



Gem Briefing Note 19/1 - January 2019

FCA - EU Withdrawal Impact Assessment

Background

The Treasury Select Committee requested the FCA to assess the impact of the UK's exit from the EU across three areas:

- The UK leaves the EU without an agreement either on 29 March 2019 or after the transitional period on 31 December 2020 (section 1)
- The draft Withdrawal Agreement (section 2)
- The outline of the political declaration on the framework for the future relationship between the EU and the UK (section 3).

As a public body, the FCA takes no position on the UK's withdrawal from the European Union. It has assessed Brexit and what might happen over the coming months strictly through the lens of achieving its strategic objective to ensure that relevant markets function well, and its specific operational objectives - to protect consumers, enhance market integrity and promote competition.

Impact assessments

1. The UK leaves the EU without an agreement either on 29 March 2019 or on 31 December 2020

If the EU and the UK do not ratify a Withdrawal Treaty in time for 29 March 2019, absent any alternative agreement, the UK would leave the EU with no implementation period. In a financial services context, this means defaulting to

a “third country” relationship, with market access determined under World Trade Organisation (WTO) rules and EU or national Member State rules.

EU legislation would cease to apply in the UK. Instead, the relevant legislation would be converted into UK law through the EU (Withdrawal) Act and amended by Government and regulators to ensure the UK continues to have a functioning regulatory regime. In the event the UK leaves the EU with no agreement, it will be crucial that all the relevant statutory instruments intended to be laid by Government are in place by exit.

The UK would no longer be part of the EU legal frameworks that provide for supervisory cooperation and data sharing between Member States, and passporting rights would cease to apply. The European Commission has encouraged the European Supervisory Authorities to put the necessary agreements in place ahead of exit to ensure EU authorities can cooperate with the UK as with other third countries, but this will not cover all areas of cooperation that currently exist between EU Member States.

Consumers could also potentially be affected, either directly if firms are unable to continue providing services or indirectly as a result of wider economic or market disruption. Over time market fragmentation could have a harmful impact on financial services’ markets more widely, through reduced competition and increased costs for customers in both the EEA and UK.

Working with the other UK authorities, the FCA have put in place measures such as temporary permissions regimes for incoming EU passported firms to mitigate risks to consumers wherever possible, and have communicated their expectation to firms that individual consumers must be informed about material changes in their position related to EU withdrawal.

The UK authorities have engaged in extensive contingency planning. As a result, the Financial Policy Committee (FPC) has judged the UK financial system to be resilient to a disorderly exit without a deal or implementation period. Nonetheless, it notes that some market volatility is to be expected in this scenario, but this should not affect the ability of markets to function effectively.

Ultimately, the impact of a no-deal scenario greatly depends on the extent to which the UK and EU can continue to cooperate and take action together to minimise disruption. The Government, the FCA and the Bank of England/PRA have taken steps to ensure appropriate mitigation is in place for risks that can be dealt with unilaterally. However, outstanding uncertainties include:

- the extent to which firm and public-sector contingency plans can be executed smoothly and how any market disruption can be mitigated, which may be affected by the timing of a no deal outcome;
- the extent to which the EU and UK are able to treat each other's regulations as equivalent, including for the purposes of sharing data;
- the extent of supervisory cooperation and how we would manage the separation of shared systems for market oversight; and
- the solutions the EU puts in place to ensure continuity of contracts and other cliff-edge risks the Financial Policy Committee (FPC) has identified.

Alternatively, in the event a Withdrawal Agreement is ratified but no future relationship is in place before the end of 2020, and absent any other agreement for financial services, or an extension of the implementation period, the UK would leave the EU with no specific framework in place governing its relationship with the EU.

2. The draft Withdrawal Agreement is ratified

The draft Withdrawal Agreement provides for an implementation period, which will run from 30 March 2019 to 31 December 2020, during which EU law applies to the UK. The implementation period may be extended once with both parties' mutual consent. The FCA has consistently supported an implementation period to avoid cliff-edge risks and smooth the UK's transition to a new relationship with the EU. The draft Withdrawal Agreement achieves this by ensuring that EU law, and rights and obligations derived from EU law, continue to apply throughout the period. This includes new EU laws that are agreed and implemented during that period.

During the implementation period, the UK will no longer be part of EU decision-making structures, nor will it be represented in the EU institutions, agencies and bodies. The FCA will therefore no longer be a voting member of the European Securities and Markets Authority (ESMA). Some participation may be possible, but the EU and UK have not yet agreed how this would work in practice. The FCA believe there is a strong case for continued close cooperation given the size of the UK's financial services sector and the importance the UK's approach to applying EU financial services law has for the rest of the EU.

The FCA have reviewed the draft Withdrawal Agreement and identified the articles relevant to the FCA's objectives. The Agreement's main impact relates to the evolution of EU law during the implementation period and the extent to which the FCA and the Government continue to input into, shape and influence the evolution of financial services law. Additionally, the FCA have reviewed the

legislation that is currently under negotiation in the EU. More than 30 EU legislative files relating to financial services are currently under discussion. It is not certain how many of these the UK will ultimately need to put in place during an implementation period.

3. The framework for the future relationship between the EU and the UK

At the end of the implementation period, the UK and EU are expected to have an agreed future trading relationship in place. The Government and the EU have agreed an outline of the political declaration setting out the framework for the future relationship between the EU and the UK. For financial services, this encompasses:

- commitments to preserve financial stability, market integrity, investor protection and fair competition, while respecting each parties' autonomy and ability to take equivalence decisions in their own interest;
- commencement of equivalence assessments by both parties as soon as possible after UK withdrawal, endeavouring to conclude these assessments before the end of June 2020; and
- close and structured cooperation on regulatory and supervisory matters, grounded in the economic partnership and based on the principles of regulatory autonomy, transparency and stability

Next steps for firms

There is still a great deal of uncertainty as to the exact terms of leaving and thus what will be the true impact on firms. Firms are advised to evidence their contingency planning in any case, even if considered to be little impact, and take a cautionary approach in their preparations to suit their business circumstances and mitigate accordingly. The FCA has maintained that its stance is continued adherence to its strategic objective of ensuring that relevant markets function well, and the underlying specific operational objectives; to protect consumers, enhance market integrity and promote competition. Regardless of the withdrawal outcome, firms will do well to keep these objectives in mind when making their own arrangements to ensure they continue to plan effectively and operate compliantly.

Disclaimer:

This note is intended as a summary only. It is not full and/or firm specific advice and it is the responsibility of each regulated firm to ensure they fully consider relevant publications.

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