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News Flash

Latham & Watkins Financial Regulatory Practice

21 January 2019 | Number 2439

Brexit and Financial Services — UK Equivalence Decisions

HM Treasury has published draft legislation that will allow the UK to make timely equivalence decisions in relation to the EU.

Key Points:

- Post-Brexit, HM Treasury will take on the role of making equivalence decisions under onshored EU financial service legislation, but the power to make such decisions will only apply after exit day.
- To ensure that all necessary equivalence decisions are in place upon exit day, and avoid undue market disruption, this legislation will give HM Treasury temporary powers to make equivalence decisions in relation to EEA Member States.
- HM Treasury will have the power to make these decisions before exit day, so that they can come into force on exit day.

Why is this draft legislation being introduced?

This legislation is part of the UK government's planning for a no-deal Brexit. It complements the approach being taken in various onshored versions of EU financial services legislation under which the European Commission's role in making equivalence decisions will be passed to HM Treasury.

However, this role will only pass to HM Treasury upon exit day, so without further provision HM Treasury would not be able to make any new equivalence decisions that can come into force on exit day. Although the onshoring process will ensure that all existing equivalence decisions taken by the Commission in relation to non-EEA jurisdictions will remain in force upon Brexit, it does not permit HM Treasury to put in place new equivalence decisions in relation to EEA jurisdictions (which will be third countries from a UK perspective in a no-deal scenario) in time for exit day.

Further, under the onshored equivalence provisions, HM Treasury will have to go through the usual procedures before making an equivalence decision, which may be problematic if HM Treasury finds that it needs to put new decisions in place swiftly.

What will the legislation do?

The draft legislation provides a temporary power for HM Treasury to make equivalence "directions" in relation to EEA jurisdictions for up to 12 months after exit day. Importantly, HM Treasury will be able to

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make these decisions as soon as the legislation is made, to come into force on exit day. This will allow HM Treasury to ensure that any necessary new equivalence decisions regarding EEA jurisdictions come into force upon Brexit, so there is no gap that could result in market disruption.

The temporary power will also enable HM Treasury to make equivalence decisions more quickly than under the onshored equivalence frameworks. Therefore, it will be of use not only when a decision needs to be put in place ready for exit day, but also in a situation where, post-exit day, HM Treasury wishes to implement a new equivalence decision promptly.

This is meant to ensure that HM Treasury can make equivalence decisions quickly and efficiently if needed, and that it has the flexibility to respond to emerging situations in the 12 months post-Brexit. The explanatory memorandum states that this power is expected to be used where it is necessary to make equivalence decisions at short notice, but not when alternative specific transitional arrangements are in place.

The temporary power will not extend to non-EEA jurisdictions, as existing equivalence decisions will remain in place, and HM Treasury will have the power under onshored EU financial services legislation to make any new equivalence decisions it wishes to make in relation to such jurisdictions after exit day under the normal procedures.

The legislation will also give HM Treasury a similar temporary power to make exemption directions for up to 12 months after exit day in relation to certain EU actors. These directions relate to, for example, the exemption in MAR for monetary and public debt management activities. These exemptions will be onshored into UK legislation with UK-only scope, so this temporary power will allow HM Treasury to extend relevant exemptions under the UK onshored regime to certain EU bodies, where appropriate.

Which equivalence regimes will be covered?

The draft legislation indicates that HM Treasury's temporary power will apply in respect of the equivalence regimes in the following EU financial services legislation:

- EU Benchmarks Regulation
- Capital Requirements Regulation
- Credit Rating Agencies Regulation
- EMIR
- MiFIR
- Prospectus Directive and Transparency Directive
- Securities Financing Transactions Regulation
- Short Selling Regulation
- Solvency II

How will decisions taken under these powers apply?

Any equivalence decisions made using HM Treasury's temporary powers will continue to have effect until revoked by a further direction or other legislation (therefore, unlike the powers, the decisions themselves will not be time-limited). However, HM Treasury will be able to revoke or vary such decisions at any time. There is no further clarity at this stage around how HM Treasury might go about revoking such decisions and whether this might, for example, involve a standard notice period. Clearly, politically there is a desire to ensure that these decisions will not carry any greater permanency than EU equivalence decisions.

To aid transparency, any relevant decisions will need to be laid before Parliament, and made publicly available.

What else will the legislation do?

The legislation will also tie up certain other loose ends relating to the UK's equivalence framework.

It will give the UK regulators the function of providing technical advice to HM Treasury in relation to equivalence decisions (as the European Supervisory Authorities (ESAs) currently do for the Commission), both under the temporary power and under the onshored equivalence frameworks. HM Treasury and the regulators will be required to enter into a memorandum of understanding to "provide clarity on aspects of the operational processes and coordination of activities" in relation to equivalence decisions.

The draft legislation also sets out some amendments to existing EU equivalence decisions in order to address deficiencies as part of the onshoring process. These amendments are of a minor or technical nature only, and are not intended to change the substance of any of the decisions.

Finally, the legislation will revoke the EU legislation relating to the establishment of the ESAs and the European Systemic Risk Board (which would otherwise be onshored onto the UK statute books). This is because it is not considered appropriate for these bodies to continue to play a role in relation to the UK in a no-deal scenario. Therefore, firms should note that the role of bodies such as ESMA will fall away upon exit day in a no-deal scenario.

What will the legislation not do?

The legislation can only make preparations from a UK perspective, so does not address any of the uncertainty concerning whether or not the EU will judge the UK to be equivalent for the purposes of various EU financial services regimes. It remains to be seen how the EU will approach equivalence determinations in relation to the UK. However, recent actions by the EU such as the approach to granting Switzerland equivalence under MiFIR, and plans to tighten third country regimes under various frameworks, mean that doubt remains as to how forthcoming equivalence decisions might be in relation to the UK.

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