

## Regulatory News Alert

### Convergence tool to support national competent authorities in the context of Brexit relocation

21 July 2017

ESMA's opinion setting out general principles aimed at fostering consistency in authorization, supervision and enforcement related to the relocation of entities, activities, and functions from the UK

#### Context

Following the notification of the United Kingdom (UK) to the European Council (EC) of its intention to leave the European Union (EU) in March 2017, many UK-based financial actors have been considering to set a foot on the European continent to continue to benefit from the EU passport and access the Single Market.

In anticipation of an increasing number of authorization requests and supervision of relocated entities, activities and functions from the UK to the remaining EU member states, the ESMA has published an [opinion](#), setting out nine general principles to be used as a practical tool supporting supervisory convergence in the context of Brexit. They aim at mitigating supervisory arbitrage risks related to the conditions for authorization as well as for the outsourcing and delegation of activities.<sup>1</sup>

<sup>1</sup>It is worth mentioning that these principles have been drafted on the assumption that the UK will become a third country following its withdrawal from the EU, notwithstanding a potential specific arrangement that may arise from the negotiations between the UK and the EU.

#### Principle 1: No automatic recognition of existing authorizations

While the EU legislative framework for financial markets remains applicable in the UK until the moment it leaves the EU, there is no automatic recognition of the authorization granted by the UK regulator into the remaining EU member states. Any entity established in a third country (i.e., potentially the UK following Brexit) wishing to benefit from the EU passport is required to have a presence in one of the EU27 member states, and EU National Competent Authorities (NCAs) will remain responsible for granting authorization to EU entities.

## **Principle 2: Authorizations granted by EU27 NCAs should be rigorous and efficient**

Approval should be granted only after a thorough evaluation to ensure that all conditions and legislations have been met by the applicant from day one (inter alia the governance structure, human and technical resources, geographical distribution of activities, outsourcing, and delegation arrangements).

## **Principle 3: NCAs should be able to verify the objective reasons for relocation**

In their assessment to authorize relocation from the UK, NCAs should pay particular attention to the rationale and objectives pursued by the applicant by obtaining exhaustive information on the future geographical distribution: the targeted clients and the location of development of products or services. This is to avoid that the choice was driven by evading stricter standards in force in other member states.

## **Principle 4: Special attention should be granted to avoid letter-box entities in the EU27**

NCAs should reject any application involving the creation of a letter-box entity where, for instance, extensive use of outsourcing and delegation is foreseen with the intention of benefitting from the EU passport, while essentially performing all substantial activities or functions outside the EU27.

## **Principle 5: Outsourcing and delegation to third countries is only possible under strict conditions**

To complement principle 4, outsourcing or delegating tasks or functions is permitted when all conditions are met, and in no case should it preclude a transfer of responsibilities from a market actor engaged in an outsourcing or delegation arrangement to the delegate. The applicants must therefore prove that they retain the ability to direct, control, and supervise outsourced or delegated functions.

## **Principle 6: NCAs should ensure that substance requirements are met**

NCAs should not allow outsourcing or delegation arrangements that may impede their aptitude to supervise: therefore NCAs must receive adequate and accurate information from applicants to properly evaluate and supervise them. In addition, NCAs must ensure that core activities and functions key to the proper functioning of regulated entities are not outsourced or delegated, or at least that the applicant entity foresees sufficient substance for decision making.

## **Principle 7: NCAs should ensure sound governance of EU entities**

Applicants must prove to comply with governance requirements and ensure that the authorized management and board members are fit and proper to perform their functions. In this context, NCAs should not only assess the knowledge and experience of board and executive members, but also dedicate time foreseen to carry out their responsibilities.

## **Principle 8: NCAs must be in a position to effectively supervise and enforce EU law**

Increasing level of authorization requests and supervision should not impede NCAs current responsibility to enforce the relevant legislation. In this context, NCAs should have adequate resources and capacity both to monitor the effective application of the relevant legislation met on a continuous basis (e.g., conduct on-site inspections) and respond to market developments.

## **Principle 9: Coordination to ensure effective monitoring by ESMA**

ESMA highlights the importance of an effective and efficient cooperation among NCAs. In that regard, ESMA will establish new practical convergence tools in the form of a forum, referred to as “Supervisory Coordination Network” for reporting and discussions among NCAs to exchange about candidates for relocation in the EU27. This network will aim to promote consistent decisions in respect to authorizations to relocate entities, activities, or functions to the remaining member states.

## **Next steps**

More sector-specific opinions are expected to be released by authorities in the coming months. Additionally, ESMA will establish the Supervisory Coordination Network aiming to promote consistent decisions by NCAs, who are preparing themselves to manage an increase in the activities related to authorization process.

We trust this information is of assistance and remain at your disposal for any questions.

## **How can Deloitte help you?**

Deloitte can help you in navigating Brexit uncertainties and structuring reallocation of entities or activities, offering a full range of services including:

- Support to execution: design and build the operating models of new structures or entities; assess the organizational design impacts, people moves, and workforce planning; design and implement new finance reporting and processes; program management support; etc.
- Regulatory implementation: legal entity structure definition and review; preparation of application file, business plan, and other relevant documentation; support in the interactions with authorities, etc.
- Tax, reward, mobility and immigration: impact assessment of restructuring and comparison of tax rates and regimes; employment taxes considerations and liaison with local tax authorities; advise on remuneration package options, including analysis of the reward-related considerations for firm relocation, etc.

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