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Regulatory News Alert

The UK's approach to EEA banks and investment firms' branches (&CCPs) authorization and supervision after Brexit

29 January 2018

Overview

On 20 December the PRA presented its overall approach for UK branches of international banks. The PRA sets great store not only by the equivalence of the home supervisory regime, but also by co-operation from home supervisors, particularly for branches that are systemically important. It is also clear that the PRA is expecting the home supervisor to be forthcoming about the risks both to the firm of which the branch is part, but also the wider group. On paper at least, the PRA is setting a high bar for co-operation.

If necessary, HMT might legislate for a temporary permissions regime, a reason why the PRA encourages firms to begin preparing for authorization in line with the approach set out in its consultation documents for third country branches. Inbound EEA firms will be able to submit applications for authorization as branches from January 2018, as long as they are not conducting material retail business.

The Financial Conduct Authority (FCA) expects to set out further detail on its approach to authorization in 2018, reducing the time to apply for the provision of service through the current passporting authorization. However, it has indicated that for sole FCA-regulated firms, at present time a notification before the exit day, rather than an application, will be sufficient to benefit from a temporary permission.

Updated approach to branches of international banks

The PRA published the **consultation paper 29/17** containing a draft supervisory statement ("SS") that sets out the PRA's **new approach to authorizing and supervising international bank branches**. Once finalized, it will replace the existing SS10/14 "Supervising international banks: the Prudential Regulation Authority's approach to branch supervision". The consultation closes on 27 February 2018.

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Retail banking

Whilst keeping PRA's previous approach, the proposal will restate the thresholds beyond which it will not be satisfied for branches to undertake retail banking activities, and it has included new detail on an additional threshold level (in excess of £500 million covered deposits) for what it considers a material liability for the FSCS. Few entities should be in the scope, but the ones that are will be forced to move to a subsidiary structure.

If the thresholds are to be determined by the new PRA requirements, the approach is expected to be firm by firm.

Wholesale banking

While the PRA's preference for retail banking activity to be conducted through a UK subsidiary above certain thresholds is well known, the proposal targets also the larger wholesale banking activities and new triggers will be introduced to force the subsidiary status.

The PRA sets out a **two levels approach:**

1. The first level is about the systemic importance of the branch to the financial stability, it is envisaged that close to a third of EEA (European headquartered banks), three key factors will influence the qualification:
    - Whether the bank holds £15 billion total gross assets (including those traded or booked out of the UK)
    - The type of functions it undertakes in the UK
    - The "overall complexity" and inter-connectedness of the business undertaken in the branch, or to which degree the bank is linked with others UK bank
2. Then where a branch is judged to be systemically important, the PRA will assess a second factor relating to the "supervisability of the branch". This factor leaving room for maneuver on the supervisor side covers both the:
    - Quality of supervisory cooperation with the home state supervisor
    - Degree of influence and visibility the PRA might have over the supervisory outcomes for the entire bank or group

The PRA sets out that the "supervisability factor" may be harder to satisfy where group structures are more complex, post March 2019 it remains to be seen how the degree of collaboration and quality of relations with other EU authorities will be interpreted.

The PRA trends is to favor simpler group structures where the UK firm is directly under the ultimate parent firm, hence allowing the PRA to have a direct relationship with the ultimate parent supervisor. Alternative group structures (for example disintermediated branches) are not ruled out but would require more justifications. The ultimate consequence may be that the PRA will require a transformation of the branch into a subsidiary.

Approach to Central Counterparties

The new PRA requirements also apply for Central Counterparties (CCP under EMIR) where the systemic impact might be felt in all circumstances.

The BoE expects recognition of non-UK CCPs immediately following the UK's withdrawal from the EU to be based on criteria that reflect Article 25(2) of EMIR and with a strong expectation of reciprocity.

The Priority

To conclude, linked to these discussions, we would like to draw your attention to the Letter addressed to CEO about the UK's withdrawal from the European Union. Among others, this letter provides firms with planning assumptions in preparation for Brexit.

The PRA recalls and insists that by its very nature there **will not be any passporting rights post-Brexit** (unless agreed otherwise between EU-UK). Firms currently exercising those rights will need to seek authorization. The authorization process may **take up to twelve months from the point of application**; firms may submit applications for authorization from January 2018.

How can Deloitte help?

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Our teams have outstanding expertise in prudential and regulatory activities and will be able to define and implement cross-border and cutting-edge structures.

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Relevant links

- PRA letter to banks, insurers and designated investment firms
- PRA consultation on approach to international banks
- BoE guidance on international CCPs
- FCA statement on EU withdrawal
- HM Treasury statement

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