The EU has so far not used a reverse gear in any of its financial services rulemaking. The process has been one of inexorable accretion. Under the UK's financial services commissioner, Lord Hill, the EU was starting to review legislation introduced after the 2008 financial crisis that had over-reached. This was the first time the EU considered deregulation in financial services in any meaningful way. The programme is now in doubt following Hill's resignation and its future without the UK's more rational influence is uncertain. The review was also unable to address the structural EU backdrop of the wider panoply of relevant EU laws and the limited and unsatisfactory EU case law. Similarly, a broader exercise of EU deregulation was proposed in former Prime Minister David

[5] See in particular the G20 Pittsburgh Summit Commitments, 25 September 2009.

Cameron's EU deal of February 2016, but this is now moribund following the referendum vote.

MiFID regulates investment banking and related services such as investment advice and brokerage. It governs authorisation, organisational requirements and passporting arrangements for investment firms. It also contains a transparency regime for securities markets.

MiFID II/MiFIR: This update to MiFID will come into effect from 2018. It includes more prescriptive conduct of business and transparency rules for investment businesses and revamps the regulation of trading venues. It introduces new rules on market infrastructure access and benchmarks.

EMIR regulates derivatives markets. It imposes reporting and conduct requirements on counterparties to derivatives. It contains a passporting regime for clearing houses and trade repositories. It imposes obligations on market participants to use central clearing, report transactions, and hold collateral.

Recent and forthcoming EU legislation has continued this trend. In particular, although much of MiFID II/MiFIR constitutes somewhat uncontroversial updates to MiFID, certain aspects will represent significant and unnecessary costs to market participants in areas which are not appropriate targets for burdensome regulations, such as equity research.[6] Indeed, the implementation of MiFID II has been estimated to cost the financial industry a total of $2.1 billion in 2017, including over $1 billion in costs for buy-side investment banks and asset management firms to adopt compliance systems and processes.[7]

Four key examples demonstrate the misalignment and over-reach of EU regulatory provisions, and illustrate the kinds of areas where unfocussed and ill-calibrated regulation has had or will have an adverse impact on the market.

a. The creation of rules in MiFID II/MiFIR for transparency of derivatives trading. MiFID II/MiFIR introduces prescriptive transparency rules for bonds, position limits for commodity derivatives, market structure provisions for listed derivative clearing, and bank capital requirements applying to investment firms. All of these exceed G20 commitments.[8] This has resulted in overly-prescriptive rules that in many cases are flawed and in some cases will interfere with the operation of markets that functioned seamlessly through the 2008 financial crisis and other historical financial stress periods.

b. Under EMIR, the EU is the only major jurisdiction to require the reporting of exchange-traded derivatives to trade repositories. Such ETD trades are already reported to CCPs as a matter of course, and so such data were already available to the regulators. This leads to the duplicative reporting of millions of trades every day.

c. The market structure requirements in MiFIR seek to challenge the so-called vertical models for exchange and clearing businesses, where an exchange is connected through ownership with a clearing house. Investigations by both the UK Office of Fair Trading and the European Commission have not identified any significant competition issues with such structures. The current optionality over market structures has resulted in flawless management of risk within cleared markets in all past financial stress periods. The vertical model has propelled huge amounts of financial and product innovation in the financial markets, most notably in contrast to the alternative, horizontal model. The new rules distort competitive market behaviours and discourage investment.

d. The attempt to create a single banking market across the EU driven by Eurozone integration has led to additional problems. For example, all EU member states are required to establish depositor guarantee schemes,[9] pursuant to which banks may be required to pre-fund or contribute to

---

6 See, for example, "*Equity research reforms will slash fund managers' profits; The EU's ongoing reforms to its Mifid markets rulebook will hit managers' bottom lines, says S&P Global*", Financial News, 17 October 2016.

7 See, for example, "*MiFID II expected to cost buy-side over $1 billion*", The Trade News, 29 September 2016.

8 The FCA has noted that there is a balance to be struck between transparency in support of price formation, and encouraging the provision of liquidity, and that MiFID II arguably goes beyond the Pittsburgh G20 Commitment. The FCA further noted that, although it does seem to offer the means to strike such a balance through its provisions to calibrate transparency obligations, it would have been preferable if the framework legislation had allowed for the phasing in of the transparency regime (Tracey McDermott, Acting Chief Executive, FCA, speech to Bloomberg, "*Independence, Confidence and Fairness*", 4 February 2016).

9 Recast Deposit Guarantee Schemes Directive (Directive 2014/49/EC).

provisions with respect to banks in other member states in financial difficulties, regardless of how well-regulated or secure (or not) those other banks are. Post-Brexit, UK banks would only be liable to contribute to a depositor guarantee fund with respect to other UK banks. Their exposure to EU member states' banks would be eliminated.

These are just four examples of how, too often, EU regulatory requirements seem to have been introduced for reasons which are neither proportionate nor evidence-based.

The introduction of more prescriptive and detailed European legislation has, in many cases, not materially improved regulatory outcomes (such as the operation of fair and transparent markets) but has introduced significant new costs ultimately borne by the end user. The net effect is more costly wholesale financial services markets without any corresponding risk reduction.

The Future of the EU: Unleashing the "Protectionist" Instinct

EU financial services legislation in recent years has been more focussed on social policy and has become significantly less market-friendly, particularly in the light of the increasing voice of the Eurozone and its currency-based objectives.

A common complaint in the UK has been that legislative measures are driven by parties with no interest in the City or its financial markets; that effect will be magnified following Brexit.

Before the referendum, the UK was somewhat isolated in advocating the interests of the City, and by extension the financial sector as a whole, providing a bulwark against the less markets-focussed proposals.[10] Going forwards, EU regulatory requirements are likely to become increasingly protectionist and less free-market-orientated as a result of the UK's exit, as the UK will not be part of the decision-making process, and EU rules will be made without the moderating influence of the UK.

"Going forwards, EU regulatory requirements are likely to become increasingly protectionist and less free-market-orientated as a result of the UK's exit."

The resulting regulatory framework is likely to become significantly less attractive. It will therefore become crucial that the UK not be a "rule-taker" as regards such protectionist requirements, but that it instead maintains control over its own regulatory system.

Maintaining the Passport: Politically and Practically Problematic

Passporting allows a financial services business in one member state to access customers in another EU member state cross-border, without obtaining additional local regulatory approvals. There is a separate ability under a passport to establish a branch in another member state. Passporting, particularly the cross-border passport, has been seen as a useful tool in recent years. However, there are various shortcomings with any proposal to continue with some form of passporting following Brexit:

a. **Rule-taking of burdensome EU regulations**. Passporting is based on a common EU rulebook, commonly applied and commonly interpreted across the EEA. Any continuation of passporting would therefore mean that the UK – without a voice in the legislative process around the EU's financial services rules – would simply be a "rule-taker". Sovereignty is not only an issue for

[10] See further Howe, M; Phillips, E, "*The UK Renegotiation: What has it really achieved*", May 2016.

the UK electorate; it is also important for the financial markets to have sensible rule-making tailored to the markets.

b. **Supranational bodies**. Various EU bodies would continue to have influence and power over the UK in the application of the financial services laws but without any UK input. The UK would have no governance over these bodies following Brexit. The bodies include:

   i. the Council, which comprises representatives of the EU Member States, and has legislative authority;

   ii. the EP, which has amendment powers over EU laws;

   iii. the European Commission, which has the sole authority within the EU to propose new legislation;

   iv. the supranational ESAs,[11] which are the arbiters of interpretation and application of financial services legislation. They have step-in rights and in some sectors such as trade repositories, supervise institutions directly (including , currently, the UK-based institutions); and

   v. the CJEU, which is the supreme arbiter of interpretation of all EU legislation. The CJEU has not always interpreted texts in a predictable manner in accordance with the text before it. It has instead pursued a fairly aggressive single market agenda. For example, the CJEU has not made any positive determinations on the basis of the treaty concept of "subsidiarity", which was designed to push powers back to member states, since that concept was introduced, partly at the behest of the UK, in 1993. By contrast, the CJEU has curtailed laws which were not made in accordance with the treaty concept of proportionality on several occasions. There is no reason for a practical distinction to be made in enforcing these parallel concepts, which exemplifies how the federalist instincts of the CJEU override the requirement to apply the treaty obligations faithfully in accordance with what was agreed to.

c. **Free Movement and Financial Contributions**. The passporting framework within the EU has been associated at an EU level with the EU's "four freedoms", which some in the EU have claimed must operate as a package. In any event, it is likely that access to the passport would entail at some level a continuation of free movement of workers or people, which is politically unsupported in the UK.[12] In addition, it is likely that the EU would require the UK to continue to contribute – perhaps at a level not dissimilar to current contributions – to the EU budget in exchange for continued access to the passport.

"It would be politically unacceptable for the UK to sign up to a framework where it has no voice in drafting, formulating, implementing or enforcing EU legislation, simply for the purposes of maintaining the passport."

It would be politically unacceptable for the UK to sign up to a framework where it has no voice in drafting, formulating, implementing or enforcing EU legislation, simply for the purposes of maintaining the passport. Even with the UK as a member state and having a vote on financial services legislation, this problem was regarded as sufficiently serious that specific safeguards were sought in the February 2016 summit renegotiation.[13] The effect would be that financial markets would be exposed to poorly-

11 EBA, ESMA and EIOPA.

12 See further Shearman & Sterling Client Publication, "*Brexit: Free Movement of Persons*", 5 August 2016.

13 In February 2016, David Cameron engaged in discussions with the European Council to renegotiate the terms of the UK's EU membership. The agreement reached purported to deliver suitable solutions in four areas: competitiveness; economic governance; sovereignty; and social benefits and free movement. David Cameron wanted safeguards to prevent the UK, as a non-Eurozone member state, becoming subject to a closer economic and monetary union. The renegotiation agreement would have given non-Eurozone member states the right unilaterally to invoke safeguards that require the Council to review proposed legislation on the banking union and integration of the Eurozone. However, the renegotiation agreement did not alter the wording on the monetary union. Instead, it added a sentence recognising that financial services regulation is a "single rulebook" aimed at ensuring uniformity across the internal market.

drafted legislation and implementation, driven by EU political whims, which are often less instinctively free-market.

"The UK should neither set out to seek, nor expect to receive, an extensive bilateral deal with the EU, contrary to the suggestions from some commentators."

Minimal Request for Bilateral Deal

The UK should neither set out to seek, nor expect to receive, an extensive bilateral deal with the EU, contrary to the suggestions from some commentators. Any such deal would be undesirable for both the UK and the EU.

From the UK's perspective, any bilateral deal would involve the UK seeking numerous bespoke amendments to the EU legislative framework and access to the single market. In such circumstances, the EU is likely to require significant concessions from the UK, including in relation to sovereignty issues, free movement of persons and budget contributions – which were three of the main issues influencing the referendum outcome. Some or all of the problems associated with continuing with some form of passporting are likely to be insisted upon by the EU as part of any bilateral deal.[14] This would render such an arrangement difficult to support politically, and the lack of flexibility involved in any such structure would preclude the UK from resetting its regulatory framework in a meaningfully beneficial way.

From the EU's perspective, there is determination by some key decision-makers not to allow the UK a smooth path for leaving the EU and not to permit cherry-picking of the EU package. Many politicians in the EU have made clear they are not willing to offer the UK special treatment. They fear such rewards would pave a path to exit for other member states exiting the EU, and would complicate the EU's own bilateral processes with other third countries, such as the on-going negotiations with Canada, and the EU's relationship with Switzerland. Discounting for rhetoric, it is difficult to see how a lengthy proposition seeking to amend the passporting regime or somehow to perpetuate the passport under a new name, solely for the benefit of the UK, would be achievable politically. The UK must recognise the EU's position (for now at least) that membership is a package, and that a "sweetheart" deal would be seen as rewarding the UK for leaving, which is politically unviable. Discussions would immediately revert to the four freedoms, EU institutional oversight and the other difficulties already discussed.[15]

Instead, it is possible to achieve the same position (if not indeed a preferable one) by other routes, as set out in this paper.

[14] The formation of a compromise as regards some of these problems is a conceivable possibility. For example, the UK might be granted some form of representation on the Council or in the EP. These compromises, however, would come at a cost in terms of negotiations and would simply serve to tie the UK closer to the EU, its objectives and its processes, contrary to the referendum outcome. In any event, compromises would only have the effect of diluting, rather than eliminating, the significant negative effects previously discussed.

[15] By way of example, the 1989 EU-Swiss Agreement, although limited to non-life insurance, demonstrates that where EU market access is given to certain non-EEA firms (other than equivalence-based access), the EU has required that such access be subject to some form of free movement of persons, leading to the legal difficulties associated with implementing the 2014 Swiss referendum. The measures around free movement of persons are required, notwithstanding the fact that Swiss access falls short of full passporting as each branch still needs to seek local authorisations in many cases.

"The UK has the expertise and experience to carry out a proper review and reset of its financial regulatory framework."

The UK as a Global Leader

The UK has the expertise and experience to carry out a proper review and reset of its financial regulatory framework. Many EU financial services measures originated from UK thinking or replicated UK legislation. The blueprint for the majority of the regulatory reforms introduced following the 2008 financial crisis is to be found in the UK's Turner Review.[16] Living wills, bail-in and other bank and investment bank resolution concepts originated with the Bank of England. The Market Abuse Directive (later, MAR) and Bank Recovery and Resolution Directive have their origins in UK market abuse offences and the Banking Act respectively.[17]

When the UK becomes autonomous in legislation and rulemaking, this does not mean that it will lose influence on the global stage. For a start, the UK will regain legislative and supervisory control over one of the two main financial centres in the world. In addition, the UK can play a full role in global fora, such as the G20, the Basel Committee and IOSCO, which are increasingly important in agreeing the direction of financial regulation. Financial regulation is now a global concern, and adherence to global standards and best practices is fundamental. The UK's exit from the EU means that global organisations could be given greater relevance in helping to set standards.

Freedom to Trade and Clear in Reserve Currencies

The City has played a pivotal role in the international currency and bond markets since before eurobond markets and electronic trading came into existence. As these markets have developed in size, complexity and scope of instruments, the City has continued to host trading and clearing services to support the markets.

"The European Central Bank does not "own" the euro any more than the Federal Reserve Bank "owns" the US dollar."

Since its introduction in 1999, the euro has established itself as the second most important reserve currency after the US dollar, and is widely used in international trade. The euro area's size, relatively stable governance and openness underpin the international markets' widespread use of euro-denominated financial instruments.

The clearing of a currency is not and cannot be "owned" by the issuer of that currency. The European Central Bank does not "own" the euro any more than the Federal Reserve Bank "owns" the US dollar. A significant amount of trading in US dollars or US dollar denominated instruments has been hosted in the City for decades. Just as there are not, and should not be, any impediments to the trading and clearing of instruments denominated in US dollars outside the territory of the US, so the City should continue to trade and clear euros as a readily-traded reserve currency.

There is no reason of principle or economics as to why the continued usage and clearing of euro-denominated instruments in the UK markets should not continue as it does today. The European Central Bank has no legal powers to prevent global banks and financial institutions from trading and clearing instruments denominated in euros. The UK should

---

[16] The Turner Review, "*A regulatory response to the global banking crisis*", March 2009.

[17] None of these measures required material conceptual amendment to reflect EU standards. However, many have been unnecessarily augmented and embellished at the EU level. Concepts intended and tailored for one sector have been applied more broadly. In addition, measures have been introduced which the UK would most likely not have implemented on its own, such as the AIFMD and most clearly the bonus cap.

strongly resist any request for an agreement voluntarily to cease such trading, which would be unduly protectionist and anti-competitive.

The EU could, however, impose protectionist rules on its own banks, prohibiting them (but not other banks) from trading or clearing euro-denominated instruments outside the Eurozone. This would be a short-sighted protectionist measure if adopted. Indeed, the forced (re)-patriation of euro-denominated instruments would mainly result in harm to EU banks and their customers. EU banks would be deprived of access to more liquid trading and clearing facilities elsewhere, and would be prevented from accessing directly those non-EU facilities supported by global banks and infrastructure. This would increase costs considerably for EU banks and their customers and damage the reputation of the EU and the euro.

If the UK were to give up this business, it would introduce considerable risk (including systemic risk) and uncertainty into the UK markets. The UK should robustly resist any compromises or offers whereby it agrees to cease trading or clearing euros within the City. It is in the interests of both the UK and the EU that trading continue as before. For the City to continue to build on its status as an international financial centre, it must remain a key centre for the trading and clearing of instruments denominated in any globally important currency, including the euro, and must continue to provide for a sophisticated system of cross-margining across currencies.

Additional UK Domestic Reforms: Promoting Competitiveness and Preventing Systemic Risk

Whether the UK proceeds with equivalence-based access to the EU or a Financial Centre model, certain key domestic reforms should be at the forefront of the agenda in the UK.

First, the UK should look to reintroduce considerations relating to the international competitiveness of the UK's financial markets as a statutory objective for all financial services regulators (the Bank of England, PRA and FCA). This was removed as part of the reforms introduced following the 2008 financial crisis, as it was blamed for a "light touch" approach to regulation that had arisen in the UK and which ended up leaving taxpayers with unacceptable exposures to the financial markets. However, it was extreme regulatory arbitrage and even, in the case of certain member states, instances of not applying the rules in accordance with their ordinary meaning at all, that drove the approach down the wrong track. The more modern EU framework, which the UK was instrumental in creating, seeks to prevent such eventualities. The removal of the international competitiveness objective was an error, as rulemaking should always consider competitiveness. This has also led to slower regulatory approval processes and less tested rulemaking. The requirement should be reintroduced as a key factor, subject always to overriding considerations around systemic risk and other regulatory objectives, which protect taxpayers from bail-out risk and the "too-big-to-fail" problem.

Secondly, the UK should separately consider removing the new competition powers of the FCA, leaving competition to be dealt with by the appropriate authority – the UK Competition and Markets Authority – in the traditional way. This would bring competition into line with other developed economies and avoid moral hazard and other issues of regulatory tools and powers being used inappropriately in the antitrust

arena. Competition is best dealt with *ex post* once a mischief has been identified, rather than through *ex ante* rulemaking.

3. UK Open For Business: EU Access to the UK

Following Brexit, the UK government has highlighted the importance of signalling to the world that the UK is "open for business". In the financial services sector, the ability of market participants around the world – from the EU and elsewhere – to access the City and carry out business will continue to be of vital importance. This Part sets out key steps that the UK should take to ensure the continued attractiveness of the City, and to ensure that it is seen as welcoming and attractive to EU financial institutions.

The City's openness to, and accessibility by, EU firms should not be compromised by Brexit. Firms that access the City's wholesale markets remotely from the EU, or who deal with or through firms that are authorised in the UK, should be able to continue to do so in a straightforward manner. In addition, it should be ensured that those who have, or who are planning to establish, a physical presence in the UK do not face new barriers in terms of increased operating costs, the need for case-by-case approvals, or both.

The UK has long had an exemption from the requirement for regulatory authorisation for third-country financial market participants carrying out investment business with institutional clients or counterparties in the UK on a cross-border basis. The "overseas persons exclusion" applies to a broad range of sectors, including exchanges, clearing, settlement, brokerage, derivatives, agency business and advice. This provision allows all non-UK firms – be they EU or non-EU – to access wholesale markets located in the UK and UK customers on a cross-border basis without local regulation.

A related issue requiring consideration is the future status of branches of EU/EEA banks, which currently operate without subsidiarisation or local regulation, on the basis of aligned regulatory standards under European regulation and the EU/EEA passport. Continued access to global financial markets operated in the UK on this basis is likely to be a significant counterbalance to possible EU protectionism in the exit negotiations. It is key to the success of UK financial markets that the regime remains as welcoming as possible. Enabling EU institutions to continue to book and conduct business from their City branches will be an important part of meeting that objective.

The UK Government should avoid creating barriers to cross-border financial services and instead streamline the process for all foreign firms (both EU and non-EU) who access the wholesale markets based in the UK.

The UK could add to the overseas persons exclusion by establishing an "equivalence" regime of its own for branches and cross-border business. This would comprise a list of overseas jurisdictions that meet international regulatory standards and which have regulatory information-sharing and cooperation agreements with UK authorities, allowing any firm authorised and regulated in one of those jurisdictions to do business in the UK with all types of client. Those who establish a branch would need to comply with local UK branch regulatory and conduct requirements. Under the Expanded Equivalence model, this would necessarily include the EU, which could be recognised as equivalent, with the on-going relationship governed by a procedural bilateral deal.

See "Predictability: Tackling Uncertainty through a Procedural Deal" in Part 5.

4. UK Access to the EU

The EU is the UK's closest neighbour, and access to EU customers and markets is, and will continue to be, of great importance to many UK businesses. This Part sets out an analysis of how such access can continue, and how the UK can flourish, from outside the EU.

How Business Crosses Borders

The ability of UK financial institutions to provide services to counterparties and customers in the EU will continue to be one of the UK's policy priorities. There needs to be a three-pronged approach:

a. **Analysing "cross-border" activities**: a careful analysis needs to be conducted of whether activities carried on from the UK are genuinely "cross-border", such that they would require authorisation in an EU member state. In many important cases, such activities are not, or can be made not to be, cross-border, and can therefore be carried on from within the UK without additional local issues arising.

b. **Reverse solicitation exemption**: an appropriate use of the "reverse solicitation" exemption should be made, by which financial institutions operating in the UK can transact business with EU customers who wish to access their services, subject to the provisions of the exemption.

c. **Third-country equivalence**: access based on existing (and forthcoming) third-country equivalence regimes should be considered, whereby UK financial institutions can deal cross-border into the EU markets without a local member state licence following a determination by the EU that the UK is "equivalent" under the relevant legal regimes.

Analysing "Cross-Border" Activities: A Closer Look

"On a careful analysis, much activity in the financial sector in the City is actually not cross-border at all, or can easily be modified so as not to be."

In recent years, a broad view of what constitutes a "cross-border" activity has been adopted by lawyers in practice, given the relative ease in terms of cost and process of engaging with the passporting process.

European guidance states that the "location" of a service is determined by reference to the "characteristic performance" of that service.[18] This refers to the place where the essential supply of the services for which payment is due. On a careful analysis, much activity in the financial sector in the City is actually not cross-border at all, or can easily be modified so as not to be. Important activities that are not traditionally regarded as being cross-border include:

a. **deposit-taking**. Deposits are generally regarded as taken at the location of the branch where a bank's books and records are located.[19] In itself, taking deposits and recording them in a UK corporate bank's City-based books would not constitute a cross-border activity;

---

18 Commission Interpretative Communication: Freedom to Provide Services and the Interest of the General Good in the Second Banking Directive, 20 June 1997. The European Commission's view for the purposes of the Investment Services Directive (the precursor to MiFID) was that the activity occurred wherever the "characteristic performance" of the activity took place. This view was adopted by the Financial Services Authority (the precursor to the FCA). However, the FCA notes that this view is not shared by all other EEA states (SUP App 3 3.3.8G).

19 This is the view historically taken by the UK and it is in conformity with the characteristic performance test. Some EU member states take the view that licencing can be required where the business is solicited. In practice, the UK's characterisation is unlikely to be challenged by a bank's customers. The more restrictive interpretations are subject to challenge under the characteristic performance test, and so their implications – both legal and practical – are unclear.

b. **online banking**. The provision of online banking services, including online deposit-taking, would take place at the branch where the bank's books and records are located and so would not constitute a cross-border activity for a UK-based entity;

c. **payment services**. Payment services, such as placement of cash on payment accounts located in the UK and the issuance of payment instruments or merchant acquiring for UK customers are similar in nature to deposit-taking and so would not constitute cross-border activities; and

d. **portfolio management**. The decision-making processes associated with portfolio management services take place where investment decisions occur and transactions are done, so these are not in principle cross-border, and the implementation of such decisions through a London-based prime broker acting as principal should not be either.

Overall, it will be important to undertake an analysis of whether activities are truly "cross-border" or are really domestic. In the latter case, requirements for equivalence simply do not arise, as the relevant activity in the City would fall within the sole remit of the UK.

Reverse Solicitation Exemptions

"Reverse solicitation" is a concept underpinning a common exemption from the requirement to be locally-licensed in many financial services regimes. Under reverse solicitation exemptions, financial institutions are permitted to provide cross-border financial services to a client, without being registered or authorised in that client's member state, provided that the services are provided on the initiative of the client. The formulation of the exemption varies depending on the legislation and country, but the most recent iteration at the European level – in MiFID II – is typical of current formulations: "where a retail or professional client… initiates at its own exclusive initiative the provision of an investment service… the requirement for authorisation… shall not apply."[20]

The details of the operation of the exemption are subject to local interpretation by each member state. In most member states, reliance on the exemption generally involves: (a) the client requesting the services on its own initiative; (b) restrictions or prohibitions on firms soliciting or advertising to such clients; and (c) the services offered being within the scope of the client's request. Additional restrictions on permanent physical presence in the jurisdictions may also be involved. In some cases (but not in the case of AIFMD for fund managers), it is possible for a client of a firm to make a more general request for information regarding services that the firm offers, perhaps in signing up to the firm's terms of business, effectively expanding the scope of the exemption.

The UK has long had a permissive view of the scope of the exemption for most incoming business activity. The exemption is reflected in the "overseas persons exclusion", whereby persons who do not carry on a regulated activity (or offer to do so) from a permanent place of business in the UK are excluded from some of the requirements for authorisation where, in essence, they comply with the UK's financial promotions restrictions.[21]

Third-Country Equivalence

Where activities are cross-border, and the reverse solicitation exemption is inapplicable, access to the single market will be available pursuant to

[20] Article 42, MiFID II.

[21] Article 72(7), Financial Services and Markets Act 2000 (Regulated Activities) Order 2001.

Votes held by **QMV** must be passed by representatives from a special majority of member states (usually 15 member states), representing a special majority of the total population of the EU (usually 65%).

current (and forthcoming) third-country equivalence regimes. As currently formulated, and assuming the EU adopts a fair and objective approach to an assessment of the UK's application to be deemed "equivalent", a significant proportion of the City's financial services in the EU could continue in their current delivery mechanisms without disruption.

"Equivalence" is not a single route to the single market; rather it is a patchwork of measures across various sectors, some of which are more wide-ranging than others. Third-country equivalence access provisions are already in place in many sectors, but it must be acknowledged that there are currently certain gaps.[22]

Addressing the gaps: the options

Third-country equivalence regimes are a relatively new concept in EU law. There are therefore certain areas in which such a regime has not yet been developed and access based on third-country equivalence is not currently available. In the case of these "gaps", two routes are open to the UK:

a. under an "Expanded Equivalence" model, these gaps would simply be filled. This could be done by amending existing legislation (which the UK could vote on both in the Council, which would vote by QMV, and in the EP, which would require a majority vote) and ensuring that future legislation provides for such third-country equivalence access for all third countries. Alternatively, and more ambitiously, this could be achieved by providing a framework for a general right of access to the single market on a third-country equivalence basis. This Expanded Equivalence model is set out in Part 5 ("Expanded Equivalence Model"); or

b. under a "Financial Centre" model, the gaps would not be filled and – in those areas where existing third-country equivalence regimes are insufficient – the UK would simply leverage its attractive, tailored regulatory framework and financial clout to drive business and liquidity to the UK, operating as an entirely free-market financial centre. This Financial Centre model is set out in Part 6 ("Financial Centre Model").

"Under either model, the UK should carefully consider, sector-by-sector, whether such a trade-off is worth it and equivalence is worth pursuing."

Obtaining an equivalence determination necessarily involves a trade-off of some flexibility. Under either model, the UK should carefully consider, sector-by-sector, the value of such a trade-off and whether equivalence is worth pursuing.

This may become particularly relevant in the context of any future EU measures that turn out to be protectionist, as equivalence necessarily involves some alignment of rules to the EU's requirements, and so (to a lesser or greater extent) some loss of flexibility. It may even be the case that, for some existing areas of law, it would be better for the UK to allow counterparties and customers to come to the UK to do business through local presences, and not to seek equivalence on those topics at all.

22 An analysis of the coverage of equivalence-based access under current regimes is highly technical. See Annexes A and B for detailed analysis.

5. Expanded Equivalence Model

Comprehensive access to the single market on a third-country basis is possible. In many sectors, the framework for such "equivalence"-based access is already in place. This Part describes how such access would operate in practice, sets out the steps that would be required to fill the gaps in existing legislation, and explores the potential advantages of doing so.

Equivalence in Practice: How it Operates

Many financial services directives and regulations provide for third country institutions to achieve recognition for EU law purposes if they have "equivalent" laws and regulations in the relevant areas. Requiring "equivalent" laws is not the same as requiring "identical" laws. Equivalence-based access allows for a certain amount of flexibility; it preserves third-country sovereignty; it does not bring with it EU institutions or "freedoms"; but it nevertheless permits full cross-border access to EU counterparties and customers in the relevant sector of the market. Many third-country institutions deal with EU counterparties and customers on this basis. The UK is well-positioned, in light of time-zones and market structure issues, to leverage an equivalence regime in ways that others have been unable to do thus far.

Equivalence requirements vary for EU market access across different sectors. However, a number of commonly imposed requirements have emerged for the recognition of third country regulatory regimes.

Equivalence determination. The country in question must be deemed to have a legal system and, sometimes, a supervision regime that is "equivalent" to the EU regime. That determination generally[23] involves the relevant ESA providing technical advice to the European Commission on how the third country's laws and regulations compare to the corresponding EU requirements and then a decision by the Commission, which takes into account political elements. An equivalence determination by the European Commission may be conditional rather than full, meaning that certain EU legislative provisions will only be disapplied for the specific area determined to be equivalent. Furthermore, temporary equivalence decisions are possible where progress is being made towards equivalence.

One question is how identical a third country's legal and regulatory regime needs to be to that of the relevant EU regime for equivalence to be forthcoming. The test to be applied for equivalence varies under the different regimes. For example, the European Commission has stated that the equivalence process "involves identifying any differences between our respective legal and supervisory arrangements and assessing whether similar regulatory outcomes are nonetheless achieved; namely the reduction of systemic risk in the financial markets."[24] Similarly, the recitals to MiFIR state that an "equivalence assessment should be outcome-based; it should assess to what extent the respective third-country regulatory and supervisory framework

[23] The process, legal tests and parties involved vary slightly amongst the various equivalence regimes.

[24] Letter from Michel Barnier, European Commissioner, to Ashley Alder, Chairman of the IOSCO Asia Pacific Regional Committee, 20 December 2013.

achieves similar and adequate regulatory effects and to what extent it meets the same objectives as Union law."[25]

Given that the UK's current regulatory regime is based on EU rules, and given that EU laws will generally be grandfathered upon Brexit, it seems likely that there will be few obstacles to equivalence determinations immediately upon Brexit. If changes are later made to (former) EU laws in the UK (and, it is suggested, they should be), then the UK would be required to show that the relevant tests and key outcomes are nevertheless still achieved.

Co-operation agreements. UK regulators may need to enter into co-operation agreements with either the relevant national regulator of a member state or with the relevant ESA, depending on the sector. Such agreements provide for the exchange of information and methods for co-operation and communication. In recent years, co-operation agreements have become more commonplace worldwide. These agreements are the basis for increased co-operation between regulators in the supervision of financial institutions as well as in enforcement actions against those falling short of the standards. Greater regulatory cooperation was mandated by the post-crisis G20 Pittsburgh Commitments. Given that the UK and EU regulators already work closely together to monitor and prevent systemic risk, it seems inconceivable that these relationships would be unwound.

Reciprocity. Some of the equivalence regimes are premised on the existence of reciprocal arrangements, allowing EU access to UK markets on similar terms to UK access to the EU. This would, of course, benefit both the EU and the UK, and should be welcomed.

De-politicisation

Brexit is, by any standards, one of the most significant recent developments in European history. The negotiations and the basis for the future EU-UK relationship will have serious ramifications for all parties. Many competing interests are at stake. For the Expanded Equivalence model to work, some of the political "heat" must be taken out of the equation, both in the short- and long-term. Such a need arises in three important areas:

a. the process of expanding the existing equivalence regimes. This will involve the usual EU legislative process (see "Legislative Process" below);

b. the process of assessing the UK's legal framework immediately on Brexit and adopting equivalence determinations with respect to the UK in each of the various sectors;[26] and

c. the process of ensuring predictability for both the EU and the UK by adopting a robust procedural agreement as regards the EU-UK relationship going forwards (see "Predictability: Tackling Uncertainty through a Procedural Deal" below).

In what might be expected to be somewhat fraught negotiations, calm heads must prevail for the Expanded Equivalence model to be viable.

---

[25] Recital 41, MiFIR.

[26] The equivalence process in each sector generally involves the European Commission accepting the advice of the European Securities Committee. The European Securities Committee is composed of high level representatives from the member states and is chaired by a representative of the European Commission. The assessment by the European Securities Committee is a technical legal exercise. The decision by the European Commission as to whether to adopt an equivalence determination injects a political element.

Retribution or politicised "interpretations" on either side will undermine what ought to be a technical legal process.

Mutual Desirability

The expansion of existing equivalence regimes would open the EU's markets to investment from around the world, promote trade, decrease costs and ultimately make the EU a more attractive place to do business. It would also result in greater consistency of EU legislation with that in the UK. This should be of clear economic advantage to the EU. Access to well-priced capital will become all the more important for the EU following Brexit, given that the UK will become a "third country". Filling in the existing gaps in the equivalence framework should therefore be seen as a priority from the EU's perspective. Brexit would simply serve as a catalyst for this logical expansion.

CRD implements the key Basel III reforms on regulatory capital, stating how much capital EU Credit Institutions and EU Investment Firms must hold. It also introduces non-Basel III reforms such as the bonus cap and provides a passport regime for EU Credit Institutions.

The Expanded Equivalence model is likely to be a mutually reciprocal arrangement, whereby the UK also provides access to the EU, including for branches in the UK of EU Credit Institutions and EU Investment Firms. This is important from the EU's perspective, as there are five times as many EU banks exercising passport rights to provide services in the UK as there are UK banks providing services in other EU jurisdictions under the CRD passport.[27] The cost implications of requiring EU Credit Institutions and EU Investment Firms to operate through UK subsidiaries rather than branches would be significant. An outcome based on mutual recognition would be welcome for the UK.

Legislative Process

The process for plugging the gaps in the existing equivalence regimes could be achieved either by piecemeal amendment of existing EU legislation, or (more ambitiously) by the introduction of a general right to access based on third-country equivalence across the board. In either case, this would be achieved through the normal EU legislative process.[28] The process would involve the European Commission submitting a legislative proposal to the EP and the Council, the adoption of a position by the EP at the first reading, and then the adoption by the Council, voting by QMV.

The addition of equivalence to existing financial services directives and regulations should be achievable in short order and could take place outside the context of the Brexit negotiations. Whether achieved by the piecemeal filling in of the various gaps,[29] or a more comprehensive equivalence regime,[30] the UK can and should be proactive in proposing the necessary legislation and guiding it through the EU legislative track. As the UK will continue to be a member of the EU until Brexit takes effect, there is nothing to preclude it from taking a lead in this regard, and

[27] FCA letter to Andrew Tyrie, 17 August 2016.

[28] Article 294, TFEU.

[29] A full analysis of the gaps in existing regimes is set out in Annexes A and B.

[30] On this model, a framework Regulation would provide for third-country access in all sectors of the single market. A "menu" of sectors for equivalence would therefore be available. Third countries and their institutions would apply for access on a sector-by-sector basis according to standard criteria for determining equivalence standards.

taking an active part in the legislative process required to implement those measures – including by voting in the EP and Council.[31]

It is to be hoped and expected that most of the EU states would see the economic benefits to themselves in adopting such an approach, and that the business lobbies in those states would assist the EP members in their understanding of the benefits. Such an approach would not prejudge any equivalence decision for particular parts of the financial sector in the UK (which would be a decision to be made separately by the EU as part of the Brexit negotiations). It would merely ensure that the EU markets have access, in principle, to third-country financial services and products where there is proper regulation in the third country under a similar regime.

Predictability: Tackling Uncertainty through a Procedural Deal

"The EU-UK relationship is an important one for historical, geographical, political and cultural reasons, and it is perfectly reasonable to take steps to ensure the continuation of good relations between the two jurisdictions."

The move from access based on passporting to access based on equivalence will not only present significant issues for financial institutions from a legal structuring perspective, but it will involve a shift in thinking. Some have objected that equivalence brings with it a certain amount of uncertainty since a determination of equivalence can be withdrawn.

The EU-UK relationship is an important one for historical, geographical, political and cultural reasons, and it is perfectly reasonable to take steps to ensure the continuation of good relations between the two jurisdictions. Considerable predictability for both the EU and the UK could be injected into the Expanded Equivalence model if there were to be a bilateral deal on process and procedure. Such an agreement would be separate from the expanded substantive rules, which would apply to all third countries, and would instead be a direct, bilateral agreement between the EU and the UK. This agreement could be concluded as part of the Article 50 settlement,[32] and could cover the following:

- a commitment to include third-country equivalence regimes in all future financial services legislation in the UK and EU;
- a commitment to de-politicise equivalence determinations with respect to the UK and EU, both at the time of Brexit and going forwards;
- modification of dispute resolution requirements in third-country equivalence regimes, such that decisions of UK courts and tribunals are recognised and enforceable in the EU, and *vice versa*;
- the creation of a standing working group between the UK and EU for discussing new legislative measures, reforms, reductions and removals in

[31] House of Commons Briefing Paper Number 7551, "*Brexit: how does the Article 50 process work?*", 30 June 2016, section 3.3.

[32] Article 50, TFEU authorises the conclusion of "an agreement with that State, setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union". That agreement would be concluded by QMV, for which purposes the UK would not be included, and 20 out of the remaining 27 member states would need to vote in favour. However, if the nature of the agreement is sufficiently complex, it might constitute an "association agreement" for the purposes of Article 218(8), TFEU, in which case unanimity would be required. In addition, if the agreement covers matters outside the EU's powers, it would have to be in the form of a "mixed agreement" to which the member states are parties in their own right. In such a case, the Member States will need to sign and ratify the agreement according to their own constitutional requirements, such as for the Comprehensive Economic and Trade Agreement with Canada. It should be possible, however, to structure the agreement so as to avoid it constituting either an association agreement or a mixed agreement, and so as to fall within the QMV process.

equivalence matters, with the ability to make referrals to an independent body or trade panel to determine disputes as to whether equivalence requirements have been breached;

- the introduction of significant notice periods whereby the EU gives the UK, and the UK gives the EU, advance notice with respect to any proposals to extend, withdraw, condition or amend recognition of equivalence;
- a commitment not to impose any other barriers on financial services business conducted cross-border between the UK and EU;
- a commitment by the UK to work to ensure that EU financial institution branches in the City can continue to operate; and a corresponding commitment by the EU to similar effect. In the UK context, this would require a modification of the PRA's current "subsidiarisation" policy for systemically-risky third-country branches; and
- an agreement as to how to treat branches of UK institutions in the EU and of EU institutions in the UK under some fast-track process, where the delineation between home and host state regulation is also agreed.

Other matters could be discussed as part of this agreement. Crucially, however, the agreement would only pertain to process and procedural matters, so as to avoid encroaching on the "four freedoms".

Opportunity to Rationalise UK Laws

Expanded Equivalence will give the UK an opportunity to review its laws and remove certain categories of problematic legislation. Laws that should not be replicated in the UK, and whose absence should not affect an equivalence determination, include:

- **rules and regulations which have been found, in equivalence determinations with respect to other jurisdictions, not to be necessary for equivalence purposes**. There are various examples of EU requirements which are not replicated in jurisdictions that have already been deemed equivalent under various equivalence regimes. Such requirements are therefore unnecessary for equivalence purposes and, if undesirable, need not be replicated in the UK.
- **rules implemented for the purposes of furthering the EU's "single market" ideal**, such as the market structure rules in MiFID II/MiFIR, and potentially much of MiFID II/MiFIR more generally. These reflect *a priori* understandings at an EU level of a cross-border ideal, which will no longer be relevant to the UK post-Brexit. For example, one of the driving factors behind the introduction of MiFID in 2004 was to harmonise conditions governing the operation of markets across the EU to allow the seamless capital flow of euros. MiFID II (including MiFIR) seeks to address shortcomings and unintended consequences in MiFID and its market structure provisions are founded on an intent to further the single market. Following Brexit, eliminating barriers to allow the cross-border intra-EU flow of business is no longer an issue for the UK. (It should be noted that some rules introduced ostensibly for "competition" reasons are actually, properly analysed, single market rules).
- **competition-based rules**. These should be a matter for UK domestic sovereignty, and should be subject to a UK-centric approach. See also, "Additional UK Domestic Reforms: Promoting Competitiveness and Preventing Systemic Risk" in Part 2.
- **rules which are duplicative and impose redundant process requirements**, such as dual-reporting of derivatives to trade repositories by both sides of a trade and of exchange-traded instruments under EMIR.
- **aspects of social policy** which are not truly financial regulatory matters, such as the bonus cap.
- **laws that create new processes or costs, or which are prohibitive and overly-prescriptive, but which do not promote practical systemic risk-based or other outcomes**, such as cumbersome fund manager rules under

the AIFMD, the costly requirements to establish new processes for "indirect clearing" which are widely acknowledged (even by ESMA) not to deliver any material benefits to end-customers on an insolvency, and commodity market position limits, which are not founded on a proper analysis of the evidence.

How to Proceed: A Step-by-Step Practical Approach

The UK should conduct a rigorous analysis of existing EU laws as a priority. Such analysis should proceed, with respect to each sector, as follows:

Step 1. Identify whether a third-country equivalence regime currently exists.

Step 2. Determine whether equivalence is required, or whether – properly analysed – the activity might not be cross-border.

Step 3. Determine whether seeking an equivalence determination is worth pursuing.

Step 4. If equivalence is desirable, but no regime currently exists, "plug the gap".

Step 5. Identify the UK rules which could be eliminated while maintaining equivalence (where desired).

An Appropriate Compromise

Under the Expanded Equivalence model, the UK would adopt (or continue with) measures equivalent to large portions of the EU's regulatory framework for the purposes of maintaining equivalence. On the day of Brexit, for reasons of time, this would involve maintaining the EU drafting and wordings on many topics, including those which have often created uncertainty and unpredictability.

The UK can then begin carefully engaging in the process of rationalising its laws. Importantly, under the Expanded Equivalence model, if properly managed, the financial services sector in the UK will at no stage be in a worse position compared to passporting under the current arrangements (while a member of the EU). In addition, having removed the most burdensome regulatory requirements, the UK will no longer be subject to some of the EU's ill-thought-out rules, and so has the opportunity to be in a better position than under current arrangements.

"…businesses in the UK and EU should feel little impact except, over time, the benefits of the better, more targeted and less burdensome regulatory framework in the UK."

The Expanded Equivalence model is premised on a comprehensive use of equivalence-based access in all sectors where the UK deems such access necessary. The practical effects of moving to this model (from the current passporting arrangements) should, properly managed, be nil, and businesses in the UK and EU should feel little impact except, over time, the benefits of the better, more targeted and less burdensome regulatory framework in the UK. In order for this approach to work, however, the EU must determine the UK equivalent in all relevant sectors, and must not withdraw that determination. The UK must also provide access for EU institutions.

Although equivalence-based access is a promising model, it must not be pursued by the UK at any cost. In order to maintain its equivalence, the UK will not have as free a hand as under the Financial Centre model. The Expanded Equivalence model is something of a compromise. The UK will be able to remove burdensome aspects of EU law that other equivalent countries do not adopt, but many of its laws are likely to need

to be recognisably similar to EU requirements, even (in some instances) when those requirements exceed G20 standards or are not as free-markets based as some UK market participants might like. This will limit the freedom and flexibility of the UK to re-think its rules in a more profound manner.

The key question will be how the detailed judgement on determining equivalence is applied. Unless sufficient repatriation of rulemaking is achieved, equivalence would be just as unacceptable as it would be for the UK to become a rule-taker in order to maintain the passport. The UK must enter these negotiations on the basis that, at the very least, it would be looking not to replicate those measures previously discussed (see "Opportunity to Rationalise UK Laws"), all of which should – provided the UK is treated fairly in the negotiations – be unproblematic from an equivalence perspective. Further, the UK would need the freedom to move to a more common law-based approach to legislation, rules and case law across the board.

Detailed Analysis

Annexes A and B consider where there are currently third-country equivalence regimes already in existence for key sector specific pieces of European legislation with effect in the UK. They address equivalence only from an EU perspective. In many cases, additional access could be implemented by EU institutions, counterparties and customers operating through UK affiliates to access the UK's markets.

Annex A sets out and comments upon sectors with existing equivalence regimes where the UK could expect to obtain equivalence.	**Annex B** sets out and comments upon sectors where there are no existing third-country access provisions.	**Annex C** sets out a summary of the equivalence decisions adopted so far under the relevant pieces of European legislation.

6. Financial Centre Model

In the event that a sensible, proportionate, and mutually-beneficial agreement on Expanded Equivalence cannot be reached, there is an alternative path for the UK, which is more radical and entirely within its control, and which has its own particular benefits. This Part sets out the Financial Centre model, whereby the UK – with a free hand – designs its own financial regulatory system, with a view to maintaining and enhancing its status as a truly global financial centre.

Financial Centre Model: Overview

"Unburdened from the shackles of European social policy, the Financial Centre model would enable the UK to re-think its regulatory framework entirely and to move to better, more targeted regulation."

The Financial Centre model is based on the adoption of a far more free market approach, where neither passporting nor equivalence are considerations. Unburdened from the shackles of European social policy, the Financial Centre model would enable the UK to re-think its regulatory framework entirely and to move to better, more targeted regulation. This approach is not entirely new. In some ways, it winds the clock back to the situation before the passport came in partially in 1995 and more fully in 2007.

Before passporting was introduced in its most basic form in the mid-1990s, counterparties and customers generally chose to come to the UK for business. They dealt through UK subsidiaries, branches, representative offices and by flying into the UK for meetings or on projects. They did so because of the attractiveness of the UK's financial markets, the cleanliness of those markets and the UK's sensible approach to law and regulation. There is much to be said for such a set-up. The UK legislators and regulators would have full control. They can operate entirely under common law thinking, with all the clarity that brings. The UK can create a system that frees itself from the excessive EU regulation, much of which has dampened the economy or increased costs, with no clear benefit to systemic risk or consumer protection objectives.

Opportunity for a Comprehensive Re-Think

There has been an uneasy marriage between the UK's common law-based system for the financial markets, with its associated pragmatism, and the EU's purposive, social policy-based approach to rulemaking.

EU financial services legislation often contains powers for the Commission to adopt so-called "Level 2" measures. These tend to deal with technical matters which require the expertise of supervisory experts.

The EU reforms introduced following the 2008 financial crisis have been highly prescriptive, with extensive Level 2 measures spelling out how businesses must be run in inordinate detail. More importantly, however, the EU approach to rule-making, implementation and interpretation imposes far more of a blanket of regulation on activity than the UK's traditional approach. In many cases, the rules provide for ill-defined outcomes, which then require extensive compliance processes to be introduced without much-needed clarity as to the true requirements.

Many of the EU's measures have their basis in UK law but were then extended and embellished in ways the UK would not have done. Brexit brings an opportunity for the UK to do something more radical, which is to re-think the regulatory framework entirely. This would include the following:

- re-drafting all laws and regulations in common-law style, where words on the page are interpreted in accordance with their natural meaning;

- stripping back unnecessarily detailed prescription and process, focussing instead on outcomes and identified risks, with intelligent oversight and compliance;
- a careful re-focus on safety, soundness, market conduct and consumer protection, which would result in many laws being pared back and some being bolstered – "better" or "smarter" regulation rather than the current, less focussed model, which has grown up by haphazard accretion;
- removal of all single markets laws and regulations; and
- removal of antitrust-based laws and regulations and the removal of antitrust from the remit of the financial services regulators, on the basis rule-making should not be based on perceived competition anomalies, but instead competition law should be applied by the UK Competition and Markets Authority after an anomaly has been identified.

This would not, properly executed, bring with it new risk and is not a proposal for deregulation to deviate from international standards. This model should in fact enable the UK to reassert full control over the risks of the financial markets and establish a better legal and regulatory framework for the City.

"A highly responsive, focussed regime could be swiftly created, re-calibrating much of the committee-based legislation and regulation that has proven unduly damaging to the financial markets."

Global standards must, of course, be a touchstone. The UK would reinvigorate its participation in global standard-setting bodies and would allow itself more nimbly to implement laws and regulations that address the true risks and are aligned with regulatory oversight. That oversight and legislative responsiveness would remain close to the financial markets by being based in London. A highly responsive, focussed regime could be swiftly created, re-calibrating much of the committee-based legislation and regulation that has proven unduly damaging to the financial markets.

Precedent: the World's Oldest "New" Financial Centre where Counterparties and Customers Come to the City

EU counterparties and customers in the wholesale markets are generally already established in a manner that would permit them to access the financial markets under the Financial Centre model. It was not long ago that counterparties and customers came to the market rather than the other way around. EU corporates can access the UK's markets through UK affiliates. Further, under existing EU member state laws, some level of cross-border business will still be possible. In particular:

- under local EU member state laws, many cross-border dealings, including multiple on-the-ground visits, can be conducted without branches being established in the EU or local licences being required;
- UK firms will generally be able, under the reverse solicitation concept, to carry out investment services upon the initiative of the client;
- further local law analysis will no doubt reveal additional workarounds;
- UK institutions could also resort to local subsidiarisation or obtaining local licenses for EU retail customer access or truly cross-border marketing and possibly trading that needs on a proper legal analysis to be subject to local regulation.

There will in some instances be some additional costs involved in back-to-back trades conducted with UK affiliates which are then reflected in back-to-back transactions with the EU counterparty or customer's head office within the EU. In the context of OTC derivatives, EU Credit Institutions and EU Investment Firms would not benefit from the intragroup exemption from clearing and margining requirements under EMIR for trades entered into between UK entities and EU affiliates.

There may also be additional costs for insurers using reinsurance from EU subsidiaries by way of back-to-back reinsurance without equivalence, although it may be possible to establish more cost-free structures when the EU corporate purchases group or other insurance through its UK affiliate.

In the retail context, the market would need to consider further the online provision of services and how they are characterised. Retail services provided to the UK's high standards of consumer protection and supervised in the UK would only be of benefit to EU consumers. If the EU wishes its consumers to access those services through local EU branch infrastructure, this could of course be established. It is important to remember that, currently, retail services are not meaningfully and freely cross-border within the EU due to the number of barriers that arise and local laws that supervene, despite the notional existence of the passport.

The UK-EU Relationship: Attracting Business to the UK

"…banks and financial institutions would be drawn from the EU to the UK as an attractive jurisdiction for business."

The development of a market-friendly, tailored regulatory framework in the UK – coupled with the avoidance of any discussion of purely political measures, such as the misguided financial transactions tax – would represent a significant attraction.

The main beneficiary of the Financial Centre model would, of course, be the City itself and the UK economy, as banks and financial institutions would be drawn from the EU to the UK as an attractive jurisdiction for business. The incentive, rather than moving business to the EU, would be for banks to continue to be established in the UK, and to have their most significant customers come to the City to transact business. Some calculations suggest that the City, under a Financial Centre model, could even expand by around 10 per cent. compared with the current position.[33] The mechanism by which such business would move, and the model under which it would operate most efficiently, is likely to vary from sector to sector. See Part 7 ("The Implications for the UK's Financial Businesses – Case Studies") for some examples of how such a move might play out in various key industries.

The UK should facilitate the establishment by EU entities of UK affiliates and the receipt of services through those affiliates, for example by structuring the UK's tax laws so as to permit a clear pass-through of funds, allowing business that currently is cross-border to be conducted through UK conduits of EU counterparties and customers. Those conduits could receive loans, engage in trading, receive insurance and so on.

The EU, in such circumstances, might "close ranks", and take protectionist steps in an attempt to sure up its own interests. Such a protectionist response by the EU to the renewed attractiveness of the UK would in fact be counterproductive for the EU, and would simply serve to highlight the appeal of the UK's free-market response. EU protectionism would not damage the City once long-term market responses are taken into account. In fact, it would primarily serve to disadvantage the EU's own financial institutions and, ultimately, its own citizens.

[33] See Minford, P, "*Flawed Forecast, The Treasury, the EU and Britain's future*", Politeia, 8 June 2016.

The Need for a Clear Choice

It is to be expected that the EU will wish to pursue an Expanded Equivalence model. However, if that is not the case or if Expanded Equivalence, on a detailed practical analysis, is less attractive, the UK should instead introduce a Financial Centre model. The Expanded Equivalence model is not necessarily preferable. Its attractiveness depends in large part on the level of equivalence required. The sooner the UK maps out its legislative and regulatory framework under the Financial Centre model, and the shape of its laws under Expanded Equivalence, the sooner it will be possible to weigh up more appropriately the benefits and drawbacks of each.

7. The Implications for the UK's Financial Businesses: Case Studies

This Part contains an exploration of the possible effects of Brexit on various common business models. In each case, the following are covered: (a) the current regulatory framework; (b) the activities that could be carried out without any equivalence determinations (i.e. on a Financial Centre model); (c) the activities that could be carried out under existing equivalence regimes; and (d) the activities that would require additional equivalence regimes to be introduced (i.e. the Expanded Equivalence model).

Case Study 1: Corporate and Investment Banking

Current Regulatory Framework

UK-regulated corporate and investment banks currently carry out a number of CRD Activities and MiFID Activities relating to investment banking with clients based in the City and across Europe under passports derived from the CRD and MiFID (the future MiFID II/MiFIR) regimes.

Post-Brexit Regulatory Framework – Financial Centre Model

Post-Brexit, UK corporate and investment banks could continue to carry on a number of activities with entities in the EU without any equivalence-based access, as follows:

a. deposit-taking, most payment services, the provision of many guarantees, and any other activities which are not cross-border in law, will be able to continue (see "Analysing "Cross-Border" Activities: A Closer Look" in Part 4);

b. investment advice relating to mergers and acquisitions (i.e. corporate finance advice) is merely an "ancillary service" under MiFID (and MiFID II), and therefore does not necessarily require local authorisation of itself in all EU countries.[34] It should be noted that generic advice and the provision of general information would not amount to the regulated activity of giving "investment advice";

c. UK corporate banks' lending activities could be re-structured as sub-participations, bond issuances or purchases of drawn loans from outside the EU; and

d. the "reverse solicitation" exemption is likely to provide a useful route for many activities of a UK investment or corporate bank, which could establish an EU subsidiary for marketing only, and then introduce the UK entity under reverse solicitation.

UK corporate and investment banks could also have counterparties and customers acquire those services which are truly cross-border through UK affiliates. The UK's tax laws would need then to permit the upstreaming of monies borrowed and so on to the EU group on a tax efficient basis. Alternatively, firms could establish an EEA-authorised branch to provide other CRD Activities.

Post-Brexit Regulatory Framework – Existing Equivalence Regimes

As regards other activities, UK institutions (including banks) will be able to carry on investment business activities that constitute MiFID Activities on a third-country basis under the MiFID II third-country equivalence

[34] The scope of what constitutes corporate finance advice is reasonably wide, and includes all circumstances where the primary purpose of the advice is "industrial, strategic or entrepreneurial". Committee of European Securities Regulators, "*Understanding the definition of advice under MiFID*", CESR/10-293, 19 April 2010.

regime, assuming there has been an equivalence decision.[35] This would include the provision of wholesale investment services cross-border to professional clients and eligible counterparties.

However, UK corporate and investment banks will lose their ability to carry out cross-border CRD Activities that do not amount to investment business under MiFID II/MiFIR, as there is currently no third-country equivalence regime in the CRD.

Post-Brexit Regulatory Framework – Expanded Equivalence Model

The introduction of a third-country equivalence regime in the CRD would ensure that UK corporate and investment banks would be able to continue to carry out all cross-border activities without adjustment to current delivery techniques.

Case Study 2: Retail Banking/Private Wealth Management

Current Regulatory Framework

UK financial institutions are currently able to provide retail banking and private wealth management services (such as deposit-taking, payment services, mortgage-lending, consumer credit and portfolio management) in other EU jurisdictions under the CRD, or to some extent MiFID, passports.

Post-Brexit Regulatory Framework – Financial Centre Model

Post-Brexit, UK retail banks could continue to carry on a number of activities with entities in the EU without any equivalence-based access, as follows:

a. portfolio management, deposit-taking, most payment services, the provision of many guarantees, and any other activities which are not cross-border as a legal matter, should be able broadly to continue (see "Analysing "Cross-Border" Activities: A Closer Look" in Part 4); and

b. the "reverse solicitation" exemption is likely to provide a useful route for many activities of a UK retail bank, which could establish an EU subsidiary for marketing only, and then introduce the UK entity under reverse solicitation.

Mortgage lending and consumer credit provided in respect of EU-domiciled clients are more straightforwardly cross-border services. However in these cases the absence of harmonisation of EU consumer credit law makes use of the passport more difficult in the first place, as firms are required to tailor their service to the regulatory requirements of the host member state. Firms should therefore consider whether the existence of passport rights in this instance, when compared with local branch authorisation, is material.

UK retail banks could also provide CRD Activities and MiFID Activities through high net worth clients establishing UK tax transparent corporate entities. Alternatively, firms could establish an EEA-authorised branch in the way that many US banks currently do.

[35] Third-Country Credit Institutions will be able to benefit from the same third-country equivalence provisions in relation to their investment business activities as Third-Country Investment Firms, under MiFID II (Article 34(1), MiFID II).

Post-Brexit Regulatory Framework – Existing Equivalence Regimes

UK retail banks will be able to carry on providing services which are MiFID Activities to professional clients and eligible counterparties under the existing equivalence regime in MiFID II/MiFIR, assuming there has been an equivalence decision. However, UK retail banks will lose their ability to carry out MiFID Activities to retail clients or elective professional clients. They will also lose their ability to carry out some of the (non-investment business) passported CRD Activities across the EEA, as there is currently no third-country equivalence regime in the CRD. However, the implications of these points are more limited than might first appear.

Post-Brexit Regulatory Framework – Expanded Equivalence Model

The introduction of (1) a third-country equivalence scheme under CRD, and (2) an expansion of the MiFID II/MiFIR third-country equivalence scheme to retail clients, would ensure that UK corporate and investment banks would be able to continue to carry out all cross-border activities without adjustment to delivery techniques. This would clearly be beneficial to both the UK and EU.

Case Study 3: Fund Management (Retail Funds)

UCITS regulates retail funds. It sets out requirements on regulatory authorisation, fund management, the use of custodians or depositaries, investment policies and investor information requirements.

Current Regulatory Framework

Under the UCITS Directive, both a UCITS fund itself and its management company must be authorised.[36] Generally, UCITS funds marketed to investors on a cross-border basis are constituted and authorised in a non-UK EU state (usually Ireland or Luxembourg). UCITS management companies authorised in the UK may manage such non-UK UCITS under the UCITS passport. UCITS management companies may market the units of UCITS they manage within the territories of other member states subject only to local laws implementing Articles 91-96 of the UCITS Directive.

Post-Brexit Regulatory Framework – Financial Centre Model

Post-Brexit, UK management companies could continue to manage non-UK UCITS and market units of UCITS they manage within other member states, if they:

a. establish a UCITS management company in an EU jurisdiction (again, such as Ireland or Luxembourg) and then delegate substantially all of the day-to-day management of the UCITS fund back to the UK manager; or

b. appoint an EU-based, third party platform provider to act as the UCITS management company. As with option (a), the day-to-day management of the UCITS fund would then be delegated back to the UK manager. This is already a common structure in the UCITS world.

The restructuring, repapering and client outreach may have an impact in the short term, but once the new structure is finalised the UK manager may continue performing most of the day-to-day investment management of the UCITS fund in much the same way as it does currently.

Post-Brexit Regulatory Framework – Existing Equivalence Regimes

There is no current UCITS third-country equivalence regime.

[36] This example only considers UCITS funds established in a non-UK EU jurisdiction (such as Ireland or Luxembourg) managed by a UK management company. Most UK UCITS funds managed by UK management companies are predominantly UK-focussed in terms of investor base.

Post-Brexit Regulatory Framework – Expanded Equivalence Model

The introduction of an equivalence regime in the UCITS Directive would enable UCITS management companies authorised in the UK to manage UCITS established in the EU, and to market UCITS they manage within the EU. This equivalence regime may be used as the basis for a recognition regime, under which UCITS management companies incorporated in the UK continue providing services to UCITS established in the EU.[37]

Case Study 4: Fund Management (Non-Retail Funds)

AIFMD regulates fund managers of so-called "alternative" investment funds, such as hedge funds and private equity funds. It establishes requirements for how fund managers carry out their business.

Current Regulatory Framework

UK AIFMs managing EU funds are currently able to utilise the marketing and management passports which the AIFMD provides to EU AIFMs. UK AIFMs are therefore authorised to manage funds established in the EU, and may market those funds in other EU jurisdictions.

Post-Brexit Regulatory Framework – Financial Centre Model

Many UK AIFMs currently manage offshore (non-EU) funds. For them, Brexit has no impact on the management and marketing of those funds.

Post-Brexit, UK AIFMs will continue to be able to manage funds established in the EU and market these funds in other EU jurisdictions as follows:

a. UK AIFMs may rely on local private placement regimes (as they already do for their non-EU funds). Some jurisdictions, such as Luxembourg, Ireland and the Netherlands, impose relatively benign private placement regimes. In these jurisdictions, it is relatively straightforward to access local investors. Other jurisdictions, such as France, Germany and Italy, impose restrictive requirements. A private placement model may not work for UK AIFMs seeking to raise capital from investors located in those jurisdictions;

b. UK AIFMs may access EU investors on a reverse solicitation basis (again, as they already do for their non-EU funds);

c. UK AIFMs may establish a new entity in an EU member state to act as the formal AIFM, which will then delegate much of the investment management function back to the UK manager (similarly to the UCITS delegation model);

d. UK AIFMs may utilise an EU-based third party platform provider to act as the formal AIFM. The third party provider then delegates much of the management back to the UK manager.

Post-Brexit Regulatory Framework – Existing Equivalence Regimes

The AIFMD provides for an equivalence-type regime under which third-country AIFMs may access the AIFMD passport. The major issue with this regime is the timing – to date, no equivalence decisions have been made, and ESMA has been slow in providing the positive advice that is the precursor to an equivalence decision.

The establishment of an EU AIFM or using a third party AIFM, which then delegates to the UK manager, would ensure continued access to the AIFMD passport, although there are costs involved in setting up and staffing the new entity or appointing the platform provider.

---

[37] The amendments to the UCITS Directive would have to ensure that UK management companies could obtain recognition of equivalent status to EU management companies. The UK could implement a reciprocal arrangement in national law to ensure EU management companies are afforded the same treatment in the UK in terms of marketing/services currently provided by such management companies in the UK.

Post-Brexit Regulatory Framework – Expanded Equivalence Model

No additional equivalence regime is required. The existing AIFMD equivalence regime is untested and the timing of any passport extension is uncertain, but the equivalence regime is in principle extensive enough to ensure UK AIFMs would be able to access EU investors.

Case Study 5: Insurance

Current Regulatory Framework

UK-authorised insurance businesses may currently carry out direct insurance, reinsurance, and insurance mediation business with EU-based customers under the Reinsurance, Solvency II and IMD II passports.

Post-Brexit Regulatory Framework – Financial Centre Model

Subject to the perimeter of the relevant local regime, UK insurers may be able to provide insurance services as a non-EEA authorised insurer on the basis of the reverse solicitation exemption with certain wholesale customers. The practice across Europe varies, with some jurisdictions e.g. Germany being more open to "home-foreign insurance".

Under the Financial Centre model, those firms that already operate in continental markets through locally-incorporated and regulated subsidiaries would be entirely unaffected. Insurers whose UK direct business is run through EEA branches (a) with Lloyd's, which draws business directly from agents, brokers and insureds throughout Europe, and (b) with the London market companies, mainly wholesale, specialist and reinsurance companies, who write EU business direct from London, would have two options. Either such insurers could establish locally-incorporated subsidiaries, which would require local licenses and associated establishment and compliance costs. Alternatively, such insurers could leverage the newly-attractive UK regulatory framework and lower associated costs to draw customers to the City. This would involve customers establishing UK affiliates to take the benefit of the insurance, with back-to-back arrangements as appropriate. The UK may need to make appropriate arrangements to facilitate this with clarity, particularly from a tax perspective. While there might be some initial friction costs at the outset, these would quickly be outweighed by the on-going benefits of the more attractive UK market.

Post-Brexit Regulatory Framework – Existing Equivalence Regimes

There is a limited third-country equivalence scheme available for reinsurance agreements entered into with third country reinsurers (to the effect that member states must treat reinsurance contracts with equivalent third country reinsurers the same way as reinsurance contracts with EEA reinsurers) but not direct insurance or insurance mediation activities. However, assuming the UK obtains equivalence status for its reinsurance supervisory regime, UK insurers could subsidiarise to establish an EEA-authorised subsidiary to provide direct insurance services and pass through risks to its UK head office as a reinsurer. The EEA-authorised subsidiary could also carry out cross-border EEA insurance mediation services.

Post-Brexit Regulatory Framework – Expanded Equivalence Model

Expansion of the third-country equivalence regimes would enable UK authorised insurers and reinsurers to offer direct insurance, reinsurance and insurance mediation services to EU customers in the way that they do now without resorting to back-to-back arrangements or local

authorisation/subsidiarisation. Subject to the UK being deemed to have an equivalent insurance supervisory regime, UK insurers could carry out insurance, reinsurance and insurance mediation services across the EEA, potentially subject to registration as a third-country firm with the relevant ESA.

8. The EU's Next Regulations: Avoiding Unnecessary New Measures

Many significant EU developments are due to be implemented in member states from 3 January 2018, in particular, the new trading rules under MiFID II/MiFIR and rules on financial benchmarks in the Benchmark Regulation. These are onerous new rules, due to be implemented at an untimely moment in the light of Brexit. It would be a significant and unnecessary expenditure of effort to implement these rules in January 2018, only to reverse out of them on Brexit some months later.

As such, the UK should consider invoking relevant national discretions embedded in MiFID II/MiFID itself to the fullest extent possible. Derogations permitted under the relevant regulations can be invoked by member states to defer full implementation by way of transitional provisions. This would have the effect of deferring the implementation of specific substantive provisions within the legislation. The application of such transitional provisions would avoid the UK entering into unnecessary commitments and signing up to questionable new regulations while it is in the process of negotiating its future relationship with the EU.

The UK should signal at an early stage its intention to invoke deferrals to the maximum extent permissible to maintain as much flexibility as possible during the negotiation process, whilst positioning itself in a manner which avoids creating new market linkages that – depending on the outcome of the negotiation – may prove to be unsustainable and lead to market disruption.

In doing so, the UK will not pre-judge any determination of equivalence, given that any delay is entirely consistent with the applicable EU regulations. Implementation timings can be aligned as part of any Brexit deal.

Annex A: Sectors with Existing Equivalence Regimes[38]

Table of Contents

Investment Firms

1. Investment Firms and Credit Institutions: Wholesale Business
2. Investment Firms: Suitability and Appropriateness Checks for Foreign Listed Instruments
3. Clearing Brokers: Derivatives
4. Counterparties to Uncleared Swaps: Collateral Eligibility

Credit Institutions

5. Credit Institutions: Collateral Management
6. Credit Institutions and Investment Firms: Group Consolidated Supervision
7. Credit Institutions and Investment Firms: Exposures to Third-Country Investment Firms, Credit Institutions and Trading Venues

Market Infrastructure

8. Trading Venues: Trading Obligation
9. Trading Venues: OTC Derivatives
10. Trading Venues and CCPs: Access Rights
11. Trading Venues: Exemptions for Market Makers from Short Selling Requirements
12. CCPs
13. CCPs: Capital Charges for Exposure to CCPs and Reporting by CCPs
14. Trade Repositories
15. Central Securities Depositories: Securities Settlement

Funds

16. Funds

Insurance

17. Insurers and Reinsurers: Group Supervision
18. Reinsurers

Other Sectors/Legislation

19. Listed Issuers: Securities Issuances
20. Listed Issuers: Accounting Principles
21. Securities Financing Transactions
22. Benchmark Administrators: Use of Benchmarks
23. Credit Rating Agencies: Use of Credit Ratings
24. Audit Firms and Auditors: Financial Statements
25. Euro Payments

[38] Where this Annex sets out the position in the investment business context, it does so in light of MiFID II/MiFIR. No third-country equivalence regime is provided for in MiFID. Unless otherwise stated, MiFID is not addressed in this Annex.

Annex A: Sectors with Existing Equivalence Regimes

Investment Firms and Credit Institutions: Wholesale Business

MiFID II/MiFIR

There is a wholesale equivalence regime for Third-Country Investment Firms and Third-Country Credit Institutions wishing to provide investment services and ancillary services to *per se* professional clients and eligible counterparties with or without the establishment of a branch.[39] The equivalence regime does not, however, cover Third-Country Investment Firms and Third-Country Credit Institutions that offer investment services to retail and elective professional clients (see Annex B, "Investment Firms and Credit Institutions: Retail Business").

Offering services to per se professional clients and eligible counterparties without an EU branch

Third-Country Investment Firms and Third-Country Credit Institutions wishing to provide investment services to *per se* professional clients and eligible counterparties throughout the EU without the establishment of a branch must be registered with ESMA.[40] ESMA registration is subject to the following conditions being satisfied:

(a) the European Commission has adopted an equivalence decision for the third country;

(b) the Third-Country Investment Firm or Third-Country Credit Institution is authorised in the jurisdiction of its head office to provide investment services or activities to be provided in the EU and is subject to effective supervision and enforcement ensuring a full compliance with the requirements applicable in that third country; and

(c) cooperation arrangements between ESMA and the third-country regulator are in place.[41]

Offering services to per se professional clients and eligible counterparties from an EU branch

Third-country Investment Firms and Third-Country Credit Institutions satisfying the following conditions can provide investment services to *per se* professional clients and eligible counterparties in other member states without establishing new branches:

(a) the Third-Country Investment Firm or Third-Country Credit Institution is established in a country whose legal and supervisory framework has been recognised as equivalent; and

(b) the EU branch of the Third-Country Investment Firm or Third-Country Credit Institution is authorised by the relevant member state regulator to provide investment services to retail or elective professional clients under Article 39 of MiFID II (see Annex B, "Investment Firms and Credit Institutions: Retail Business" for conditions that must be satisfied for authorisation).[42]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most provisions of MiFID II/MiFIR will enter into force on 3 January 2018.[43] For the provision of services to *per se* professional clients and eligible counterparties, Third-Country Investment Firms and Third-Country Credit Institutions in the UK are still able to continue to provide investment services into EU member states under their national regulatory perimeter laws until three years after the adoption of an equivalence decision.[44]	National EU authorisation regimes and regulatory perimeters would apply. UK firms providing investment services or performing investment activities would not be able to provide investment services into those EU member states which have protectionist national regulatory perimeters (i.e. most member states except Ireland and Luxembourg). Such firms would need to establish a subsidiary or obtain state-by-state licences for local EU branches.	**No changes required**. Obtaining equivalence under existing regime should be sufficient for Third-Country Investment Firms and Third-Country Credit Institutions providing investment business with wholesale clients. The MiFID II/MiFIR equivalence regime does however need extending to retail clients and elective professional clients (see Annex B, "Investment Firms and Credit Institutions: Retail Business"); and some other sectors such as exchanges and reporting venues (see Annex B, "Investment Firms and Credit Institutions: Retail Business" and "Data Service Providers").

39 Title VIII, MiFIR.

40 Article 46(1), MiFIR.

41 Article 46(2), MiFIR.

42 Article 47(3), MiFIR.

43 Article 93, MiFID II.

44 Article 34(1) MiFIR.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Investment Firms: Suitability and Appropriateness Checks for Foreign Listed Instruments

MiFID II/MiFIR

There is an equivalence regime that allows EU Investment Firms wishing to make use of the exemption from the requirement to provide information relating to the appropriateness of a product or service for its client where the services relate to shares, bonds or other forms of securitised debt admitted to trading on a third-country market.[45]

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the legal and supervisory framework of the third-country satisfies the following conditions:

(a) markets in that third-country are subject to authorisation and to effective supervision and enforcement on an on-going basis;

(b) markets have clear and transparent rules regarding admission of financial instruments to trading so that such securities are capable of being traded in a fair, orderly and efficient manner, and are freely negotiable;

(c) security issuers are subject to periodic and on-going information requirements ensuring a high level of investor protection; and

(d) it ensures market transparency and integrity via rules addressing market abuse in the form of insider dealing and market manipulation.[46]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most provisions of MiFID II/MiFIR will enter into force on 3 January 2018, although the provisions on equivalence decisions are currently in force.[47]	UK exchanges would potentially be less attractive venues for EU Investment Firms providing investment services to clients. The UK market could lose trading or related execution business, if EU Investment Firms cannot make use of the exemption or alternatively compliance costs for EU Investment Firms may increase.	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

45 Article 47(3) MiFIR.

46 Article 28(4) MiFIR.

47 Article 93, MiFID II.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Clearing Brokers: Derivatives

EMIR

This is an equivalence regime incorporated into EMIR with the effect that if a non-EU entity is established in a jurisdiction which has been determined as equivalent, EU or non-EU brokers could comply with the equivalent rules in that country rather than any applicable EMIR requirements as to derivatives market conduct, for example, timely confirmation and portfolio reconciliation.[48]

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the third-country regime:

(a) imposes requirements equivalent to those imposed by EMIR as regards mandatory clearing, mandatory reporting, mandatory clearing for non-financial counterparties and risk mitigation techniques;

(b) ensures equivalent protection of professional secrecy;

(c) is applied and enforced to ensure effective supervision and enforcement in the third country.

No co-operation agreement is required. ESMA will liaise with the relevant third country regulators in preparing the technical advice on equivalence that is provided to the European Commission.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
The need for equivalence for rules on margin for uncleared swaps has been delayed until 1 March 2017.	Probably not a major issue, in that ISDA protocols executed by almost all market participants have resulted in them all signing up to the EU's requirements already. EU financial counterparties would need to apply EU standards when trading with UK counterparties until the UK's regulatory regime is determined to be equivalent. Given the regulatory standards in the UK, it would likely only be a matter of time whilst negotiations are undertaken with the EU to ensure that an equivalence decision is rendered.	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

48 Where two non-EU entities are trading with each other, it is open for the European Commission to impose EMIR's obligations on each of the two entities if the contract falls within EMIR's extraterritoriality provisions which apply: (i) if the contract has a "direct or foreseeable effect" in the EU; or (ii) if it is necessary to prevent the evasion of EMIR. The EU Level 2 legislation detailing these requirements has been adopted in fairly limited circumstances.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Counterparties to Uncleared Swaps: Collateral Eligibility

EMIR
CRD
RTS on Margin for Uncleared OTC Derivatives

There is an equivalence regime that enables a collecting counterparty, for the purposes of assessing the credit quality of certain collateral, to use an internal ratings based model of the third-country posting counterparty, where that counterparty is subject to laws applying equivalent prudential and supervisory requirements on a consolidated basis.

Equivalence Decisions

An equivalence decision will only be adopted by a national competent authority, at the request of the parent undertaking or of any regulated entities authorised in the EU, or on its own initiative if the third-country supervisory authority imposes equivalent principles to the CRD.[49]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Although EMIR entered into force in August 2012, the detailed provisions on margin for uncleared derivatives will only apply to different categories of counterparties according to size, starting with the largest counterparties, which will be in effect from one month after the final RTS enters into force,[50] which is expected to be in the coming months.	The credit quality assessment of a UK counterparty would have to be undertaken using more standardised (and potentially less liberal) methodologies. These would include a credit quality assessment of a credit rating agency that is registered or certified in accordance with the CRA Regulation, or a central bank issuing credit ratings that are exempt from the application of the CRA Regulation. This would lead to a higher cost of capital for EU institutions dealing with UK counterparties.	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

49 This reflects the position under Article 6 of a proposed RTS adopted by the European Commission on 4 October 2016. This will be published in the Official Journal after the expiry of the objection period of the Council and the EP, assuming that no objections are made.

50 Article 36, RTS on Margin for Uncleared OTC Derivatives.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Credit Institutions: Collateral Management

CRR
RTS on Margin for Uncleared OTC Derivatives

There is an equivalence regime that enables derivatives counterparties to hold initial margin collected as cash with a Third-Country Credit Institution.

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the third-country supervisory authority imposes equivalent principles to those in CRR.[51]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
CRR is in force. However, the detailed provisions on margin for uncleared derivatives will only apply to different categories of counterparties according to size, starting with the largest counterparties, which will be in effect from one month after the final RTS enters into force,[52] which is expected to be in the coming months.	UK institutions could lose custody or margin deposits if they cease to be valid places for EU participants' cash collateral to be held. Equivalence should be expected, as UK institutions will likely be subject to the same regulatory requirements as EU institutions under the CRR upon exit.	**No changes required**. Obtaining equivalence under existing regime would be sufficient for EU derivatives counterparties to continue to hold initial margin with UK institutions.

[51] Article 19(1)(e)(i), RTS on Margin for Uncleared OTC Derivatives.

[52] Article 36, RTS on Margin for Uncleared OTC Derivatives.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Credit Institutions and Investment Firms: Group Consolidated Supervision

CRD

There is an equivalence regime that allows an EU Credit Institution or EU Investment Firm to be subject only to third-country consolidated supervision (and so avoid additional EU consolidated supervision) if it has a third-country parent.

Equivalence Decisions

An equivalence decision will only be adopted by the national competent authority that would have been responsible for consolidated supervision of the EU Credit Institution or EU Investment Firm had the normal determination principles set out in CRD been applied (in consultation with the EBA). The equivalence assessment is taken at the request of the parent undertaking or of any of the regulated entities authorised in the EU, or on its own initiative. An equivalence decision will only be adopted if the third-country supervisory authority imposes equivalent principles to those contained in CRD IV and those principles on prudential consolidation contained in CRR.[53]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	An EU Credit Institution or EU Investment Firm which has a UK parent which is a financial holding company or mixed financial holding company would be subject to the full requirements of CRD at UK group level downwards, in addition to any UK consolidated supervision, resulting in it having two group regulators for capital purposes. Alternatively, the EU would be subject at UK topco level downward, to "other appropriate supervisory techniques" which also achieve the objectives of consolidated supervision, as determined by the national laws of the member state where the EU Credit Institution or EU Investment Firm is established, which may include requiring the establishment of a holding company in the EU. There is no list of approved third countries for institutions eligible for group consolidated supervision as this is done at EU member state level. However, we understand that some member states have approved institutions in groups headquartered in the US, China, Brazil, Switzerland and others under CRD IV or its earlier iterations.	**No changes required**. Obtaining equivalence under existing regime in respect of the UK's consolidated supervision of UK parents of EU Credit Institutions or EU Investment Firms would be sufficient.

[53] Article 127(1), CRD.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Credit Institutions and Investment Firms: Exposures to Third-Country Investment Firms, Credit Institutions and Trading Venues

CRR

There is an equivalence regime that allows EU Credit Institutions and EU Investment Firms to treat their exposures to Third-Country Credit Institutions, Third-Country Investment Firms and third-country trading venues on the same terms as exposures to the EU equivalents.

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the third-country supervisory authority imposes equivalent prudential and supervisory requirements to those applied in the European Union.[54]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force. Where no equivalence decision had been made and until 1 January 2015, EU Credit Institutions and EU Investment Firms could continue treating exposures to the relevant third-country entity as if they were exposures to EU Credit Institutions or EU Investment Firms, provided that the relevant competent authorities have approved the third country as eligible for that treatment before 1 January 2014.[55]	EU Credit Institutions and EU Investment Firms would be subject to higher capital requirements.	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

[54] Article 107(3) and (4), CRR.

[55] Article 107(4), CRR.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Trading Venues: Trading Obligation

MiFID II/MiFIR

There are equivalence regimes in respect of the trading obligation for transactions in:

(a) shares. EU Investment Firms must ensure that trades in shares take place on a regulated market, MTF, systemic internaliser, or an equivalent third-country trading venue;[56] and

(b) derivatives of a class of derivatives that has been declared subject to the trading obligation.[57] EU Investment Firms may only trade such derivatives on a regulated market, MTF, systemic internaliser, or an equivalent third-country trading venue.[58]

Equivalence Decisions

In each case, an equivalence decision will only be adopted by the European Commission if the legal and supervisory framework of the third-country satisfies the following conditions:

(a) trading venues in that third-country are subject to authorisation and to effective supervision and enforcement on an on-going basis;

(b) trading venues have clear and transparent rules regarding admission of financial instruments to trading so that such financial instruments are capable of being traded in a fair, orderly and efficient manner, and are freely negotiable;

(c) issuers of financial instruments are subject to periodic and on-going information requirements ensuring a high level of investor protection; and

(d) it ensures market transparency and integrity via rules addressing market abuse in the form of insider dealing and market manipulation.[59]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most provisions of MiFID II/MiFIR will enter into force on 3 January 2018,[60] although the provisions on equivalence decisions are already in force.[61]	UK trading venues, including exchanges, would not be third-country trading venues on which EU Investment Firms could satisfy the derivatives trading obligation. Therefore, they would not benefit from business resulting from the introduction of the mandatory derivatives trading obligation in the EU or may cease to be used by existing EU customers. Falling short of the UK gaining equivalence, UK trading venues could consider restructuring to provide trading venue facilities from EU-regulated subsidiaries so that customers could satisfy the derivatives trading obligation on those venues.	**No changes required**. Obtaining equivalence under the existing regime would ensure that UK trading venues maintain their status as valid options for EU Investment Firms subject to the derivatives trading obligation. The MiFID II/MiFIR equivalence regime does not, however, provide any level of regulatory access for exchanges. A broader equivalence regime allowing third-country exchanges access to EU customers is required (see Annex B, "Regulated Markets").

56 Article 23(1),MiFIR.

57 To date, there have been no cases of derivatives that have been declared subject to the trading obligation.

58 Article 28(1)(d), MiFIR.

59 Article 28(4), MiFIR.

60 Article 93, MiFID II.

61 Article 55, MiFIR.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Trading Venues: OTC Derivatives

EMIR

There is an equivalence regime for third-country trading venues to be deemed equivalent to an EU regulated market.[62] Trades executed on such an equivalent third-country trading venue are not regarded as "OTC" for the purposes of determining the applicability of the clearing obligation and certain other requirements under EMIR which apply only to OTC (and not exchange-traded) derivatives.

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the third-country market:

(a) complies with legally binding requirements equivalent to those applicable to regulated markets under MiFID II/MiFIR; and

(b) is subject to effective supervision and enforcement in the third country.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	Derivatives contracts traded on non-equivalent third country trading venues would be deemed 'OTC derivatives contracts' under EMIR. Counterparties to such derivatives would – provided the relevant thresholds are exceeded and no intragroup transaction exemption applies – be subject to the OTC derivatives contracts obligations under EMIR. These obligations include clearing requirements and risk-mitigation requirements for non-cleared OTC derivatives. A non-equivalent third country trading venue would also be disadvantaged by being unable to offer trading for derivatives contracts that would fall outside of the application of obligations under EMIR.	**No changes required**. Obtaining equivalence under existing regime would be sufficient for counterparties to OTC derivatives to avoid inappropriate rules for exchange trades under EMIR.

[62] 'Regulated Market' means a regulated market within the meaning of Article 4(1)(21), MiFID II.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Trading Venues and CCPs: Access Rights

MiFID II/MiFIR

There is an equivalence regime for third-country trading venues to access an EU CCP.[63]

A third-country CCP may only request access to an EU trading venue if has been recognised by ESMA under EMIR (see Annex A "CCPs").

Third-country trading venues and CCPs may only make use of the access rights under MiFIR if the European Commission has adopted an additional equivalence decision in relation to the legal and supervisory framework of the third country.[64]

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the legal and supervisory framework of the third country satisfies the following conditions:

(a) trading venues in that third country are subject to authorisation and to effective supervision and enforcement on an on-going basis;

(b) it provides for an effective equivalent system for permitting CCPs and trading venues authorised under foreign regimes access to CCPs and trading venues established in that third country; and

(c) it provides for an effective equivalent system under which CCPs and trading venues are permitted access on a fair, reasonable and non-discriminatory basis to: (i) relevant price and data feeds and information of composition, methodology and pricing of benchmarks for the purposes of clearing and trading; and (ii) licenses, from persons with proprietary rights to benchmarks established in that country.[65]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most provisions of MiFID II/MiFIR will enter into force on 3 January 2018,[66] although the provisions on equivalence decisions are already in force.[67]	A lack of equivalence is unlikely to be a material issue for financial markets in this case, given that no such access rights previously existed in EU legislation before MiFID II/MiFIR, which are not yet in force, and so no such rights are being relied on presently by UK trading venues or CCPs. This equivalence right therefore contrasts to the trading obligation, which is new but will be mandatory across Europe; and the access regime for EU Investment Firms, which adds to the existing MiFID regime and so is already relied upon.	**No changes required**. An equivalence regime exists already. The MiFIR access provisions, particularly its requirements around contractual netting, are widely regarded as unworkable, controversial and driven by EU single market thinking rather than regulatory thinking, so are likely to be modified or abandoned post-Brexit. Doing so would likely mean that equivalence is not available but that should not be an issue for financial markets. In fact, not having equivalence here could in many ways improve the ability of financial markets to withstand systemic shocks.

[63] Article 38(1), MiFIR.

[64] Article 38(1), MiFIR.

[65] Article 38(3), MiFIR.

[66] Article 93, MiFID II.

[67] Article 55, MiFIR.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Trading Venues: Exemptions for Market Makers from Short Selling Requirements

SSR

There is an equivalence regime for third-country market makers to benefit from the exemptions in the SSR relating to the restrictions on uncovered short sales in shares and sovereign debt and credit default swap positions and the notification requirements for short sales in shares and sovereign debt. The third-country market maker must provide written notification to its home member state regulator that it intends to make use of the exemption at least 30 days before the intended use of the exemption.[68]

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the third-country regime applies legally-binding requirements to markets in that third country that are:

(a) equivalent to the requirements set out in MiFID II/MiFIR as to regulated markets;

(b) equivalent to the requirements set out in MAR as to insider dealing and market abuse;

(c) equivalent to the requirements set out in the Transparency Directive; and

(d) subject to effective supervision and enforcement in that third country.[69]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	A UK market maker would not be able to benefit from the exemptions under the SSR and so would be subjected to a greater level of public and regulatory reporting, including in respect of transactions done in their capacity as market maker.	**No changes required**. Obtaining equivalence under existing regime would be sufficient for UK firms involved in market making activity to remain exempt. Notably, much of the rest of the SSR is extraterritorial in scope and so would still apply to the UK post-Brexit. Potentially, a broader equivalence regime involving compliance with UK reporting could be established. However, the lack of such a regime should not present a particular issue for UK markets in that the rules involve reporting based on the location of listing or the home country of a sovereign instrument, which will necessarily sometimes involve reporting to the EU. Moreover: (i) UK firms are set up for compliance with SSR already; and (ii) third-country firms need to comply with the SSR regime currently, and generally speaking, most third-country firms already do so.

[68] Article 17(5), SSR.

[69] Article 17(2), SSR.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

CCPs

EMIR

There is an equivalence regime that allows third-country clearing houses to provide direct access to European members or exchanges without needing to be established in the EEA. Co-operation arrangements between ESMA and the third-country regulator must be in place.

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the third-country clearing house is subject to a legal regime that:

(a) imposes effective supervision and enforcement on an on-going basis;

(b) provides for an effective equivalent system for the recognition of third-country clearing houses to be recognised under that third country's regime; and

(c) imposes equivalent requirements as those set out in EMIR as regards organisational conduct and prudential requirements.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force. A list of recognised CCPs is available (last updated on 17 June 2016) and a list of applicants is available (last updated on 8 January 2016).	UK clearing houses would not be able to clear derivatives for EU clearing members or EU exchanges or trading venues. Considering the diverse range of CCPs that have been recognised it is to be expected that the UK's regime and regulators should pass without difficulties.	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

CCPs: Capital Charges for Banks for Exposure to CCPs and Reporting by CCPs

CRR
EMIR

There is an equivalence regime that allows third-country CCPs to gain status as a QCCP. Lower capital requirements are imposed on institutions calculating risk-weight of their exposures for exposures to a QCCP than for exposures to a non-QCCP.

The requirements for CCP recognition and equivalence under EMIR are set out in Annex A, "CCPs".

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
The transitional period for regulatory capital requirements for EU institutions' exposures to CCPs and the transitional period for CCPs to report the collection of initial margin from clearing members have been extended to 15 December 2016.[70]	Higher capital requirements would be imposed on EU institutions for their exposures to a UK CCP that is not recognised as a QCCP (based on standard exposures of up to 100%, rather than the 0-4% model available for QCCPs).	**No changes required**. Obtaining equivalence under existing regime would be sufficient to avoid increased capital requirements in respect of EU institutions' exposures to UK CCPs.

[70] Commission Implementing Regulation (EU) 2016/892 of 7 June 2016.

Trade Repositories

EMIR
SFTR

There is an equivalence regime that enables a third-country trade repository to provide services to counterparties, subject to the SFTR[71] and EMIR[72] reporting obligations. The trade repository must be recognised by ESMA under the SFTR or EMIR. Co-operation arrangements between ESMA and the third-country regulator must be in place (SFTR[73] & EMIR[74]).

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if:

(a) trade repositories in that third country comply with legally binding requirements (applies to both the SFTR[75] and EMIR[76] regimes);

(b) trade repositories in that third country are subject to supervision and enforcement on an on-going basis (SFTR[77] & EMIR[78]);

(c) guarantees of professional secrecy exist (SFTR[79] & EMIR[80]); and

(d) trade repositories authorised in that third country are subject to a legally binding and enforceable obligation to give direct and immediate access to the data to the ESAs and national competent authorities.[81]

Where condition (d) has not been satisfied, the European Commission will submit recommendations to the Council for the negotiation of mutual access between the specified ESAs, national competent authorities, and third-country authorities of the relevant third country to the data held by trade repositories.[82]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
The SFTR is in force, subject to certain exceptions dependent on the adoption of delegated acts by the European Commission, including for the reporting obligation for third-country entities. EMIR is in force.	UK trade repositories could not offer reporting obligation services to EU clients, because any such reporting would not discharge the EMIR and SFTR reporting obligations. Almost all the current EU trade repositories and most of its largest providers are all located in the UK, making this an important equivalence regime to establish for both the EU and the UK.	**No changes required**. Obtaining equivalence under existing regime for UK regulated trade repositories would be sufficient. It is in the interests of the EU to recognise UK trade repositories as four of the six trade repositories currently authorised by the EU are established in the UK.

71 Article 19(4)(a) and, SFTR. The SFTR provides for a trade repository that is recognised by ESMA under EMIR to apply for an extension for the purposes of registration under the SFTR.

72 Article 77, EMIR.

73 Article 19(5)(b), SFTR.

74 Article 81, EMIR.

75 Article 19 (1)(a), SFTR.

76 Article 77, EMIR.

77 Article 19 (1)(b), SFTR.

78 Article 77 and 78, EMIR.

79 Article 19 (1)(c), SFTR.

80 Article 83, EMIR.

81 Article 19 (1)(d), SFTR.

82 Article 19(2) SFTR.

Central Securities Depositories: Securities Settlement

CSD Regulation

There is an equivalence regime that allows a third-country CSD to provide services, including by establishing a branch,[83] to issuers with securities admitted on regulated markets, MTFs or trading venues in the EU. Co-operation arrangements between ESMA and the third-country regulator must be in place.[84]

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if:

(a) the CSD is subject to effective authorisation, supervision and oversight or, if the securities settlement system is operated by a central bank, oversight, ensuring full compliance with the prudential requirements applicable in that third country;

(b) the third country provides for the equivalent recognition of foreign CSDs in its country;

(c) where relevant, the third-country CSD takes the necessary measures to allow its users to comply with the relevant national law of the member state in which the third-country CSD intends to provide CSD services; and

(d) the third-country regime applicable to the third-country CSD must impose legally binding requirements which are in effect equivalent to the requirements contained in the CSD. This can include an assessment of whether the third-country regime meets internally agreed CPSS-IOSCO standards.[85]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force. The Target2-Securities platform became operational on 22 June 2015.[86] There is a programme for migration and, according to the European Central Bank, Target2-Securities will service 21 jurisdictions (EU and non-EU) by the end of 2017.	UK CSDs would not be able to operate a securities settlement system or provide notary services or central maintenance services that are made available to issuers with securities admitted on regulated markets, MTFs or trading venues in the EU. UK CSDs such as CREST/Euroclear UK&Ireland provide a significant function across the EU for EU regulated financial institutions and other entities, particularly for UK shares and government bonds. Accordingly, the business impact would be likely to be significant.	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

83 Article 25(1), CSD Regulation.

84 Article 25(4), CSD Regulation.

85 The Committee on Payments and Settlement Systems was renamed the Committee on Payments and Market Infrastructures on 1 September 2014.

86 Target2-Securities is a Eurosystem securities settlement system offering settlement in central bank money across European securities markets.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Funds

AIFMD

A third-country access scheme, distinct from an equivalence regime is in place. This requires non-EU AIFMs to be authorised in an EU member state in order to manage EU AIFs, or to market either EU or non EU AIFs in the EU.[87]

Authorisation of a non-EU AIFM would require:[88]

(a) full compliance with the AIFMD as though the AIFM were based in the EU;

(b) appropriate co-operation arrangements to be in place;

(c) the non-EU country to not be listed by the FATF as a NCCT;

(d) tax agreements to be in place between the third country that the non-EU AIFM is established in and the member state; and

(e) the appointment of a legal representative established in the member state of reference.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force. Authorisation of non-EU AIFMs is not expected to be possible until late 2016 at the earliest, and not expected to become compulsory until 2018 at the earliest. Until authorised, a non-EU AIFM may only market AIFs in accordance with national private placement regimes in EU countries, or must rely on reverse solicitation. There is no "equivalence" regime under AIFMD. Instead, ESMA conducts an assessment of the third country in question and decides whether to issue positive advice to the European Commission to extend the "passport" to that third country.[89]	At some stage in the future, if private placement regimes are abolished, UK AIFMs may not (1) manage EU AIFs, or (2) market AIFs (whether EU or non-EU AIFs) in the EU unless they can rely on reverse solicitation. UK fund managers should consider taking advantage of EEA private placement regimes to sell funds into Europe or reverse solicitation exemptions under local member state law. AIFMs seeking to benefit from the marketing passport could establish an affiliated EU AIFM (or use an EU third party AIFM) and delegate substantial parts of management back to the non-EU AIFM. This would enable UK fund managers to carry out delegated everyday management as sub-managers, whilst the fund benefits from a passport. This is already a well-established practice for fund managers.	The UK fund manager may need to be authorised under MiFID II/MiFIR to be carrying out such management services (see Annex A, "Investment Firms and Credit Institutions: Wholesale Business ".)

[87] Article 37, AIFMD.

[88] Article 37(7), AIFMD.

[89] Article 67, AIFMD.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Insurers and Reinsurers: Group Supervision

Solvency II

There is an equivalence regime for insurers and reinsurers for the purposes of group solvency and group supervision requirements. Equivalence allows EU supervisors to rely upon third-country consolidated solvency supervision, rather than impose a second level of its own consolidated supervision. Equivalence may be full or in part and temporary equivalence is also possible.

Equivalence Decisions

In the case of (re)insurers headquartered within the EEA with participations or subsidiaries located outside the EEA, an equivalence decision will only be adopted by the European Commission or, in the absence thereof, by the group supervisor in consultation with other relevant supervisors if:[90]

(a) the third-country solvency regime applies standards to the third-country (re)insurer that are equivalent to certain specified rules on the valuation of assets, liabilities, own funds, minimum solvency capital, investment rules and overall reinsurance and insurance supervision as set out in Solvency II;

(b) the third-country regime requires (re)insurers to hold adequate financial resources based on equivalent principles;

(c) the third-country regime applies capital requirements that are risk-based;

(d) the third-country regime applies adequate standards of professional secrecy; and

(e) the third-country regime applies adequate standards as to information exchange by regulators.

In the case of (re)insurers headquartered within a third country which has related undertakings located within the EEA, an equivalence decision will only be adopted by the European Commission or, in the absence thereof, by the group supervisor in consultation with other relevant supervisors if:[91]

(a) the third-country supervisory authorities have the means and capacity of to enforce its prudential regime;

(b) the third-country regime imposes adequate governance requirements;

(c) the third-country regime imposes adequate risk management and reporting requirements;

(d) the third-country regime imposes adequate restrictions on the use of own fund items; and

(e) the third-country regime imposes adequate professional secrecy standards and permits information exchange amongst regulators.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Solvency II applied from 1 January 2016.	EU groups that include UK insurers or reinsurers would not be able to rely on UK capital requirements instead of the Solvency II rules for UK entities as part of group solvency calculations. For EEA insurers or reinsurers with UK parents, there would be no ability to rely on the supervision of the parent entity by the UK regulators. Member states would be permitted to apply many of the rules set out in Solvency II directly to a UK insurance or reinsurance entity that is subject to EU group supervision, or to agree "other methods" so as to ensure appropriate supervision of the relevant entity within the group.	For group prudential supervision and group solvency purposes, obtaining equivalence would be sufficient. For UK direct insurers, a new equivalence regime for access will need to be established to supplement this limited equivalence right (see Annex B, "Direct Insurance".)

[90] Article 227, Solvency II. See also Article 379, Solvency II Delegated Regulation.

[91] Article 260, Solvency II Directive. See also Article 379, Solvency II Delegated Regulation.

Reinsurers

Solvency II

There is an equivalence regime that requires third-country reinsurance contracts to be treated the same manner as contracts with EEA supervised reinsurers. This ensures that third-country reinsurers remain attractive to EEA supervised direct insurers, as the equivalence regime does not allow national competent authorities to treat third-country reinsurers differently for solvency purposes from EEA reinsurers.

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if:[92]

(a) the third-country solvency regime imposes effective supervision, sanctions and enforcement of reinsurers;

(b) the expertise and capabilities of the third-country supervisory authorities is adequate to protect policy holders and beneficiaries effectively;

(c) the third-country solvency regime authorises reinsurers on clear, objective and publicly-available written standards;

(d) the third-country solvency regime imposes effective governance requirements for reinsurers;

(e) the third-country solvency regime imposes effective reinsurer risk management systems;

(f) the third-country solvency regime imposes adequate financial resources requirements on reinsurers;

(g) the third-country solvency regime imposes adequate requirements as to professional secrecy, confidentiality, and regulatory information exchange.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Solvency II applied from 1 January 2016.	Competent authorities would not be prohibited from treating reinsurance contracts with UK reinsurers differently from reinsurance contracts with EEA reinsurers. This may mean that competent authorities could have the ability impose additional supervisory or collateral requirements on EEA regulated insurers in respect of EEA risks that are reinsured by the UK reinsurer.	Obtaining an enhanced equivalence regime for UK reinsurers that permits reinsurance services to be offered throughout the EEA and equivalence status to require UK reinsurance contracts to be treated in the same way as EEA reinsurance contracts would be sufficient.

[92] Article 378(a), Solvency II Delegated Regulation.

Listed Issuers: Securities Issuances

Prospectus Directive
Proposed Prospectus Regulation

A third-country access regime is available in the Prospectus Directive and proposed Prospectus Regulation, although this falls short of full equivalence. The regime permits third-country issuers access to the EU capital markets, provided that the following conditions are satisfied:[93]

(a) approval by the national regulator of the relevant EU member state;

(b) the prospectus must be drawn up in accordance with the international standards set by IOSCO; and

(c) the information requirements are equivalent to the requirements under the Prospectus Directive.

The Prospectus Directive allows for third-country issuers to choose a "home member state" which is responsible for the approval of offering and listing documentation. Approval by that home member state allows the issuer to apply for a "passport", under which an offering may be made into other member states, using the same prospectus, subject only to minor additional requirements.

Once one national regulator has approved the prospectus it can be passported into other EU member states.

The provisions on access by third-country issuers are very similar in the proposed Prospectus Regulation.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
The Prospectus Directive is in force. The proposed Prospectus Regulation will repeal the Prospectus Directive when it comes into force.	The prospectus requirement does not apply to exempt and wholesale offers, which are exempt from the Prospectus Directive. This means that offers to investment professionals or where minimum denomination is greater than €100,000 and unlisted offerings would not be affected. UK companies who seek to engage in retail offers of securities in the EU or who want an EU listing would need a further level of review and approval of relevant prospectuses by an EU "home member state" supervisor (in addition to any applicable UK process). For current third-country entities, this usually means adding a small "EU wrapper" and is not a material barrier for those who wish to obtain a listing or offer securities in the EU. Failure to gain approval could render the prospectus ineligible for an offer to the public or for admission to trading on an EU regulated market. Under the proposed Prospectus Regulation, UK-listed companies would also need to appoint an EU supervised firm as its representative for the purposes of its retail offers.	The exemptions and access arrangements under the Prospectus Directive provide for a degree of access for third country issuers. An equivalence regime providing access in respect of the remaining gaps e.g. an equivalence regime to allow passporting of prospectuses without further local member state approvals could be considered but is unlikely to deliver material additional practical benefits.

[93] Article 20(1), Prospectus Directive.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Listed Issuers: Accounting Principles

IAS Regulation
IAS Equivalence Mechanism Regulation
Transparency Directive
Prospectus Directive

There is an equivalence regime for third-country issuers that are listed on EU exchanges to be able to use local GAAP in the preparation of their financial statements.[94]

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the GAAP of the third country enables investors to make a similar assessment of the assets and liabilities, financial position, profit and losses and prospects of the issuer as financial statements drawn up in accordance with IFRS, with the result that investors are likely to make the same decisions about the acquisition, retention or disposal of securities of an issuer.[95]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	No impact: UK listed companies must use IFRS under the current Companies Act 2006, which is a UK domestic law.	**Equivalence not needed**.

[94] EU laws require issuers whose securities are traded on a regulated market to apply IFRS to their consolidated financial statements. Third country issuers may prepare their financial reports in accordance with IFRS or any other standard that has been declared equivalent to IFRS.

[95] Article 2, IAS Equivalence Mechanism Regulation.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Securities Financing Transactions

SFTR

There is an equivalence regime that allows transactions between an EU and third-country counterparty to be subjected to the equivalent rules in the third country (instead of applicable SFTR reporting requirements).[96]

No co-operation agreement is required. ESMA will liaise with the relevant third country regulators in preparing the technical advice on equivalence that is provided to the European Commission.

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if the third-country regime:[97]

(a) imposes requirements that are equivalent to the reporting obligations set out in the SFTR;

(b) ensures the protection of professional secrecy to the same standards as set out in the SFTR;

(c) is effectively applied and enforced to ensure effective supervision and enforcement in that third country; and

(d) ensures that specified ESAs and relevant national competent authorities and third country regulators have direct or indirect access to securities financing transactions data equivalent to the access provisions of the SFTR.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Mostly in force. However, the main new obligation in SFTR – reporting of transactions – will apply only after the RTS are finalised.[98]	EU counterparties would need to apply EU standards e.g. as to the SFTR's reporting requirements when trading with UK counterparties until the UK's regulatory regime was determined to be equivalent.	**No changes required**. Obtaining equivalence under existing regime would be sufficient. Note that the proposed reporting regime under the consultation versions of RTS under SFTR is extremely onerous. It will be interesting to see how legislators react to the consultation and whether the UK chooses not to introduce any aspects of this regulation.

96 Article 21(2), SFTR.

97 Article 21(1), SFTR.

98 ESMA will use the responses to its DP earlier in 2016 to develop detailed rules on which it will publish a follow-up consultation. ESMA shall send its draft rules for approval to the European Commission by 13 January 2017.

Benchmark Administrators: Use of Benchmarks

Benchmark Regulation

There are three regimes that allow the benchmarks produced by a benchmark administrator established in a third country to be used in the EU by EU-supervised entities. The benchmark administrator and its benchmarks must be included in ESMA's register of benchmarks.

Benchmarks administered by third-country administrators can be accessed by EU-supervised entities through the following methods:[99]

(a) an equivalence decision and satisfaction of certain other requirements;

(b) the administrator obtaining prior recognition in a member state of reference; or

(c) endorsement of the benchmark by an EU authorised or registered benchmark administrator or other supervised entity.

Equivalence

For this option, the following requirements must be fulfilled:

(a) a co-operation agreement is in place;

(b) an equivalence decision has been adopted by the European Commission for either all benchmark administrators or for specific administrators or specific benchmarks or families of benchmarks;

(c) the administrator of the benchmark is authorised and supervised in its own country;

(d) the administrator has notified ESMA of its consent that its benchmarks may be used by supervised entities in the EU, the list of benchmarks covered by that consent and the details of its national regulator; and

(e) the third-country regime complies with the IOSCO Principles for Financial Benchmarks and the IOSCO Principles for Oil Price Reporting Agencies.

Member State of Reference recognition

Until an equivalence decision is made under the Benchmark Regulation, a third-country benchmark administrator may provide its benchmarks for use in the EU by supervised entities provided that:[100]

(a) the benchmark administrator is subject to certain exceptions, complies with the Benchmark Regulation which may be fulfilled by complying with the IOSCO Principles;

(b) the benchmark administrator establishes a legal representative in its member state of reference;

(c) the benchmark administrator applies for recognition to the relevant regulator of the member state of reference;

(d) co-operation arrangements are in place; and

(e) the laws of the third country do not prevent the effective supervision and oversight of the benchmark administrator by the regulator in its member state of reference.

Endorsement

Until an equivalence decision is made, a third-country benchmark administrator may provide its benchmarks for use in the EU by supervised entities provided that an EU-authorised or registered administrator or any other supervised entity has endorsed for use in the EU the benchmark or family of benchmarks provided by the benchmark administrator. The EU-authorised or registered administrator or any other supervised entity must apply to its national regulator for approval of the endorsement, satisfying the following conditions:[101]

(a) it has a "clear and well defined role within the control or accountability framework of the third-country administrator which allows such person to effectively monitor the provision of the benchmark";

(b) verification that the provision of the benchmark to be endorsed meets requirements that are as stringent as those in the Benchmark Regulation;

---

[99] Article 30(1), Benchmark Regulation.

[100] Article 32, Benchmark Regulation.

[101] Article 33, Benchmark Regulation.

(c) demonstrate the necessary expertise to monitor the provision of activities performed in the third country effectively and to manage the associated risks; and

(d) demonstrate an objective reason to provide the benchmark or family of benchmarks in a third country and endorse them for use in the EU.[102]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most of the Benchmark Regulation will apply from 1 January 2018.[103] Certain provisions giving ESMA powers to produce draft technical standards and giving the European Commission power to adopt delegated legislation, including in relation to the third-country provisions, applied from 30 June 2016. A benchmark provided by a third-country administrator that is already being referenced in financial instruments and financial contracts in the EU on 1 January 2020 may continue to be referenced in those contracts and financial instruments. However, no financial instruments and financial contracts in the EU may start to reference a benchmark provided by a third-country administrator on or after 1 January 2020. An EU index provider that was providing a benchmark on 30 June 2016 must apply for authorisation or registration by 1 January 2020. An EU index provider may continue to provide an existing benchmark until 1 January 2020 unless or until its application for authorisation or registration is refused.[104]	EU-supervised entities would not be allowed to use UK-produced benchmarks, such as LIBOR, ISDAFix, Brent oil, certain FX rates or global gold or silver or other precious metal standards. UK benchmark administrators would not be able to distribute these benchmarks to EU supervised entities.	**No changes required**. Obtaining equivalence under existing regime would be sufficient. The UK and EU should both press for equivalence, to avoid the other two rather tortuous alternatives being needed.

102 The European Commission is responsible for setting the conditions for a national regulator to assess whether there is an objective reason for the provision of a benchmark or family of benchmarks in a third country and their endorsement for use in the EU.

103 Article 59, Benchmark Regulation.

104 Article 51, Benchmark Regulation.

Credit Rating Agencies: Use of Credit Ratings

CRA Regulation

There is an equivalence regime that allows credit ratings issued on non-EU issuers or instruments and from third countries by a CRA established and supervised in a third country, without a presence in the EU can be used for regulatory purposes in the EU by EU-regulated entities if the following conditions are satisfied:[105]

(a) the CRA is authorised or registered and is subject to supervision in that third country;

(b) co-operation arrangements between the third-country regulator and ESMA are in place;

(c) the credit rating issued by the third-country CRA and its credit rating activities are not of systematic importance to the financial stability or integrity of the financial markets of one or more member states; and

(d) the CRA is certified by ESMA.

Equivalence Decisions

An equivalence decision will only be adopted by the European Commission if:[106]

(a) CRAs in that country are subject to authorisation or registration and effective supervision and enforcement on an on-going basis;

(b) CRAs in that country are subject to legally binding rules equivalent to the EU rules; and

(c) the regulatory regime of the third country prevents interference by supervisory (or other public) authorities with the content of credit ratings and methodologies.

Endorsement

Credit ratings on EU and non-EU issuers or instruments issued by a CRA based outside the EU but belonging to the same group of a CRA registered with ESMA may be "endorsed" by an EU CRA, and used for regulatory purposes in the EU by EU-regulated entities if the following conditions are satisfied:[107]

(a) the credit rating activities resulting in the issuing of the credit rating to be endorsed are undertaken in whole or in part by the endorsing CRA or by CRAs belonging to the same group;

(b) the CRA has verified and is able to demonstrate on an on-going basis to ESMA that the conduct of the third-country CRA resulting in the credit rating to be endorsed fulfils requirements which are at least as stringent as those in the CRA Regulation;

(c) there is an objective reason for the credit rating to be produced in a third country;

(d) the CRA established in the third country is authorised or registered, and is subject to supervision in that third country; and

(e) co-operation arrangements between ESMA and the third-country regulator are in place.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	The credit ratings of a UK CRA would not be able to be used by EU Credit Institutions, EU Investment Firms, insurance undertakings, reinsurance undertakings, institutions for occupational retirement provision, management companies, investment companies, AIFMs and CCPs in the EU, unless equivalence status or endorsement is obtained. Considering the role of UK CRAs in their use by EU regulated financial institutions and other	**No changes required**. Obtaining equivalence under existing regime would be sufficient here and is the better option. Endorsement of the UK CRA would be contingent upon an EU-established CRA.

[105] Recital 15 and Article 5(6), CRA Regulation.

[106] Article 5, CRA Regulation.

[107] Article 4, CRA Regulation.

entities, it is to be expected that an equivalence decision could be obtained or access via the endorsement process to be available. Failing that, UK CRAs may have to establish additional subsidiaries in EEA member states.

A UK CRA may be able to apply for an exemption from the requirement to have a physical presence in the EU by demonstrating that the requirement would be too onerous and disproportionate based on the nature, scale and complexity of its business and the nature and range of its issuing of credit ratings.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Audit Firms and Auditors: Financial Statements

Statutory Audit Directive

Use of audit accounts

There is an equivalence regime for third-country auditors to audit financial accounts for third-country issuers. For a third-country audit firm or auditor to provide the financial accounts for a third-country issuer whose securities are admitted to trading on an EU exchange (subject to limited exceptions), the following conditions must be satisfied:[108]

(a) there is an equivalence decision in respect of the third country to the effect that the audits of the annual or consolidated financial statements are carried out in accordance with international auditing standards and EU requirements or the equivalent thereof; and

(b) registration with the national regulator of the relevant EU exchange.

In the absence of an equivalence decision, a member state may make an equivalence assessment before registering an audit firm or auditor.

Member state oversight

Registered third-country audit firms and auditors may be exempt from being subject to the national regulator's quality assurance system if the firm or auditor has been subject to a quality review in another member state or its own third country, provided that:[109]

(a) an equivalence decision has been made in respect of that third country's quality assurance system;

(b) there is reciprocity from the third country; and

(c) the third country's quality assurance system has carried out a quality review of the third-country auditor or audit entity concerned during the previous three years.

Once an equivalence decision is made, each member state may decide whether to rely on it fully or partially and may disapply or modify the requirements accordingly.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force. Until an equivalence decision is made, a member state may make its own assessment of equivalence or rely on that of another member state. If the European Commission gives a negative equivalence decision, it may allow third-country audit firms and auditors to continue their audit activities under the laws of the relevant member state for a transitional period.	The audited accounts of a UK audit firm or auditor would not be able to be used by UK issuers admitted to trading on an EU (non-UK) exchange if neither equivalence nor oversight is established. If equivalence but not oversight is established, then additional costs of audit would be involved.	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

[108] Article 45(4) to (6), Statutory Audit Directive.

[109] Article 46(1), Statutory Audit Directive.

Annex A: Sectors with Existing Equivalence Regimes (cont.)

Euro Payments

SEPA Rules

There is an equivalence regime that allows non-EEA banks and financial institutions to access SEPA.

Equivalence Decisions

An equivalence decision will only be adopted by the European Payments Council if:[110]

(a) the third country maintains rules that ensure a "legal and regulatory playing field", including maintaining rules equivalent to the PSD, CRD and MLD III and IV;

(b) the third country maintains a functionally equivalent system of competition law; and

(c) the third country has a strong on-going legal relationship with the EU, including "the practice of adoption of EU norms or standards in national legislation in the area of payment services".

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	Access to SEPA is itself an access criterion of other euro payment schemes, such as the EBA Step 2, which provides clearing services for retail payments in euro. Losing access to SEPA would therefore impact on UK financial institutions' ability to provide settlement and euro currency services. Alternatively, firms could establish EEA branches or obtain indirect access through *nostro* arrangements with EU Credit Institution intermediaries. Nostro arrangements may increase costs for end users, but equivalence and branch establishment would not be necessary (see Annex B, "Payment Services".)	**No changes required**. Obtaining equivalence under existing regime would be sufficient.

110 Paragraph 3, SEPA Rules.

Annex B: Sectors That Lack Existing Equivalence Regimes[111]

Table of Contents

Investment Firms

1. Investment Firms and Credit Institutions: Retail Business

Credit Institutions

2. Credit Institutions: Deposit Taking
3. Credit Institutions: Wholesale Lending (Including Trade Finance)
4. Interchange Fees
5. Mortgage Lending: Consumer Credit
6. Mortgage Providers

Market Infrastructure

7. Regulated Markets
8. Data Service Providers
9. Payment & Securities Settlement Systems

Funds

10. UCITS Funds

Insurance

11. Direct Insurance
12. Insurance Mediation

Non-Investment Retail Services

13. E-Commerce
14. Electronic Money Services
15. Payment Services

Other Sectors/Legislation

16. Financial Collateral Arrangements

[111] Where this Annex sets out the position in the investment business context, it does so in light of MiFID II/MiFIR. No third-country equivalence regime is provided for in MiFID. Unless otherwise stated, MiFID is not addressed in this Annex.

Annex B: Sectors That Lack Existing Equivalence Regimes

Investment Firms and Credit Institutions: Retail Business

MiFID II/MiFIR

The MiFID II/MiFIR equivalence regime (see Annex A, "Investment Firms and Credit Institutions: Wholesale Business ") does not allow Third-Country Investment Firms or Third-Country Credit Institutions to provide investment services to retail or elective professional clients (a category including private individuals and most small- and medium-sized enterprises).

Instead, MiFID II gives member states the option of requiring third-country firms intending to provide investment services or perform investment activities with or without ancillary services to retail or elective professional clients to establish a locally-regulated retail branch in that member state.[112] Where member states have chosen to require the establishment of a locally-regulated retail branch, third-country firms may establish a locally-regulated retail branch and thus obtain equivalence-based access for wholesale services across the EU upon the following requirements being satisfied:[113]

(a) the Third-Country Investment Firm or Third-Country Credit Institution requesting access is authorised and subject to supervision in the relevant third country for the services it wishes to carry on in the EU member state;

(b) the third country regulator pays due regard to FATF anti-money laundering and countering terrorist financing recommendations;

(c) cooperation agreements are in place between the relevant third-country regulator and the member state regulator where the branch is to be established;

(d) the branch has sufficient initial capital;

(e) one or more persons are appointed to be responsible for the management of the branch and they all comply with Article 9(1) of MiFID II (provisions on the management body);

(f) tax agreements are in place between the third country that the Third-Country Investment Firm or Third-Country Credit Institution is established in and the member state that the third country is applying to for branch access; and

(g) the third-country firm belongs to an investor compensation scheme.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most provisions of MiFID II/MiFIR will enter into force on 3 January 2018.[114]	MiFID II/MiFIR provides for a limited reverse solicitation exemption to permit Third-Country Investment Firms to provide investment services or activities on the exclusive initiative of a retail or elective professional client established or situated in the EU. Such initiative does not entitle the Third-Country Investment Firm to market new categories of investment products or investment services to that client or other than through the branch if required.[115] Outside this and limited other exemptions, UK firms would not be able to provide investment services to retail or elective professional clients, to the extent that the services or activities are truly cross-border and are locally regulated under a relevant national law. This would require either subsidiarisation or obtaining local licences for local EU branches.	**Extension of MiFID II/MiFIR equivalence regime** for wholesale businesses to cover retail, probably subject to a certain level of additional local (host member state) conduct of business rules (e.g. language and disclosures) compliance.

[112] Article 39(1), MiFID II.

[113] Article 39(2), MiFID II.

[114] Article 93, MiFID II.

[115] Article 42, MiFID II.

Credit Institutions: Deposit Taking

CRD

There is no equivalence regime for Third-Country Credit Institutions to carry out deposit taking or other CRD Activities within the EU.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	Traditionally deposit-taking is not seen as a cross-border activity but one that takes place in the branch receiving the deposit. The European Commission's characteristic performance test[116] means that it is likely that a deposit accepted at an EU branch of a UK bank could be regarded as UK deposit taking activity only if the deposit was intended for and the credit was recorded at the account at the UK institution. The provision of online deposit taking services is also a domestic UK activity; deposits made online by customers located in the EU via a platform provided by a UK institution may be accepted without recourse to a passport in the jurisdiction of the customer. On this basis, UK firms should consider whether they provide deposit taking services for EU customers on a cross-border basis at all. However, some jurisdictions apply a solicitation test to determine whether the consumer or the service provider initiates the relationship. In these jurisdictions, it may be necessary to establish clearly that the customer is initiating the relationship with the UK institution, to ensure that the deposit taking activity is not on a cross-border basis or otherwise subsidiarise.	The MiFID II/MiFIR third-country equivalence regime should be extended to all CRD Activities. In practice, both MiFID Activities and CRD Activities are carried out in the same institution across most of Europe. The UK should offer a similar level of access to EU institutions in return for this.

[116] Commission Interpretative Communication: Freedom to Provide Services and the Interest of the General Good in the Second Banking Directive, 20 June 1997.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Credit Institutions: Wholesale Lending (Including Trade Finance)

CRD

There is no equivalence regime for Third-Country Credit Institutions to carry out wholesale lending or other CRD Activities within the EU.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	As an alternative to direct lending activity, it is already possible for third country entities to purchase sub-participations, bond issuances or even drawn loans from outside the EU. Additionally, in some EU countries, wholesale cross-border lending is unregulated or restricted only in process terms or in relation to marketing issues, where marketing restrictions apply, the MiFID II/MiFIR third-country equivalence regime should mean this is not an issue. Wholesale lending is currently passportable under the mutual recognition provisions of CRD IV. In the absence of an equivalence regime enabling the recognition of third country lenders, UK firms would have to establish a branch or subsidiary in the jurisdiction in which they make wholesale loans.	See Annex B, "Credit Institutions: Deposit Taking" for proposals for an extended combined equivalence regime for CRD Activities and MiFID Activities. It is unlikely that the EU would not plug this gap in the equivalence framework in order to obtain maximum access to the UK's financial institutions balance sheets; not doing so merely adds cost for its borrowers or may dry up sources of much needed funding.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Interchange Fees

Interchange Fee Regulation

There is no equivalence regime for card-based payment transactions from third countries. The Interchange Fee Regulation only applies to card-based payment transactions carried out within the EU, where both the payer's payment service provider and the payee's payment service provider are located in the EU.[117]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	The Interchange Fee Regulation does not apply to transactions between UK payment service providers and EU payment service providers. UK payment service providers are not be subject to the technical and business requirements provided for under the Interchange Fee Regulation, including the cap on fees payable per transaction.	The UK should offer to adopt the Interchange Fee Regulation as part of payment services equivalence. This will ensure that the EU and UK rules are aligned in this area, and that transactions between UK payment service providers and EU payment service providers are undertaken on equal terms.

[117] Article 1(1), Interchange Fee Regulation.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Mortgage Lending: Consumer Credit

CRD IV
CCD
MCD

There is no equivalence regime for Third-Country Credit Institutions to carry out consumer credit business within the EU.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	In the absence of an equivalence regime for mortgage credit or credit intermediaries, a UK bank would have to establish a branch or subsidiary in the jurisdiction in which it grants mortgage credit on a cross-border basis. This branch or subsidiary would only be able to provide services in the jurisdiction in which it is established. UK firms providing these services from EU branches established under the CRD passport may be able to adjust their operating models post-Brexit to provide those services as third country branches, operating wholly under local law, without necessarily limiting the range of services that can be offered to customers in the target EU jurisdiction.	See Annex B, "Credit Institutions: Deposit Taking" for proposals for an extended combined equivalence regime for CRD Activities and MiFID Activities. CCD and MCD equivalence should also be considered as part of the UK exit arrangements. The incomplete harmonisation of consumer protection regimes in the EU means that firms currently passporting mortgage finance and consumer credit are already effectively required to comply with the local legal frameworks of the countries in which they are providing services. The value of a new equivalence regime would therefore not be as complete for the sector as for some other regimes.

Mortgage Providers

MCD

There is no equivalence regime for third country mortgage intermediaries to provide mediation services across the EU. The MCD does not establish passport rights for mortgage lending, which most lenders carry out under their CRD passport.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	UK credit intermediaries would no longer be able to provide services throughout the EEA on the basis of the MCD passport. UK credit intermediaries would need to establish an EU presence, authorised in accordance with MCD, to regain access to the passport.[118] Alternatively, a third-country firm may enter into an agreement with a duly-registered EU credit intermediary under which that firm becomes an "appointed representative" of that intermediary.[119] Appointed representatives may provide credit intermediation throughout the EU in those member states which allow appointed representatives to operate.[120]	An equivalence regime should be prioritised (see Annex B, "Mortgage Lending: Consumer Credit".)

118 Article 29(2) MCD.

119 Article 31(1), MCD.

120 Article 32(2), MCD.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Regulated Markets

MiFID II/MiFIR

The MiFID II/MiFIR equivalence regime for trading venues (see Annex A, "Trading Venues: Trading Obligation") does not permit third-country firms to act as market operators of regulated markets.[121]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most provisions of MiFID II/MiFIR will enter into force on 3 January 2018.[122]	Third country market operators would be subject to state by state authorisation to access EU established customers.	A broadened equivalence regime should be established to enable UK market operators to establish EU regulated markets. This would also be consistent with the equivalence regime already in place that, for the purposes of discharging the MiFID II/MiFIR trading obligation, permits EU Investment Firms to trade shares and non-equity instruments on equivalent third country venues.

[121] Operating an MTF/OTF is a MiFID Activity (Annex I (8) and (9), MiFID II). Being a market operator of a regulated market is not an investment service. The MiFID II/MiFIR equivalence regime allows Third-Country Investment Firms and Third-Country Credit Institutions to provide investment services to eligible counterparties and *per se* professional clients. A third-country firm could therefore operate an MTF/OTF (although this would be difficult in practice without the establishment of a branch), but not a regulated market.

[122] Article 93, MiFID II.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Data Service Providers

MiFID II/MiFIR

The MiFID II/MiFIR equivalence regime for trading venues (see Annex A, "Trading Venues: Trading Obligation") does not permit third country data services providers to act as "approved reporting mechanisms" or "approved publication arrangements" or "consolidated tape providers".[123]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
Most provisions of MiFID II/MiFIR will enter into force on 3 January 2018.[124]	UK data service providers will not be able to provide these reporting services for EU-regulated firms that validly satisfy the obligations of EU Investment Firms under MiFID II/MiFIR. The same applies in relation to UK consolidated tape providers.	A third country equivalence scheme should be prioritised for these sectors. This would allow UK data services providers to provide MiFID II/MiFIR-compliant reporting services to EU Investment Firms. The same also applies to UK consolidated tape providers. Without an equivalence regime in place, UK data services providers and consolidated tape providers will need to establish EU-authorised subsidiaries to provide MiFID II/MiFIR-compliant services to EU Investment Firms and EU trading venues.

[123] Under Article 59(2), MiFID II.

[124] Article 93, MiFID II.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Payment & Securities Settlement Systems

SFD

There is no equivalence regime allowing a third-country firm to carry out payment and securities settlement services within the EU.

However, a settlement system that is located in a third country may become a "designated system" under the SFD if the system is governed by the law of an EU member state as chosen by its participants.[125] The participants may only choose the law of a member state in which at least one of them is headquartered.[126]

The SFD may be applied by EU member states to domestic institutions (including EU Investment Firms and EU Credit Institutions) that participate in third country systems.[127]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	As there is no equivalence regime incorporated into the SFD, UK settlement and payment systems would not be entitled to the same EU-wide protections that EU systems have.	A new equivalence regime should be pursued whereby a third country's payment and settlement systems could be recognised. The absence of such a regime is an anomaly related to the age of this legislation. UK payment and settlement systems already have stronger protections than those under the SFD pursuant to national laws (Companies Act 1989 and EMIR). SFD protection would be a helpful addition to allow EU entities to use UK market infrastructure and *vice versa*, to protect EU settlement systems with UK users. Maintaining existing SFD designations would require UK-based designated systems to change the governing law of the rules of their systems to EU member state law and relocating, so is impracticable.

[125] For example, SIX x-clear is a designated system under the SFD, although it is located in Switzerland.

[126] Article 2(a), SFD.

[127] Recital 7, SFD.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

UCITS Funds

UCITS Directive

There is no equivalence regime under the UCITS Directive.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	Upon exiting the EU, UK UCITS funds would cease to be governed by the UCITS Directive. UK funds that were previously considered UCITS funds, upon exit, would be treated in EEA countries as AIFs governed by AIFMD. As mentioned in Annex A, "Funds", there is scope for non-EEA AIFMs to market into the EEA and also for sub-delegation of portfolio management to the UK. It is also currently possible for a UK fund manager to act, under delegation, as a day-to-day portfolio manager of an EEA (non-UK) UCITS fund. Such a UCITS fund would need (if it does not have one already) to have an EEA-domiciled management company or be self-managed, to continue as a UCITS fund – a structure that is already well-used in the funds industry. Finally, for UK managers already operating under delegation from an EEA management company of an EEA UCITS or from a self-managed EEA UCITS, it is likely that nothing would change.	A new equivalence framework for UCITS should be prioritised, to avoid unintended consequences of the AIFMD equivalence regime instead applying.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Direct Insurance

Solvency II

There is a limited equivalence regime for third country firms to carry out direct insurance activities in the EU. The regime only covers consolidated supervision and does not allow for any customer access (see Annex A, "Insurers and Reinsurers: Group Supervision").[128]

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
The majority of Solvency II applied from 1 January 2016.[129]	A UK insurer would need to establish an EU-regulated direct insurance subsidiary, or alternatively insure a UK-based affiliate of the client, if it wanted to insure an EU client.	A new equivalence regime based on that available in other sectors should be pursued. Without this, a UK direct insurer could consider establishing either an insurance mediation (marketing) firm in Europe or a pass-through vehicle that reinsures risks back to a UK head office (depending on the EU country where customers are located). Reinsurance is discussed in relation to the limited third-country equivalence regime in Annex A, "Reinsurers".

[128] Article 260, Solvency II.

[129] Article 311, Solvency II.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Insurance Mediation

IMD
IMD II

There is no equivalence regime for third country firms to carry out insurance mediation activities (e.g. insurance advice or sales) within the EU.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
IMD is in force. IMD II must be transposed by 23 February 2018 and will repeal and replace IMD.[130]	Insurance and reinsurance sales and distribution by UK entities in the EU provided on the basis of the IMD passport would need to take place through an EU presence authorised in accordance with IMD.[131] Alternatively, third country firms could act solely as tied insurance intermediaries registered by EU insurance undertakings in the member states in which those insurers are established.[132]	An equivalence regime will need to be established and should be prioritised, to avoid subsidiarisation costs. Doing so is likely also to ameliorate the situation for direct insurance under the national laws of many member states, so should be a priority.

130 Article 42(1), IMD II.

131 Article 3(1), IMD/IMD II.

132 Article 3(1) IMD/IMD II.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

E-Commerce

ECD

There is no equivalence regime for third country firms to carry out e-commerce activities within the EU.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	UK institutions' ease of e-commerce supply would be affected. When dealing in the EU, UK institutions would likely need to adhere to contractually binding terms that reflect the ECD. The ECD's recitals state that the directive does not apply to services supplied by service providers established in a third country, nonetheless the ECD states that where a service provider is regarded as established is determined by the "centre of… activities relating to [a] particular service".[133] Applicability of the ECD provisions is therefore a matter of fact, and as a result, UK institutions may still have to comply with ECD standards. Without a scheme of negotiated mutual recognition, the UK could be subject to additional requirements imposed by individual member states on activities of UK-established information services providers in addition to other areas where the UK would no longer have the rights or protections against barriers that it would have had as a member state.	Consider a new equivalence regime, to enable UK and EU institutions' ability to continue to do business under existing arrangements. This should include, inter alia, extension of certain protections to UK established service providers as "mere conduits" and for "caching" and hosting services.[134]

[133] Recital 40, 58, 19, ECD.

[134] Articles 12-14, ECD.

Electronic Money Services

EMD II

There is no equivalence regime for third-country firms to perform electronic money services within the EU.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	Without an equivalence regime in place, any UK-authorised electronic money institutions would no longer be able to provide passported electronic money and payment services into the EEA.[135] Establishment of a local subsidiary may be necessary. EMD II states that electronic money institutions issuing electronic money should not be regarded as a deposit-taking activity, and it is therefore unclear whether the cross-border analysis as applies to deposit-taking is applicable here.[136]	In reality, firms may choose not to use EMD II, for example if they are already authorised to issue electronic money as EU Credit Institutions under CRD,[137] so this may not be a material omission in the equivalence framework. However, this equivalence gap would be best remedied as part of any package.

135 Article 3(1), EMD II.

136 Article 13, EMD II.

137 Article 25, EMD II.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Payment Services

PSD
PSD II

There is no equivalence regime for third-country payment services firms to carry out payment services within the EU.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
PSD is in force. PSD II must be transposed by EU member states by, and will apply from, 13 January 2018.[138]	Payments services providers operating cross border would not be able to provide passported payment services without an alternative EU-regulated affiliate. Where a UK institution seeks to provide services under the EU, particularly euro, (see Annex A, "Euro Payments".) Payment services are often not cross-border under English law. Deposit-taking is historically regarded as being provided at the relevant bank branch offering the payment services. Where local EU regimes regard cross-border activity as taking place, UK payment services providers would need to restructure themselves so that the service is provided by updating the books and records of the UK institution. Otherwise, UK authorised payment services institutions would have to establish separate legal entities regulated in an EU member state or adopt a licensing model with an EU-authorised payment services firm.	A new equivalence regime should be established. It ought to be the case that the EU will permit UK institutions operating under equivalent standards to continue to provide services in those systems, since otherwise the liquidity and robustness of the systems will be significantly impaired and unnecessary additional costs would be introduced for euro payments through use of affiliates and back-to-back trades.

[138] Article 115, PSD II.

Annex B: Sectors That Lack Existing Equivalence Regimes (cont.)

Financial Collateral Arrangements

FCD

There is no equivalence regime with respect to financial collateral arrangements.

Current Status And Any Transitional Period	Consequences Of Failure To Achieve Equivalence	Proposed Additions To Equivalence
In force.	The FCD imposes harmonised European minimum requirements for member states to incorporate in local legal systems for certain financial collateral arrangements. The minimum protections in the FCD (that are required to be implemented by member states) are not limited to EU established counterparties with the effect that the FCD's requirements (wherever locally implemented) apply whenever a collateral arrangement is subject to the laws of a member state that has transposed the FCD. In order to achieve harmonised treatment of financial collateral arrangements, the UK would not have to ask for an expanded equivalence regime to be included in EU law. The regulated activity of entering into financial collateral arrangements with EU counterparties will be dealt with under other EU equivalence regimes under MiFID II/MiFIR. The UK should continue to recognise and enforce financial collateral arrangements and disapply normal insolvency proceedings in respect of financial collateral arrangements.	Current protections in UK law (and recognising protections under the FCD) should be maintained. No equivalence advocacy is required. The UK Financial Collateral Regulations provide such protections to collateral takers and providers that are non-natural persons including entities constituted under the law of a country outside the UK, reflecting the territory neutral protection required by the FCD. So long as other member states have implemented the FCD along the same standards required by the FCD, UK banks can still benefit from the same FCD protections as third country institutions.

Annex C: Summary of Equivalence Decisions

Full equivalence decision	F
Transitional equivalence decision	T
Partial equivalence decision	P

EQUIVALENCE DECISIONS		Abu Dhabi	Argentina	Australia	Bermuda	Brazil	Canada	Caymans	China	DIFC	Egypt	Guernsey	Hong Kong	India	Indonesia	Isle of Man	Israel	Japan	Jersey	(South) Korea	Malaysia	Mauritius	Mexico	Monaco	New Zealand	Russia	Saudi Arabia	Singapore	South Africa	Switzerland	Thailand	Taiwan	Turkey	US
Accounting Standards For Prospectus	Third country GAAP with IFRS						F		F									F		F														F
Accounting Standards For Consolidated Reporting	Third country GAAP with IFRS						F		F									F		F														F
AIFMD	Alternative Investment Fund Managers — EU/non-EU AIFs																																	
Benchmark Regulation	Benchmark administrator - use of benchmark within the EU																																	
Credit Rating Agencies Regulation	Credit rating agencies-use of ratings within the EU		F	F		F	F						F					F					F					F						F
CRR	Credit institutions - Article 107(4)			F		F	F		F			F	F	F		F		F	F				F	F			F	F	F	F				F
	Investment firms - Article 107(4)			F		F	F		F				F		F			T 139		F			F				F	F	F					F
	Exchanges - Article 107(4)			F		F	F		F					F	F			F		F			F				F	F	F					F
	Exposures to central governments, central banks, regional governments, local authorities and public sector entities			F		F	F		F			F	F	F		F		F	F				F	F			F	F	F	F				F
	Credit institutions - Article 142			F		F	F		F			F	F	F		F		F	F				F	F			F	F	F	F				F
	Investment firms - Article 142			F		F	F		F				F		F			T 140		F			F				F	F	F					F

139 Japan's investment firms' regime is limited to Type I Financial Instruments Business Operators.

140 *Ibid.*

EQUIVALENCE DECISIONS		Abu Dhabi	Argentina	Australia	Bermuda	Brazil	Canada	Caymans	China	DIFC	Egypt	Guernsey	Hong Kong	India	Indonesia	Isle of Man	Israel	Japan	Jersey	(South) Korea	Malaysia	Mauritius	Mexico	Monaco	New Zealand	Russia	Saudi Arabia	Singapore	South Africa	Switzerland	Thailand	Taiwan	Turkey	US
	Calculation of own funds requirements																																	
CRR And CRD IV	Group consolidated supervision																																	
CSD Regulation	CSDs																																	
EMIR	Regulated markets																																	F
	Transaction requirements																																	
	CCPs			F			F [141]						F					F		F			F					F	F	F				P [142]
	Trade repositories																																	
	CCPs - reporting of initial margin																																	
EMIR — Margin for Uncleared Swaps	Banks prudential and supervisory arrangements on a consolidated basis																																	
	Banks supervisory and regulatory prudential arrangements																																	
MiFIR / MIFID II	Trading venues - trading obligation for derivatives and shares																																	
	Derivatives. trade execution and clearing obligations																																	
	Trading venues - clearing access																																	
	Trading venues and CCPs-access to benchmarks and licences for the purposes of clearing and trading obligation																																	
	Investment firms providing investment services to EU professional clients and eligible counterparties																																	
	Regulated markets-																																	

141 The decision for Canada relates to the Canadian provinces of Alberta, British Columbia, Manitoba, Ontario and Quebec.

142 The US CCP regime is limited the framework of the Commodity Futures Trading Commission.

EQUIVALENCE DECISIONS		Abu Dhabi	Argentina	Australia	Bermuda	Brazil	Canada	Caymans	China	DIFC	Egypt	Guernsey	Hong Kong	India	Indonesia	Isle of Man	Israel	Japan	Jersey	(South) Korea	Malaysia	Mauritius	Mexico	Monaco	New Zealand	Russia	Saudi Arabia	Singapore	South Africa	Switzerland	Thailand	Taiwan	Turkey	US
	exemption for investment firms from certain appropriateness & suitability rules																																	
SFTR	Trade repositories																																	
	Transaction requirement																																	
SSR	Requirements for markets																																	
Solvency II	Third-country reinsurers in the EU. equivalent treatment of their activities and of EU reinsurers' activities				F													T												F				
	EU insurers and reinsurers in third countries. equivalence of third-country solvency rules for calculation of capital requirements and own funds			T	P / T	T	T											T					T							F				T
	Third-country insurers and reinsurers in the EU - equivalence of group supervision by the third-country supervisory authorities				P																									F				
Statutory Audit	Audit firms and auditors	F		F		F	F		F	F		F			F	F		F	F	F	F		F		F			F	F	F	F	F	F	F
	Audit firms and auditors - transitional period				T			T			T											T			T	T							T	

Annex D: Glossary of Terms Used

Term	Meaning
	Legislation
AIFMD	Alternative Investment Fund Managers Directive (Directive 2011/61/EU)
Benchmark Regulation	Benchmark Regulation (Regulation (EU) 2016/1011)
CCD	Consumer Credit Directive (Directive 2008/48/EC)
CRA Regulation	CRA Regulation (Regulation (EC) 1060/2009) as amended by CRA Regulation II (Regulation (EC) 513/2011) and CRA III Regulation (Regulation (EU) 462/2013)
CRD	Capital Requirements Directive (Directive 2013/36/EU) and Capital Requirements Regulation (Regulation (EU) 575/2013)
CRD IV	Capital Requirements Directive (Directive 2013/36/EU)
CRR	Capital Requirements Regulation (Regulation (EU) 575/2013)
CSD Regulation	Central Securities Depositories Regulation (Regulation (EU) 909/2014)
ECD	Electronic Commerce Directive (Directive 2000/31/EC)
EMD II	Electronic Money Directive II (Directive 2009/110/EC)
EMIR	European Market Infrastructure Regulation (Regulation (EU) 648/2012)
FCD	Financial Collateral Directive (Directive 2002/47/EC)
IAS Equivalence Mechanism Regulation	IAS Equivalence Mechanism Regulation (Regulation (EC) No 1569/2007)
IAS Regulation	International Accounting Standards Regulation (Regulation (EC) No 1606/2002)
IMD	Insurance Mediation Directive (Directive 2002/92/EC)
IMD II	Insurance Mediation Directive II (Directive 2016/97/EC)
Interchange Fee Regulation	Interchange Fee Regulation (Regulation (EU) 2015/751)
MAR	Market Abuse Regulation (Regulation (EU) 596/2014)
MCD	Mortgage Credit Directive (Directive 2014/17)
MiFID	Markets in Financial Instruments Directive (Directive 2004/39/EC)
MiFID II	Markets in Financial Instruments Directive (Directive 2014/65/EU)
MiFIR	Markets in Financial Instruments Regulation (Regulation (EU) 600/2014)
MLD III	Third Money Laundering Directive (Directive 2005/60/EC)
MLD IV	Fourth Money Laundering Directive (Directive (EU) 2015/849)
Prospectus Directive	Prospectus Directive (Directive 2003/71/EC)
Prospectus Regulation	Proposal for a Regulation of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading, adopted by the European Commission on 30 November 2015
PSD	Payment Services Directive (Directive 2007/64/EC)

Term	Meaning
PSD II	Payment Services Directive II (Directive 2015/2366/EU)
RTS on Margin for Uncleared OTC Derivatives	Regulatory Technical Standards for Risk-Mitigation Techniques for OTC Derivatives Not Cleared by a Central Counterparty, adopted by the European Commission on 4 October 2016
Second Banking Directive	Second Banking Directive (Directive 89/646/EEC)
SEPA Rules	Criteria for Participation in the SEPA Schemes for Communities of Banks or Financial Institutions outside the European Economic Area, EPC061-14
SFD	Settlement Finality Directive (Directive 98/26/EC)
SFTR	Securities Financing Transactions Regulation (Regulation (EU) 2015/2365)
Solvency II	Solvency II Directive (Directive 2009/138/EC)
Solvency II Delegated Regulation	Solvency II Delegated Regulation (Commission Delegated Regulation 2015/35)
SSR	Short Selling Regulation (Regulation (EU) No 236/2012)
Statutory Audit Directive	Statutory Audit Directive (Directive 2006/43/EC)
Transparency Directive	Transparency Directive (Directive 2004/109/EC)
UCITS Directive	Undertakings for Collective Investment in Transferable Securities Directive (Directive 2014/91/EU)
Other Definitions	
AIF	Alternative Investment Fund
AIFM	Alternative Investment Fund Manager
Basel Committee	Basel Committee on Banking Supervision
Brexit	Brexit
CCP	Central Counterparty
CFTC	Commodity Futures Trading Commission
Council	Council of the European Union
CJEU	Court of Justice of the European Union
CRA	Credit Ratings Agency
CRD Activities	The list of activities set out in Annex I to CRD IV
CSD	Central Securities Depository
DIFC	Dubai International Financial Centre
EBA	European Banking Authority
EEA	European Economic Area
Elective professional clients	Under MiFID and MiFID II/MiFIR, public sector bodies, local public authorities, municipalities and private individual investors may opt to be treated as professional clients either generally or for a particular service or transaction. The EU Investment Firm will need to assess the expertise, experience and knowledge of its client including whether the client satisfies at least two of the following requirements. (i) the client has traded significantly ten times on average in last four quarters; (ii) has cash and investments exceeding EUR 0.5 million; and (iii) has been a financial

Term	Meaning
	services professional for over a year
Eligible counterparty	Under MiFID and MiFID II/MiFIR, EU Credit Institutions, EU Investment Firms, insurers, asset managers, funds, other institutional investors, other EU regulated firms, national governments, central banks, supranational organisations and non-EU equivalent regulated entities as well as commodity dealers and large companies consenting to be treated as an eligible counterparty
EIOPA	European Insurance and Occupational Pensions Authority
EP	European Parliament
ESA	European Supervisory Agency
ESMA	European Securities and Markets Authority
ETD	Exchange-traded derivative
EU	European Union
EU Credit Institution	A credit institution, as defined in point (1) of Article 4(1) of the CRR
EU Investment Firm	An investment firm authorised and supervised in accordance with MiFID or MiFID II
FATF	Financial Action Task Force
FCA	Financial Conduct Authority
FSB	Financial Stability Board
GAAP	Generally Accepted Accounting Principles
IFRS	International Financial Reporting Standards
IOSCO	International Organization of Securities Commissions
ISDA	International Swaps and Derivatives Association
MiFID Activities	The investment services and activities and ancillary services listed in Sections A and B of Annex I to MiFID or, from the date on which MiFID II enters into force, MiFID II
MTF	Multilateral Trading Facility
NCCT	Non-Cooperative Countries or Territories
OTC	Over-the-counter
OTF	Organised Trading Facility
***Per se* professional clients**	Under MiFID and MiFID II/MiFIR, EU Credit Institutions, EU Investment Firms, insurers, asset managers, funds, commodity dealers, other institutional investors, non-EU equivalent entities; national and regional governments, central banks, bodies managing public debts, international and supranational institutions; large companies and other institutional investors whose main activity is to invest in financial instruments including those that mostly securitise assets and finance transactions
PRA	Prudential Regulation Authority
QCCP	Qualifying Central Counterparty
QMV	Qualified majority voting
Retail clients	Under MiFID and MiFID II/MiFIR, clients that are not professional clients
RTS	Regulatory Technical Standards

Term	Meaning
SEPA	Single Euro Payments Area
TFEU	Treaty on the Functioning of the European Union
Third-Country Credit Institution	A firm that would be a credit institution providing investment services or performing investment activities if its head office or registered office were located within the EU
Third-Country Investment Firm	A firm that would be an EU Investment Firm if its head office or registered office were located within the EU
UCITS	Undertakings for Collective Investment in Transferable Securities
UK	United Kingdom
US	United States of America

Subscribe to Politeia's Publication!

For £35 a year (£30 standing order) you will receive an electronic copy of each of our publications, plus hard copies of two new publications on request, and, if you wish, free hard copies of your choice from our back catalogue. You will also receive advance notice and invitations to Politeia's conferences and flagship events, with guest speakers from the UK and overseas.

More information can be found on our website: www.politeia.co.uk. Or, write to the Secretary, Politeia,14a Eccleston Street, London, SW1W 9LT or at secretary@politeia.co.uk

A Selection of Recent and Related Publications

Trading Places: Consumers v Producers in the New Brexit Economy
Patrick Minford

How to Leave the EU: Legal and Trade Priorities for the New Britain
Martin Howe

Ruling the Ruler: Parliament, the People and Britain's Political Identity
Sheila Lawlor

Joining the World: Britain Outside the EU
Nigel Lawson

Banking on Recovery: Towards an accountable, stable banking sector
J. McFall, S. Kamall, G. Lyons, F. Capie and others

Dumbing Down the Law – The SRA's Proposals for Legal Education
Anthony Bradney

The British Bill of Rights: Protecting Freedom Under the Law
Jonathan Fisher

Paying for the Future: Working Systems for Healthcare and Pensions
Ludger Schuknecht, Matthias Dauns, Werner Ebert

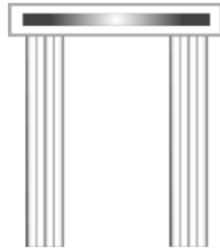
Working Welfare: Contributory Benefits, the Moral Economy and the New Politics
Frank Field

Financial Sector and the UK Economy: The Danger of Over-Regulation
McFall, Matthews, Minford, Green, Dannhauser, Hodgson, Cochrane, Smith, George

History in the Making: The New Curriculum, Right or Wrong
David Abulafia, Jonathan Clark, Robert Tombs

University Diversity: Freedom, Excellence and Funding for a Global Future
Martin Rees

Nuclear Options: Powering the Future
Roger Cashmore, David Mowat, Simon Taylor



As Britain prepares to leave the EU, the spotlight has switched to the UK's financial services. What course will enable this pivotal sector, with the City as its hub, to maintain and extend its global lead? What policy is best to promote trade with the EU and globally, while also attracting business and investment to the UK?

In *A Blueprint for Brexit: The Future of Global Financial Services and Markets in the UK*, Barnabas Reynolds shows that Brexit will bring many opportunities to financial services. The author, a UK and EU regulatory lawyer working across the sector, explains that the gains from no longer being subject to the regulatory requirements of the EU could be considerable. Moreover, much if not all of the current activity will be unaffected if passporting is replaced by other arrangements for mutual EU-UK access.

Reynolds analyses the options for continued free trade for financial services. The equivalence arrangements already in place for US trade with the EU are one option, particularly if they are expanded and a procedural process is put in place for maintaining equivalence in the future. Alternatively, a "Financial Centre" model would allow the UK to establish a market-friendly regulatory framework, set in accordance with global standards and best practices.

Both models presented would permit some removal and reworking of EU laws in the UK. They would also allow the UK to do what it has always done best: lead the world in financial services as a champion of free trade and market competition under the rule of law.

POLITEIA