

### Brexit Statutory Instruments – a series of briefings

November 2018

## The EEA Passport Rights (Amendment, etc, and Transitional Provisions) (EU Exit) Regulations 2018

This paper is part of a series of briefings for clients and contacts of Allen & Overy on the review of financial services statutory instruments (SIs) to be laid down under the European Union (Withdrawal) Act 2018 (the **Withdrawal Act**).

### Introduction

In June 2018, the UK Parliament passed the **Withdrawal Act** which will repeal the European Communities Act 1972 and convert existing EU law into UK domestic law following the UK's exit from the EU. The purpose of the Withdrawal Act is “to provide a functioning statute book on the day [the UK] leave[s] the EU”. The Act gives temporary powers to UK ministers to correct deficiencies in EU laws retained as UK law on exit day through secondary legislation. These powers will be used extensively in the financial services space to ensure that UK domestic laws can function independently of EU laws after Brexit.

On 5 September 2018, HM Treasury laid before Parliament the EEA Passport Rights (Amendment, etc, and Transitional Provisions) (EU Exit) Regulations 2018 (the **TPR SI**). The SI provides for a temporary permissions regime (**TPR**) that will allow passported EEA firms operating in the UK to continue their activities for a limited period after the UK's exit from the EU. In the event of a ‘hard’ Brexit, the TPR will extend the current regulatory regime to allow passported EEA firms (operating in the UK either on a cross-border or branch basis) to continue operating whilst allowing sufficient time for such firms to obtain full UK authorisation after Brexit.

The SI will not come into effect should the UK and EU agree a transitional period<sup>1</sup> that extends the status quo until a later time.<sup>2</sup>

### What does the TPR SI do?

It seeks to provide a backstop that ensures the continued provision of services by EEA firms in the UK, were the UK and EU to fail to come to an agreement on a withdrawal deal by 29 March 2019. It therefore assumes that there will be no cooperation with EU authorities.

In the event of a ‘hard’ Brexit, EU laws applicable to activities conducted in the UK by passported EEA firms will cease to apply. This would include the loss of passporting rights. To fill this void, the TPR will provide temporary relief to allow EEA firms to be authorised with permission to continue operating in the UK after exit day for a transitional period. The precise impact of the TPR will vary depending on the area of regulation, and we set out some of the key areas below.

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<sup>1</sup> Referred to by the UK Government as ‘implementation period’.

<sup>2</sup> In March 2018, the UK and EU negotiators have agreed in principle to an implementation period to last until 31 December 2020.

### Authorisation to provide services in the UK after Brexit

In order to take advantage of the TPR, prior to exit day EEA firms will be required to notify the relevant UK regulator of their intention to be within the regime. The FCA has indicated that it will provide a window from January until late March 2019 for firms to submit the appropriate notifications online. Firms that do not submit a notification will not be able to rely on the TPR. Authorisation applications submitted before the TPR SI is in force will be sufficient to get firms within the regime (as long as such applications have not been withdrawn by the firm or accepted/rejected by the relevant regulator prior to exit day).

Thereafter, firms in scope of the TPR will be provided with a three-month 'landing slot'<sup>3</sup> during which they will need to submit a full authorisation or variation of permission application,<sup>4</sup> and the regulators will have up to three years<sup>5</sup> after exit day to determine the outcome of such applications.<sup>6</sup>

The TPR will cease to apply to a firm on the earlier date of when the firm obtains a full authorisation, if the application is withdrawn by the firm or rejected by the regulators, or the end of the transitional period of three years from exit day (this is capable of an extension by HM Treasury of up to one year).

### Applicable regulation

As the EEA passport falls away, passported EEA firms will become subject to the UK rules applicable to third-country firms on exit day. This will be a significant change of ruleset. In order to maintain the status quo, UK regulators have expressed willingness to take a proportionate approach to compliance with UK rules on Day 1 – for example, the FCA has indicated that it will accept some level of 'substituted compliance' in respect of rules currently reserved to the home state,<sup>7</sup> as long as firms can demonstrate their continued compliance with the equivalent home state rules in respect of their UK business. The regulators are expected to consult on how they propose to deal with applying UK rules to TPR firms in the autumn.

### Approvals for senior managers/approved persons

It remains to be seen how the requirements relating to individuals performing senior management/controlled functions will apply to TPR firms. The FCA has stated that firms operating through a branch would be subject to the approved persons regime as it currently applies throughout the TPR and then the senior managers and certification regime (**SM&CR**) once the requirements come into force. The PRA appears to be requiring EEA banks to comply with the SM&CR as it applies to third-country firms from exit day. Firms operating on a cross-border basis without a branch will not be brought into the scope of the approved persons regime or SM&CR during the TPR.

### Compensation schemes

The PRA and the FCA have confirmed that the UK Financial Services Compensation Scheme (**FSCS**) membership will be extended to firms that operate through a branch in the UK.<sup>8</sup> Firms that do not operate through a branch will not have access to the FSCS (other than in certain limited circumstances).

### Requirements imposed by home state regulators

Any requirements imposed on a passported EEA firm by a home state regulator before exit day will be preserved after exit day during the TPR as if they have been imposed by the PRA or the FCA.

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<sup>3</sup> The first 'landing slot' is likely to be October to December 2019, and the last – January to March 2021.

<sup>4</sup> Depending on whether the firm operates in the UK with or without a top-up permission.

<sup>5</sup> HM Treasury will have the right to extend this period multiple times by up to 12 months each time.

<sup>6</sup> TPR SI will temporarily increase the statutory periods for the regulators to determine the outcome of applications for authorisation, including in respect of outstanding applications by passported EEA firms within to take advantage of the TPR that are not determined by the UK regulators before exit day.

<sup>7</sup> With the exception of capital requirements, where the FCA is not proposing to apply home state rules.

<sup>8</sup> EEA insurers that currently operate in the UK through an EEA passport but without a branch will retain their existing FSCS membership. The same applies to EEA managers of UK authorised funds (as they are also already members of FSCS).

### Main legislation amended by the TPR SI<sup>9</sup>

Financial Services and Markets Act 2000 (**FSMA**)

Building Societies Act 1986

Bank of England Act 1998

Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

### Areas identified by industry as requiring further consideration

The precise impact of the TPR will depend on the final wording of the TPR SI and the rules published by the FCA and PRA. For example, HM Treasury and the regulators are yet to specify:

- the process for EEA firms to notify the regulators of their intention to take advantage of the TPR
- the extent to which, and when, EEA firms will need to comply with the revised UK regulatory ruleset post Brexit (eg whether substituted compliance with home state regulations will be acceptable and, if so, for how long and under what circumstances)
- the interaction of the TPR SI with other SIs, for example the expected (but yet unpublished) SI on contractual continuity

### What does this mean for you?

In the event of a ‘hard’ Brexit, passported EEA firms which need authorisation to continue to provide services in the UK will, as a minimum, need to submit notification to the UK regulators to continue operating within the TPR after exit day.

The precise impact of the TPR will depend on the final wording of the SI and the rules published by the FCA and PRA. Until such time, EEA firms should continue to prepare for Brexit (including any changes to the regulatory ruleset) and monitor developments in the UK and EU.

### Next steps

HM Treasury consulted the initial draft TPR SI (published in July 2018) with industry bodies, and the final draft was laid before Parliament on 5 September 2018; however, it has not been scheduled for consideration in Parliament for a specified date.<sup>10</sup> The FCA and the PRA are expected to consult on changes to their rulebooks relating to the TPR in autumn.

The FCA encourages all passported EEA firms to complete an [online survey](#) to the extent they have not already done so.

We will continue to monitor developments and publish further updates once authorities provide further clarity on the post-Brexit regulatory landscape for passported EEA firms.

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<sup>9</sup> The Schedule to the TPR SI contains lists of primary and secondary legislation that the SI amends – predominantly by removing references to the relevant sections of FSMA that underpin the EEA passporting framework in the UK (ie Section 31(1)(b) and (c) and Schedules 3 and 4 to FSMA).

<sup>10</sup> As at 11 September 2019, it has been provisionally set for consideration on 23 November 2018, though it has been acknowledged that this will not be the actual date when Parliament will consider the TPR SI. See <https://publications.parliament.uk/pa/cm201719/cmagenda/fb180911.htm> (last checked on 13 September 2018).

## Your Allen & Overy contacts

For further information please speak to:

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