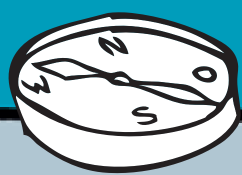
EXIT NEGOTIATIONS BETWEEN THE EUROPEAN UNION AND THE UNITED KINGDOM:

MINIMISE BREXIT RISKS AND STRENGTHEN THE EUROPEAN CAPITAL MARKET

Recommendations of Deutsches Aktieninstitut



Deutsches Aktieninstitut

Publisher: Deutsches Aktieninstitut e.V.
Senckenberganlage 28
60325 Frankfurt am Main
www.dai.de

February 2017

ISBN 978-3-934579-79-8

For download see www.dai.de

EXIT NEGOTIATIONS BETWEEN THE EUROPEAN UNION AND THE UNITED KINGDOM:

MINIMISE BREXIT RISKS AND STRENGTHEN THE EUROPEAN CAPITAL MARKET

Recommendations of Deutsches Aktieninstitut

Position Paper of Deutsches Aktieninstitut e.V. on the Brexit Negotiations
Version: 28 February 2017

Foreword

The United Kingdom's departure from the European Union ("Brexit") will inevitably have serious consequences on the European economy and society. In this regard, the concrete impact depends on the result of the Brexit negotiations and therefore cannot be predicted in detail. However, it is certain that the Brexit constitutes a major challenge for everyone involved.

It is up to the lead negotiators on both sides to frame a constructive and adequate solution for the future relations between the European Union and the United Kingdom which strengthens the European capital and other markets and minimises the negative fallout of Brexit for both sides.

To support the lead negotiators at regional, federal and EU level, Deutsches Aktieninstitut has put in place an interdisciplinary project group. Members of Deutsches Aktieninstitut input their specific experience and viewpoint in order to define which thematic areas should be assigned special importance in the negotiations. Ways to minimise the negative consequences on the affected national economies are highlighted. I take this opportunity to thank all members of the Brexit project warmly for their excellent and time-consuming work which has made this position paper possible.

To this end, Deutsches Aktieninstitut's "Brexit project" has busied itself intensively with the British referendum and the consequences for individual areas of law. The analyses and recommendations presented are oriented on the needs, which Deutsches Aktieninstitut and its members have identified for German and European companies, financial centres and legal systems. This paper will be constantly reviewed, further discussed and reworked as necessary. It constitutes a snapshot of thinking at the time of its drafting. We reserve the right to adjust the statements to reflect the status of the negotiations.

The content is divided into two sections: part I comprises general, overarching comments and considerations which should be taken into account in the framework of the Brexit negotiations. Part II goes into the details of the technical aspects and issues linked to regulation of capital and financial markets as well as company law.

This paper has been drawn up with the objective of keeping the consequences of Brexit as bearable as possible. It is absolutely essential not to damage the core of the European idea which is manifested in the four fundamental freedoms of the single market – free movement of goods, persons, services and capital.

Deutsches Aktieninstitut and its members would be pleased to act as a competent discussion partner of the lead negotiators and other interested parties on the basis of the subsequent analyses and comments on Brexit.

Frankfurt, February 2017

Dr. Christine Bortenlänger

Chief Executive
Deutsches Aktieninstitut e.V.

Contents

List of Abbreviations

ACPR	Autorité de Contrôle Prudentiel et de Résolution
AIFMD	Alternative Investment Fund Managers Directive
AG	Aktiengesellschaft (Public Limited Company)
AMF	Autorité des Marchés Financiers
APA	Approved Publication Arrangement
ARM	Approved Reporting Mechanism
BGBl.	Bundesgesetzblatt (German Federal Law Gazette)
BGH	Bundesgerichtshof (German Federal Court)
BörsG	Börsengesetz (German stock exchange act)
Brexit	Exit of the United Kingdom from the European Union
CCP	Central Counter Party
CE marking	Administrative label for EU free movement
Cf.	Confer (Latin for "compare")
COM	European Commission
Co. KG	Compagnie Kommanditgesellschaft (Limited Commercial Parternship)
CPMI	Committee on Payments and Market Infrastructures
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CSD	Central Securities Depository
CSDR	Central Securities Depositories Regulation
CTP	Consolidated Tape Provider
CVA	Credit Valuation Adjustment
DRV	Deutscher Rahmenvertrag (German Master Agreement)
DTCC	Depository Trust & Clearing Corporation
EBA	European Banking Authority
EC	European Community
ECB	European Central Bank
ECDB	European Company (SE) Database
ECJ	European Court of Justice
ECMR	European Commission Merger Regulation
ECR	European Court Report
EEA	European Economic Area
EFET	European Federation of Energy Traders
EGC	European General Court
EGInsO	Einführungsgesetz zur Insolvenzordnung (German introductory act to the insolvency act)
EIOPA	European Insurance and Occupational Pensions Authority
EMA	European Master Agreement
ESAs	European Supervisory Authorities
ESMA	European Securities and Markets Authority

ESRB	European Systemic Risk Board
ETD	Exchange Traded Derivative
Et seq.	Et Sequens (Latin for "and the following")
Et seqq.	Et Sequentia (Latin for "and those which follow")
EU	European Union
EUREX	European Exchange
e.V.	Eingetragener Verein (registered association)
FinDAG	Finanzdienstleistungsaufsichtsgesetz (German financial services supervisory authority act)
FinfraG	Finanzmarktinfrastrukturgesetz (German financial market infrastructure act)
FMStFG	Finanzmarktstabilisierungsfondsgesetz (German financial market stabilisation funds act)
G20	Group of the twenty most important industry and emerging countries
GATT	General Agreement on Tariffs and Trade
GbR	Gesellschaft bürgerlichen Rechts (Partnership defined under German civil law)
InvG	Investmentgesetz (German investment act)
IOSCO	International Organization of Securities Commissions
IPO	Initial Public Offering
IPR	International Private Law
ISDA	International Swaps and Derivatives Association
ITS	Implementing Technical Standard
KWG	Kreditwesengesetz (German banking act)
L	Législation
LME	London Metal Exchange
MAC	Material Adverse Change
MAR	Market Abuse Regulation
MgVG	Mitbestimmung der Arbeitnehmer bei einer grenzüberschreitenden Verschmelzung (German act on co-determination of employees in a cross-border merger)
MiFIR	Markets in Financial Instruments Regulation
MiFiD	Markets in Financial Instruments Directive
MoMiG	Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen (German act to modernise the law on private limited companies and combat abuses)
MTF	Multilateral Trading Facility
NFC	Non-Financial Counterparty
NSFR	Net Stable Funding Ratio
OJEU	Official Journal of the European Union
oHG	Offene Handelsgesellschaft (General Partnership)
OTC	Over-The-Counter
OTF	Organised Trading Facility
plc	Public Limited Company

PSD	Payment Services Directive
QCCP	Qualifying Central Counterparty
RCB	Reasonable Commercial Basis
RM	Regulated Market
RTS	Regulatory Technical Standard
SE	Societas Europaea (European Public Limited Company)
SEAG	SE Ausführungsgesetz (German act implementing the SE Regulation)
SEBG	SE Beteiligungsgesetz (German act on the employe participation in a SE)
SFTR	Securities Financing Transactions Regulation
SI	Systematic Internaliser
SLL	Securities Law Legislation
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
TR	Transaction Register
UCITS	Undertakings in Collective Investments in Transferable Securities
UK	United Kingdom
UmwG	Umwandlungsgesetz (German act regulating transformation of companies)
US	United States
USA	United States of America
VAG	Versicherungsaufsichtsgesetz (German Insurance Supervision Act)
WpHG	Wertpapierhandelsgesetz (German securities trading act)
WpPG	Wertpapierprospektgesetz (German securities prospectus act)
WpÜG	Wertpapiererwerbs- und Übernahmegesetz (German securities acquisition and takeover law)
WTO	World Trade Organization

List of Figures

Executive Summary

The United Kingdom's departure from the European Union (Brexit) poses considerable problems for both sides. Never before has an EU Member State wanted to leave the community of European nations. Above all, the situation is characterised by one factor: great uncertainty about the future shape of relations between the European Union and its remaining Member States and the United Kingdom.

But one thing is sure: insofar as not agreed and implemented otherwise, the facilitations of the single market for economic exchanges between the European Union and the United Kingdom will lapse with Brexit. This has an impact on virtually every area of law and every area of law therefore needs to be examined intensively in the exit negotiations.

In the framework of its "Brexit project", Deutsches Aktieninstitut has identified the essential issues with relevance for capital markets and which deserve particular attention due to their significance for business and society in connection with the Brexit negotiations. This first position paper concentrates on the thematic blocks of capital and financial markets law as well as company law. In addition, we address overarching issues which constitute the decisive basis for the functioning of business and society in Europe irrespective of particular areas of law and sector, and thus need to be taken into consideration in the negotiations.

The purpose of this position paper is to highlight how the negative impact of Brexit on the affected national economies can be minimised.

Against this background, Deutsches Aktieninstitut proposes the following as overarching objectives of the upcoming negotiations:

1. Minimise drawbacks for all affected parties and ensure the attractiveness of European markets

The Brexit negotiations between the European Union and the United Kingdom must be conducted in an objective, cooperative and constructive manner. If the outcome is a departure of the United Kingdom from the single market without a compromise solution ("hard Brexit"), cross-border economic flows would become considerably more difficult. This would lead to damage and disadvantages which cannot today be predicted in all consequences for all national economies affected.

The competitiveness of European companies must be safeguarded also in the future in the interests of consumers, employees and shareholders. The position paper points to a range of approaches including, for instance, broadly framed and efficient third-country regimes for financial services or introduction of the English language as the court language for international negotiations.

It is also of great importance to prevent distortions of competition caused by a race to deregulate and tax dumping between British and EU markets.

Deutsches Aktieninstitut calls on the lead negotiators on both sides not to lose sight of these overarching objectives and to make them the guiding principle in what will certainly be very difficult and complex negotiations.

2. Buy time with transitional arrangements and ensure the continuing existence of European-British economic relations

It cannot be expected that all Brexit-related issues will be discussed in the necessary detail and solutions found within two years. In addition, implementation of the negotiation outcomes will not be possible overnight. Accordingly, adequate transitional arrangements are indispensable in order to avoid legal uncertainty.

These transitional arrangements must ensure first and foremost that the relations between the European Union and the United Kingdom do not revert automatically to the level applicable between third countries in the absence of negotiated results at the time of the Brexit and might only be brought back to a finalised level after many years of negotiations. Furthermore, those involved – regulators, companies and society – buy time with transitional arrangements. It enables them to prepare adequately for the new legal situation and to adjust business processes and structures accordingly.

Deutsches Aktieninstitut regards a feasible and effective transitional arrangement at EU level as indispensable. There are already positive models such as the MiFIR rules, whereby firms established in third countries have up to three years after a negative equivalence decision when they can continue to provide securities services in the EU Member States.

If no adequate European arrangement can be found, Deutsches Aktieninstitut alternatively advocates comparable arrangements at German level. These could be implemented relatively rapidly and without red tape, thereby increasing Germany's attractiveness as a financial centre by keeping costs predictable and ensuring planning certainty. This can be of decisive importance in international competition.

3. Capital and financial markets regulation: Widen and harmonise third-country regimes while making them more efficient

At the current time, a hard Brexit slightly softened through bilateral agreements between the European Union and the United Kingdom seems to be emerging. With a hard Brexit, the possibility of providing regulated financial services across borders by applying EU single market freedoms under simplified conditions ("EU passporting") would disappear. British law exclusively would be determinant for financial services in the United Kingdom following Brexit. The legal framework for the provision of financial services by UK financial service providers in the European Union would then be governed by so-called third-country regimes which are specified in European directives and regulations only to a very limited extent. Third-country regimes give companies from non-EU/EEA Member States uniform, regulated access to EU markets enabling them to transact cross-border business more securely and more efficiently. In many areas, the United Kingdom would have to be treated like any other third country outside the European Union, if it is not possible to reach agreement on a special third-country regime in the negotiations.

The third-country regimes currently provided for in European regulations and directives do not reach far enough. They do not encompass all the thematic areas to be regulated in the framework of Brexit and, where they exist, are too narrowly framed for intensive trade relations. Moreover, these rules have the disadvantage of relatively short-term revocability, which limits their general suitability. For that reason, they do not offer sufficient certainty for the various players.

Third-country regimes appropriate for the intensity of the economic interdependence between the United Kingdom and the countries of the European Union must therefore be a decisive point in the Brexit negotiations. In this regard, the existing third-country regimes can serve as basis for a more comprehensive, "customised" equivalence regime between the United Kingdom and the European Union. A wide scope, high level of certainty and easy implementation of the third-country regime are key elements of a functioning agreement between the European Union and the United Kingdom. This also implies close cooperation between regulatory authorities on both sides. Third-country regimes which benefit providers from the United Kingdom should also be made dependent on equivalent rules in the United Kingdom benefiting EU providers (reciprocity).

In addition, a general extension, harmonisation and more efficient structuring of existing third-country regimes could be the basis not only for the future relationship with the United Kingdom but also for increasing the attractiveness of financial centres within the European Union vis-à-vis other third countries such as the USA.

4. Fundamental structures of company law: Safeguard functionality of proven and necessary legal institutions

A very high degree of legal harmonisation and flexibility in cross-border legal traffic has been realised in recent years in Europe in the area of (widely interpreted) company law. Preservation of this achievement is in the interest of both the European Union and the United Kingdom. Tearing these company law linkages apart without the necessary preparations would lead to serious and unnecessary consequences.

By contrast with capital markets regulation, there is no instrument comparable with the third-country regime in company law whose judicious application would be suitable for solving a majority of the foreseeable problems – still bearing in mind the remaining complexity. Rather, a separate solution has to be found and negotiated for each thematic area. The position paper therefore presents a series of specific proposed approaches – with no claim of completeness.

This position paper sets out the ideas of the Brexit project of Deutsches Aktieninstitut at this point in time. It does not claim that the list of topics to be addressed is complete or that the proposed approaches are definitive. As the negotiations unfold, probably dominated primarily by political considerations, the document may be expanded, elaborated and updated as and when necessary.

Part I: Brexit – Overarching Considerations

1 RESTRUCTERING BRITISH-EUROPEAN RELATIONS

1.1 STARTING POINT AND OBJECTIVES OF THE BREXIT PROJECT

The decision of a majority of voters in the United Kingdom (UK) to leave the European Union (EU) will in all probability have serious consequences for the German economy and society, in particular also for companies, consumers and investors. As things currently stand, these consequences cannot be predicted but depend essentially on the exit scenario that finally becomes reality. However, the exit scenario itself will be the outcome of negotiations to be conducted at political level and therefore can be influenced, at least in part.

All business relationships, contracts and processes which are based on EU stipulations are affected by Brexit. A fundamental problem is that companies which are active in both markets will in future have to comply with both British[1] and EU law in some cases. In the worst case, two permits would in future have to be obtained, two sets of reports issued, two different sets of rules complied with, etc. Depending on the configuration of the treaties between the United Kingdom and the European Union, this will be the case in all areas insofar as it cannot be simplified through adequate agreements.

In order to give policy-makers recommendations for the upcoming negotiations, it is indispensable to highlight the conceivable consequences of different scenarios. This in turn calls for an early and most complete possible overview of the issues to be regulated within the exit negotiations. The more incomplete this overview, the greater the danger of inadequate or completely failed agreements, and the greater the already incalculable economic damage caused by the United Kingdom's departure from the European Union – for both sides.

[1] To simplify matters, the collective term British law or UK law is used throughout the text to cover English, Welsh, Scottish and Northern Irish law.

Deutsches Aktieninstitut's "Brexit project" seeks to give the lead negotiators at regional, federal and EU level support for the upcoming complex negotiations by drawing attention to problem areas, underpinned with concrete examples from practice.

The Brexit project's objectives are:

- identification of the issues to be solved in the exit negotiations,
- formulation and evaluation of alternative regulatory solutions, and
- a substantiated recommendation to policy-making lead negotiators which solutions should be preferred (from the EU angle).

Virtually every area of law is affected by the exit negotiations. However, Deutsches Aktieninstitut's Brexit project cannot and should not work on all thematic areas but consciously concentrate on work fields which have a link to capital and financial markets (in the broadest sense) and are of particular importance for business and society in Germany.

1.2 BRITISH-EUROPEAN RELATIONS IN FIGURES

The European Union is the United Kingdom's largest trading partner. 44 percent of British exports (goods and services) went to the European Union in 2014, against just 18 percent to the USA.[2] On the EU side, trade with the United Kingdom accounted for just under 16 percent of goods exports in 2014, at a value of more than 290 billion euros.[3] In 2015, these imports into the United Kingdom rose as high as 316 billion euros. In the other direction, the European Union imported 180 billion euros and 183 billion euros of UK goods in 2014 and 2015 respectively.

With around 2.2 million jobs and annual tax revenues of more than 65 billion British pounds, the financial services sector is the United Kingdom's most important industry (see also section 5).[4] In no other EU Member State (excluding Luxembourg) is this sector as important as in the United Kingdom where it earns almost 12 percent of gross domestic product, employs 7 percent of the country's workers and generates a trade surplus of 72 billion British pounds.[5] The European Union is the largest market for these UK financial services and generated around 41 percent of this trade surplus in 2015.

---

[2] Cf. Office for National Statistics, The Pink Book 2015, at http://www.ons.gov.uk/ons/rel/bop/united-kingdom-balance-of-payments/2015/rft-chapter-09.xls.

[3] Cf. European Commission, Statistics, Export Helpdesk, 2014 and 2015.

[4] Cf. International Regulatory Strategy Group and Hogan Lovells, The EU's Third Country Regimes and Alternatives to Passporting, January 2017.

[5] Cf. The CityUK, Key Facts, London, March 2016, at https://www.thecityuk.com/assets/2016/Reports-PDF/Key-facts-about-UK-financial-and-related-professional-services-2016.pdf.

The importance of the closely intertwined financial markets between the European Union and the United Kingdom becomes also clear from the following examples:

- A not unconsiderable portion of share trading on German stock markets currently takes place with UK market participants (more than 30 percent of trading volume on the Frankfurt Stock Exchange).[6]

- Furthermore, a considerable portion of trade in German shares takes place in the United Kingdom (for instance, more than 30 percent of the trading volume of Daimler and Siemens shares[7] takes place on UK trading platforms).

- A large portion of German derivative volumes is traded by UK market participants (for example, more than 50 percent of Eurex Frankfurt's trading volume comes from the United Kingdom).

- London currently brings together a 77 percent share of clearing with Euro-denominated derivatives (corresponding to a daily trading volume of 573 billion US Dollar).[8]

In 2014, around 2.9 million EU citizens lived in the United Kingdom – 5 percent of the total population.[9] 1.2 million UK citizens live in the other 27 EU Member States.[10]

1.3 PROFESSIONAL AND CONSTRUCTIVE NEGOTIATIONS A MUST!

It is of decisive importance for successful negotiations on Brexit that the latter must be conducted professionally and constructively but with a clear eye on the realities and difficulties. Deutsches Aktieninstitut warns against excessive confidence that a bilateral agreement between the United Kingdom and the European Union could cover all areas of law in such a way that the current status quo regarding integration remains virtually unchanged. Given the range of themes and rules, it will scarcely be possible to capture every theme completely.

However, the negotiators must try to minimise the damage for all sides. A hard Brexit without compromises (cf. explanation in section 5.1.1) would have wide-ranging negative consequences for all stakeholders – business and society – not only in the European Union and the United Kingdom but also the rest of Europe.

[6] Source: Deutsche Börse AG.
[7] Cf. Fidessa group plc, at http://fragmentation.fidessa.com/fragulator/. If the OTC trading volume is included, it can be assumed that this share is considerably higher.
[8] Cf. Bank for International Settlements, April 2016.
[9] Cf. Office for National Statistics, Population by Country of Birth and Nationality Report, August 2015, at https://www.ons.gov.uk/peoplepopulationandcommunity/populationandmigration/internationalmigration/articles/populationbycountryofbirthandnationalityreport/2015-09-27/pdf.
[10] Cf. International Business Times, EU referendum: How many UK citizens live in the European Union and where?, at http://www.ibtimes.co.uk/eu-referendum-how-many-uk-citizens-live-european-union-where-infographic-1526116.

The Brexit negotiations must be conducted objectively, cooperatively and constructively.

Emotions are therefore out of place. An emotional or even a punitive approach helps nobody and ultimately increases the damage for all sides. Just as clearly, we reject any "cherry-picking" by the United Kingdom. This would set a precedent for other Member States with a critical attitude towards the European Union. Every effort must be made to prevent the European Union from drifting apart.

Meeting the wish of the British voter for limits on free movement of persons and greater freedom to take decisions on legislation will have a major influence on the British negotiating position. However, this can be achieved only by the United Kingdom exiting from the entire EU single market, as another solution would run counter to the idea that the four fundamental freedoms of the European Union – free movement of goods, persons, services and capital – are indivisible, as expressly underlined on the EU side.

This partially contrary negotiating positions must necessarily lead to the relationship between the European Union and the United Kingdom being newly and differently arranged. But Deutsches Aktieninstitut appeals to the chief negotiators on both sides to engage in objective, cooperative and constructive work taking these overarching objectives into account and hence minimising the damage for business and society.

1.4 MOVING FORWARD

Following the above introduction to the many-layered issues of Brexit and the future of European-British relations, section 2 explains the significance of transitional regimes which we deem to be particularly important due to the narrow timeframe of the Brexit negotiations.

In addition, Deutsches Aktieninstitut has identified a range of topics which deserve special attention due to their importance for business and society in connection with Brexit (overview in section 3).

Some of these topics are first discussed in general terms, since they are of particular relevance for business and society in the European Union, independently of any particular areas of law (section 4).

In the framework of this position paper, we then concentrate in part II in particular on the two thematic blocks of capital and financial markets law (section 5) as well as company law (section 6), since these relate to essential areas of law for companies oriented on the capital market. In this regard, we look in detail at regulatory problem areas and aspects.

Further topics will be examined in the framework of subsequent position papers as and when necessary.

2 TRANSITIONAL PROVISIONS REQUIRED

2.1 NEED FOR TRANSITIONAL ARRANGEMENTS

The narrow timeframe for finding solutions plays a decisive role in the Brexit negotiations. This creates two successive problem areas:

1. First, it cannot be expected that all issues can be discussed down to the last detail and a solution found on every point within two years. This may happen for major topics, but many areas which seem to be secondary will be first dropped due to the pressure of time and the wish to produce a result. However, this is problematic, since EU directives and regulations only partially or inadequately provide third-country or equivalence regimes. A "break" will occur when UK stipulations come into play in parallel with those of the European Union from one day to the next. In addition, these third-country regimes only regulate the activity of companies from third countries in the European Union. In the future, UK rules will apply primarily for business services from the European Union in the United Kingdom, possibly supplemented by EU provisions insofar as these relate to the export of business services to third countries.

This will cause great difficulties for companies, supervisory authorities and national economies on both sides, because it is currently absolutely impossible to predict the areas for which solutions will be found or not found, left aside how the respective solution will look like. This means: no company, no regulator, no customer can make long-term and comprehensive preparations for the period after when Brexit becomes effective, simply because no stipulations, arrangements or treaties yet exist. Those affected can of course try to anticipate the changes and develop solution scenarios accordingly. But this is practically impossible given the extent of the imminent changes and the wide range of conceivable scenarios.

2. Second, those affected – in particular supervisory authorities and the economy – will need time to implement the changes.[11] This becomes strikingly clear, if we remember how long the concrete transposition of new directives and stipulations in the framework of the ordinary legislative procedure often lasts. This could not be achieved overnight, neither with legal certainty nor with the available capacity of qualified negotiators and specialist personnel in companies (and regulatory authorities). Similarly, entire business models cannot be restructured within two years on the basis of provisional negotiating outcomes and then eventually be adapted again once the negotiations are concluded. Not to mention the difficulties in areas in which no arrangement has yet been found.

[11] Cf. AFME/PWC, Planning for Brexit - Operational impacts on wholesale banking and capital markets in Europe, January 2017, at http://www.afme.eu/globalassets/downloads/publications/afme-pwc-planning-for-brexit.pdf.

2.2 TRANSITIONAL ARRANGEMENTS BUY TIME AND SECURITY FOR ALL PARTIES AFFECTED

Transitional arrangements are urgently necessary to prevent legal uncertainty and to enable the continuation of existing business relations of and with UK market participants. It is important that market participants have planning certainty and can prepare adequately for the new legal situation and adapt business processes accordingly. However, they are only helpful for those affected, if it is known at an early stage whether such regimes will exist and how they will be structured in concrete terms. Transitional regimes are understood to be not only arrangements to be agreed with the United Kingdom but also European or German arrangements which are temporary and serve to ensure a gradual and seamless separation of the United Kingdom from the European Union.

! Without transitional regimes, great uncertainty arises and hence incalculable and unnecessary damage for the economy and society might be caused.

The importance of transitional arrangements can easily be clarified using the cases of application in sections 5 and 6. For instance, a British limited company headquartered in Germany can become a Partnership defined under German civil law (GbR[12]) or a German General Partnership (oHG[13]) overnight. This and the other numerous examples show that companies face drastic changes and uncertainties and that transitional regimes are essential to reduce serious short- and long-term damage for the economy and society.

Non-UK companies sometimes have significant production capacities in the United Kingdom. This raises issues linked not only to the rights of employees to work and reside there but also to the import of intermediate products and the export of finished goods and services into the European Union. In case of a division of production across locations, multiple border crossings may occur. British locations are often not limited merely to serving local demand but also cover other markets served by the wider corporate group. In addition, thanks to cross-border transport links, the United Kingdom is strongly integrated in the European single market for electricity and gas. The non-discriminatory grid access needed as well as the cooperation between electricity exchanges are regulated through binding European legislation. But they do not apply beyond the EU's external frontiers. A Brexit without a transitional regime could lead to distortions, if electricity and gas flows are no longer driven by price but are influenced in the short term by the risk of purely regulatory changes. This results not only in a macroeconomic loss of prosperity but could even impair security of supply on both sides.

---

[12] GbR: Gesellschaft bürgerlichen Rechts.
[13] oHG: Offene Handelsgesellschaft.

Sufficient time is therefore of decisive importance. In the first place, transitional arrangements allow those affected to adjust to the new legal situation and to adapt processes and structures accordingly. In the second place, they prevent relations between the European Union and the United Kingdom from reverting automatically to the level between third countries in the absence of negotiated results at the time of Brexit and might only being brought back to a finalised level after many years of negotiations. This "gap" would durably disrupt business flows between the European Union and the United Kingdom and the damage could only be compensated in the long term, if at all.

2.3 DESIGN OF TRANSITIONAL ARRANGEMENTS

It would be a good idea to decide binding transitional arrangements at EU level instead of aiming for individual solutions in 27 EU Member States. It is therefore problematic that each Member State is responsible for the individual implementation and design of an equivalence decision in many cases, which can lead to a large number of different regimes and market fragmentation. That would be particularly problematic for companies which are active in several EU countries.

The example of the transitional regime in the framework of MiFIR[14] can serve as a model. MiFIR comprises transitional arrangements whereby firms established in third countries have up to three years after a negative equivalence decision during which they can continue to provide securities services in the Member States (article 54 MiFIR). These provisions enable companies to prepare comprehensively for the legal situation after the three-year transition period, either by relocating, by applying for a permit or by making other necessary changes. In addition, implementation of these transitional arrangements should be binding in all EU Member States through an EU regulation.

! Create uniform and binding transitional arrangements at EU level for all – or at least the most relevant – areas.

To prevent market fragmentation and uncertainty among those affected, Deutsches Aktieninstitut recommends the creation of a comparable, uniform and binding regime at EU level for all – or at least the most relevant – areas.

[14] MiFIR: Markets in Financial Instruments Regulation: Regulation (EU) No. 600/2014 of 15 May 2014 on markets for financial instruments and [...].

For the possible case that no EU-wide arrangement is decided, we call on the German legislator – together with the competent supervisory authorities – to find a workable and effective transitional solution. In this case, Deutsches Aktieninstitut advocates the application of transitional arrangements similar to that in the framework of MiFIR. These could be implemented relatively rapidly and without red tape, and would increase the attractiveness of Germany as a financial centre by keeping costs predictable and ensuring planning certainty. This can be of decisive importance in international competition.

3 BREXIT AFFECTS VIRTUALLY ALL THEMATIC AREAS

Deutsches Aktieninstitut has identified a range of topics which deserve particular attention in connection with Brexit due to their importance for the economy and society. This first position paper concentrates on the thematic blocks of capital and financial markets law as well as company law, since these comprise relevant core issues for capital market-oriented companies.

Further topics will be examined in the framework of subsequent position papers as and when necessary. However, we would like to list them below in order to give an overview. If necessary, the provisional list of issues below will be adapted on the basis of the latest state of knowledge and the most recent political developments.

The following points do not constitute a complete list of the issues to be addressed in a particular thematic area:

1. Overarching thematic blocks

- Single market: Movement of goods and services
- Single market: Movement of persons
- Distortion of competition, tax dumping and financial transaction tax
- Financing of research and development
- Administrative, court language and communication

2. Capital and financial markets law

- Licensed activities
- Supervision
- Litigation

3. Company law

- Recognition of companies established in the UK
- Cross-border mergers
- European Company (Societas Europaea – SE)
- Merger control notification in the case of M&A
- M&A takeover law
- Contracts with a reference to EU law
- Contracts with a reference to UK law

4. Tax law

- Contracts with a reference to EU tax law
- Value-added tax
- Refund of contributions
- (Withholding) tax reduction
- Interest and licence fees
- Conversion tax law
- Netting of cross-border losses
- Taxation upon leave of tax net
- Foreign base company income tax
- Currency risks

5. Data protection and cyber-security

- Data protection
- Trademarks and patents
- Cyber-security
- Encryption and digital evidence

6. Miscellaneous themes

- IFRS convergence and reporting
- FinTech

4 OVERARCHING THEMATIC BLOCKS

Below a series of topics is firstly addressed from the list of relevant thematic areas (cf. section 3). These should be considered independently of particular areas of law and sectors for all fundamental negotiating decisions, since they currently constitute the basis for the functioning of the economy and society in Europe. The advance examination of these overarching topics makes unnecessary repetitions in the subsequent text redundant.

4.1 SINGLE MARKET: MOVEMENT OF GOODS AND SERVICES

Deliveries between the United Kingdom and the European Union which were originally intra-Community deliveries will become export deliveries after Brexit. Consequently, customs duties and other costs for cross-border trade in goods between the European Union and the United Kingdom will become payable. Moreover, mutual recognition of national product and service permits will broadly cease to apply. For example, a wide range of UK products cannot be placed on the market within the European Union without the CE marking which is applicable across Europe. Clearly, the reverse is the case for European products which have no UK marking.

All this is relevant not only for sales of goods but in particular also in the framework of companies' international value-added chains. For instance, intermediate products are often produced in various countries, fitted together into larger components in a further country and then built into the end product in another country, this end product being sold in yet other countries. In particular, if the United Kingdom plays an intermediate function as a production location in a value-added chain, which starts and ends in the European Union, this would lead to (at least) two border crossings and the associated extra costs, delays, permits and other additional bureaucratic effort.

Generally speaking, it should be taken into account at this point from the German or continental European viewpoint that for example Germany, with around 89 billion euros of goods in 2015, exports clearly more to the United Kingdom than the reverse (around 40 billion euros, cf. also section 1.2).[15] Particular attention should therefore be paid in the Brexit negotiations that agreements are reached wherever non-agreement risks the introduction of customs duties by the United Kingdom.

[15] Cf. European Commission, Statistics, Export Helpdesk, 2014 and 2015.

4.2 SINGLE MARKET: MOVEMENT OF PERSONS

It is not only the movement of goods and services that would be restricted. In particular, the principle of free movement of EU workers ends in the case of Brexit. Under this principle, every Union citizen has the possibility to take and perform work in every Member State of which he is not a national under the same conditions as a national of that Member State. Considerable restrictions with regard to taking up employment in the United Kingdom could in future be imposed on EU citizens, and vice versa.

Restrictions on movement of persons would relate in particular to the practice of corporate groups in the area of posting of workers. Employers would be clearly more restricted than hitherto with respect to cross-border deployment of workers and would have to deal with considerable bureaucratic hurdles, such as application for a work permit or even a lengthy priority test. A flexible, time-saving and non-bureaucratic solution is therefore important for the deployment of employees within corporate groups.

4.3 DISTORTION OF COMPETITION, TAX DUMPING AND FINANCIAL TRANSACTION TAX

The United Kingdom will probably seek to take measures which create a competitive advantage to the benefit of British companies and/or which enhance the United Kingdom's attractiveness as a business location vis-à-vis the European Union. For example, the British government has expressed the idea of reducing tax on companies located in the UK following Brexit. Furthermore, regulatory facilitations for UK suppliers could be created or – insofar as allowed under GATT[16] rules – high import duties could be introduced for foreign companies. It would also be problematic, if the current EU practice for the award of public contracts was restricted in the United Kingdom.

All these measures would establish a clear competitive disadvantage for suppliers from the European Union vis-à-vis British competitors. As a result, mechanisms must be created which protect EU companies against discriminatory measures or prevent them. Only in this way can fair competition conditions be ensured and a relocation of companies in the United Kingdom be avoided.

In the context of Brexit, it seems nearly absurd that various EU countries are still calling for the introduction of a financial transaction tax. A unilateral introduction in the European Union would run counter to the objective of strengthening the European Union as a financial centre and positioning itself as an attractive alternative to London, setting aside a series of reasons which generally militate against the introduction of such a tax.[17] It would legitimise and stimulate the United Kingdom's plans to create competition and tax advantages for local companies. At the same time, it would mean a major disadvantage for the EU capital market and European companies in international competition. Even more questionable would be the introduction of a financial transaction tax only in ten EU Member States participating

[16] GATT: World Trade Organization's General Agreement on Tariffs and Trade.
[17] Deutsches Aktieninstitut e.V. has published various documents on the financial transaction tax, available at https://www.dai.de/de/das-bieten-wir/tag-suche-ergebnis/tag/Finanztransaktionssteuer.html.

in the “enhanced cooperation”. A partial introduction would disadvantage these countries not only vis-à-vis the United Kingdom but also vis-à-vis the other EU Member States such as Ireland and Luxembourg. The German Federal Finance Minister Wolfgang Schäuble also spoke in similarly sceptical terms in February 2017. In his words, it is “possibly not the most attractive basis at this point in time”.[18]

4.4 RESEARCH AND DEVELOPMENT

The European Union has financed pioneering research projects in the United Kingdom over many years, in particular in Oxford and Cambridge. It is feared that this cooperation will end following Brexit, knowledge will be lost and/or EU institutions will no longer have access to this knowledge. Whereas a diversion of research funds to EU companies helps future research in the European Union, it cannot replace the loss of existing knowledge and the absence of exchanges within science. This would set European research back by years and jeopardise international competitiveness. Inasmuch, cooperation between EU and British research institutions continues to be desirable. At the very least, access to the knowledge built up in the past must be safeguarded.

4.5 ADMINISTRATIVE, COURT LANGUAGE AND COMMUNICATION

At the present time, London is attractive as a European capital market location in part because it works in a language which a prevelant majority of market participants can use business fluent and is therefore inclusive. This aspect is very often underestimated when competitiveness and efficiency of other capital markets are discussed. The absence of barriers which goes hand in hand with a common administrative and communication language should be replicated across the European Union in order to match the not inconsiderable advantage which London enjoys in this respect. Thought should therefore be given to allowing English to be used as a prospectus and general administrative language also in other EU Member States (alongside the official national language). The French financial market regulation authorities ACPR[19] and AMF[20], which accept some English documents and even have an English-speaking contact person, are already moving in this direction. Existing special rules such as the possibility allowed under German prospectus law to enable a prospectus in “a language common in international financial circles” must therefore be maintained and developed at all costs.

An international financial centre needs communication and law to function predictably among those involved and that as many participants as possible are able to read and understand legal texts. This is particularly important in litigation. If this takes place only for example in German or French, market participants will be hesitant about moving the place of

---

18 Cf. FinanzNachrichten.de, Schäuble compares financial transaction tax with Swiss cheese, 21 February 2017, at http://www.finanznachrichten.de/nachrichten-2017-02/39985108-schaeuble-vergleicht-finanztransaktionssteuer-mit-schweizer-kaese-015.htm.

19 ACPR: Autorité de Contrôle Prudentiel et de Résolution.

20 AMF: Autorité des Marchés Financiers.

jurisdiction from London to other EU Member States. Conflicts between companies active across borders should therefore also be able to be negotiated before e.g. German courts in the English language. The German Federal Council proposed an initiative along these lines back in 2014. Chambers for international trade issues, for which English can be chosen as the language of proceedings, should be established in regional court structures. This also applies for higher appeal and judicial review bodies. The condition should be an international dimension in the legal dispute, e.g. English as the contract language and both parties explicitly deciding for English.

Part II: Regulatory aspects of Brexit in detail

5 CAPITAL- UND FINANCIAL MARKETS LAW

Financial markets play a central role for the economic development in Member States of the European Union and the European Economic Area (EEA). They are crucial for support of the real economy, for job creation (often also indirectly) and for economic growth.[21] But in no other EU Member State is the financial sector of such great importance for the national economy as in the United Kingdom (cf. section 1.2).

Not only since the start of the global financial crisis in 2008, but certainly to a particular extent since then, stabilisation of financial markets across the European Union/the European Economic Area and particularily also in the United Kingdom has been a top priority. The financial markets regulation that this requires relates not only to bank and insurance companies but also to providers of financial services, for example brokers, advisers, infrastructure providers, securities investment funds, alternative investment funds from real estate and private equity to hedge funds but also rating agencies, stock exchanges as well as, for instance, electronic trading platforms, central counterparties, central depositories, other custody systems and other market participants, their products and their services (cf. examples in section 5.1.3 onwards).

Financial markets regulation is built on harmonisation provisions for completion of the single market (articles 114, 26 TFEU[22]) as well as freedom to provide cross-border services (either directly or through dependent branches) (article 56 et seqq. TFEU), freedom of establishment for self-employed persons (article 49 et seqq. TFEU) and free movement of capital and payments (article 63 et seqq. TFEU). Of the four fundamental EU freedoms, free movement of capital is the only one which is broadly applicable also in relation to third countries.

---

[21] Cf. European Commission, press release, Commission report underlines importance and urgency of financial sector reforms as a basis to restore long-term growth, Brussels, 25 April 2013; Cf. European Commission, Action plan on building a capital markets union, Brussels, 30 September 2015, page 7 et seqq.

[22] TFEU: Treaty on the Functioning of the European Union, OJEU of 26 October 2012.

Nevertheless, under the case law of the European Court of Justice (ECJ), restrictions on the free movement of capital in a third-country context could be justified, even if there would not be any in the EU case.[23] This aspect could assume particular relevance in connection with Brexit.

In secondary legislation, EU financial market rules consist of EU regulations which are directly applicable in all Member States and EU directives which have to be transposed into the law of the Member State in question and are binding only in terms of their "objectives" being met. But the details of many of these secondary legislative acts are then shaped to a large extent by tertiary legislation, i.e. through implementing regulation, implementing technical standards (ITS), regulatory technical standards (RTS) or other measures released by the European Commission or the European supervisory authorities (ESMA, EIOPA, EBA, ESRB, ECB[24]). Following Brexit, EU law will directly cease to be applicable in the United Kingdom and must be superseded by national provisions. Conversely, the national rules enacted for transposition of EU directives will continue to exist. We examine below primarily how EU law should react to Brexit. However, it is of decisive importance that corresponding rules are requested from the United Kingdom in order to maintain access to the London financial market for EU companies (reciprocity).

5.1 LICENSED ACTIVITIES

5.1.1 Problem definition

Probably the most important of the financial market rules created by the above-mentioned secondary or tertiary EU law are licensing obligations and the EU-wide authorisation sometimes associated with them (so-called EU passports). A licensing obligation and/or an EU passport can have as its object authorisation of a market participant (e.g. banking permit, financial service permit, insurer permit, fund manager permit, central counterparty permit, central depository permit), authorisation of a product (e.g. securities prospectus) or authorisation of a service (e.g. marketing a fund).

All cross-border activities requiring a license will be particularly affected by Brexit. Following Brexit, these will need a second national permit: European companies which want to offer their banking or financial servies will then need both an EU and a British license. Similarly, UK market participants or institutions will no longer be able to fall back on these privileges under EU law. This also applies for other authorisations, approvals or licences which then have to be applied for and granted several times – in the United Kingdom and in the relevant Member States of the European Union.

[23] ECJ ruling of 28 October 2010, Établissements Rimbaud, C-72/09.

[24] ESMA: European Securities and Markets Authority; EIOPA: European Insurance and Occupational Pensions Authority; EBA: European Banking Authority; ESRB: European Systemic Risk Board; ECB: European Central Bank.

As a rule, the possibility of a one-off EU authorisation with EU-wide applicability will consequently lapse for affected UK companies, products and services. The associated administrative, monetary and time effort for companies and supervisory authorities would be immense. Under these circumstances, it seems highly probable that UK companies and suppliers of products and services will verify which Member States merit this effort.

This is explosive in particular insofar as international credits to and financial transactions with large corporations are often granted or organised by UK subsidiaries of international financial service providers, or these providers even have their headquarters in the United Kingdom.

If the two markets disintegrate, competition and supply in the market can deteriorate and the financing or investment opportunities for companies and investors reduce as a result.

The supply side would probably shrink even further in smaller and economically weaker EU/EEA Member States due to cost-benefit considerations of companies.[25]

The extent to which a permit would continue to be possible from the United Kingdom into the European Union and vice versa, and for which companies, products and services, and how it is shaped depends on the form of the upcoming exit:

- **Alternative 1: Soft Brexit**
  The exit agreement in accordance with article 50 TEU[26] could make provision for an equivalence of UK and EU companies, products and/or services, and inasmuch for the United Kingdom to continue to participate in the EU and EEA single market ("soft Brexit"). Or it could provide a guarantee that permits and/or EU passports which exist at the time of exit (or some other point in time) will be maintained ("grandfathering"). Nevertheless, that would presuppose at least that, in return, EU companies, products and/or services would not be subject to restrictions in the United Kingdom to the same extent (reciprocity). Such solutions should be considered seriously only, if the United Kingdom either maintains the relevant part of EU Community law from the reciprocity angle (acquis communautaire) or reflects it now and in the future in its own law.

- **Alternative 2: Hard Brexit**
  Without an accord on the issues set out above in the exit agreement in accordance with article 50 TEU, the United Kingdom would have to be classified as a third country ("hard brexit"). It would therefore be necessary in many individual cases to check whether certain EU rules contain a third-country regime and

[25] Cf. International Regulatory Strategy Group (IRSG), The EU's Third Country Regimes and Alternatives to Passporting, January 2017. Cf. European Commission, Capital Markets Union - Accelerating Reform, COM(2016) 601, 14 September 2016.
[26] TEU: Treaty on European Union.

whether this can be applied in the concrete case. WTO rules[27] would otherwise govern trade relations between the United Kingdom and the European Union.

- **Alternative 3: Compromise solution**
  Furthermore, a compromise solution could be envisaged whereby the exit agreement contains an accord not on the above-mentioned four fundamental freedoms (hard Brexit) but rather on the United Kingdom, now classified as a third country, having certain rules which are equivalent to those of the European Union. For this, it would have to be decided to provide those EU legislative acts without a so-called "equivalence regime" with such a regime or implement a third-country solution which embraces several individual laws (cf. section 5.1.2). Alternatively, a dedicated bilateral agreement between the European Union and the United Kingdom could address and supplement such third-country regimes individually. Nevertheless, these considerations are helpful only against the background of reciprocity in the provisions in question. But that would also mean that the United Kingdom would not be able or only conditionally able to enter into competition with the European Union with its own, more attractive supervisory rules, as wished by many Brexiteers (including in the government).

Since the British Prime Minister Theresa May's speech in January 2017 and the British government's White Paper in February 2017[28] it can be foreseen that there will be a hard Brexit. In this case, it is important to work with particular emphasis on a compromise solution (alternative 3) – a softening of the hard Brexit through third-country regimes and bilateral agreements between the United Kingdom and the European Union. In this regard, the long-term design of these relations should minimise possible negative consequences for the European and international financial system. Though it is possible for non-EU companies to apply for a permit to operate in an EU Member State, without comprehensive, functioning equivalence regimes this does not generate a right to deploy the fundamental EU freedoms or to offer services across the European Union. Under the current EU legal situation, it is necessary either to transfer the firm's seat into an EU Member State or to establish a subsidiary in an EU Member State for this purpose.

For that reason, some international financial groups, which currently use London as a hub for Europe, are considering at least a partial relocation into the EU area or have already started the relocation process because they cannot wait for the outcome of the Brexit negotiations. Once again, the question arises here on the EU side as to how it is possible and desirable to offer such companies support (for example, also through legislative measures).[29] But at the same time these changes show urgency and need for an adequate agreement between the European Union and the United Kingdom. We therefore look in the following in closer detail at the issue of third-country regimes.

---

[27] WTO: World Trade Organization.

[28] Cf. HM Government, The United Kingdom's exit from and new partnership with the European Union, February 2017, at https://www.gov.uk/government/publications/the-united-kingdoms-exit-from-and-new-partnership-with-the-european-union-white-paper.

[29] German Federal Financial Supervisory Authority BaFin has already reacted to increased requests, a first event for foreign financial undertakings has been held and a dedicated contact address has been created. Cf. BaFin press releases of 17 and 30 January 2017, at https://www.bafin.de/DE/RechtRegelungen/Dokumentlisten/ListePressemitteilungen/liste_pressemitteilungen_node.html.

5.1.2 Third-country regimes

All non-EU/EEA Member States are classified as third countries in EU law. Third-country regimes are intended to give companies from these countries uniformly regulated access to EU markets so that cross-border transactions can be processed more securely and more efficiently. Third-country regimes exist in a very wide range of forms and in the most diverse regulatory texts. It exists therefore so far no uniform regime for all areas of regulation, rather the regulatory landscape is comparable to a large patchwork of individual solutions.

In the public discussion on the future following Brexit, reference is made inter alia to the third-country regime for the MiFID II provisions[30] as a model for the possible future and hence as an alternative to the EU passporting regime. This provides for equal treatment of third countries (as the United Kingdom would be) and EU/EEA Member States, where equivalence of the provisions is given. In this regard, both the legislative framework and the supervisory authorities in the third country are a decisive factor. In addition, cooperation between supervisory authorities is a precondition. But this third-country regime described as an "equivalence regime" applies only for very limited areas, e.g. for the provision of investment services for professional clients, and is thus a long way from being as comprehensive as the EU passporting regime.

"Equivalence regimes" so far apply only for very limited areas and are thus a long way from being as comprehensive as the EU passporting regime.

Other EU legislative acts sometimes have other third-country regimes. In addition, only a small portion of EU provisions provide for any such equivalence regimes whatsoever. A comprehensive extension of the use of the equivalence regime technique would consequently be urgently needed just in order to start to cover the market. Furthermore, the United Kingdom would in future have to refrain from competing with the EU single market with its own more attractive supervisory rules and also in the future to reflect evolving EU law in its own national law. Whereas verifying the equivalence of regimes and supervision can be time-consuming and unwieldy, its immediate withdrawal in the event of small modifications to the legislative and supervisory regime of the third country or of the European Union itself is possible. As a result, the equivalence regime has so far only had a limited reach and offers less legal certainty than the fundamental freedoms enshrined in EU law. In addition, companies from third countries are reliant on numerous decisions by the European Commission and national supervisory authorities, for instance recognition decisions, issue of licenses and approval of exemption possibilities. Policy-makers are encouraged to make the relevant conditions and procedures more transparent and more easily understandable in order to create more legal clarity and certainty.

[30] MIFID II: Revised Markets in Financial Instruments Directive: Directive 2014/65/EU of 1 May 2014 on markets for financial instruments and [...].

Given the level of payment and business flows between the United Kingdom and the European Union, the EU third-country regimes which currently exist are neither suitable nor sufficient. These may be enough for smaller trading partners, but they are too narrowly framed for intensive trade relations and do not offer adequate security for the various players, as becomes also clear from the first relocation initiatives of financial institutions. The questions and constellations raised make it all the more evident that a harmonisation and extension of the scope of third-country regimes should be a decisive point in the Brexit negotiations. In this regard, the existing third-country regimes can serve as basis for a more comprehensive, individual equivalence regime between the United Kingdom and the European Union. However, the extension of third-country regimes, which also benefits suppliers from the United Kingdom, should be made dependent on corresponding regimes being granted in the United Kingdom (reciprocity). A wider scope, adequate security – inter alia through transition periods in the case of equivalence being withdrawn – and "easy" implementation of such an agreement are key factors for a functioning bilateral agreement.

But, also independently of Brexit, we recommend that the issue of third-country regimes is taken up in particular in the framework of the EU "Better Regulation" and "Capital Markets Union" projects.[31] Uniform, understandable and easily implementable regimes with a wide scope would enhance the overall attractiveness of the EU financial and capital markets and hence increase the interest of third-country companies. Accordingly, it is important not only to cover new areas of application but also to structure the existing third-country regimes more efficiently.

The issue of transactions requiring a license is clarified below in the context of Brexit on the basis of various EU directives and regulations. In addition, reference will be made to existing third-country regimes based on the EU-wide passporting and licensing regime, highlighting where such regimes are still absent or fall short of requirements.

5.1.3 Use case: Financial, banking and securities services

1. Overview

MiFID II/MiFIR: On the basis of MiFID II/MiFIR, companies can establish themselves freely within the European Union and offer securities and derivatives across borders without needing an additional national permit. This also encompasses all ancillary services which are necessary to provide securities and derivatives services. An EU-wide permit for data provision services as well as trading venues is also contained in MiFID II/MiFIR (cf. section 5.1.5 on market infrastructure).

CRD I-IV: The Capital Requirements Directives (CRDs)[32] allow credit institutions to offer banking services across the entire European Union and to open branches for this purpose.

[31] Cf. European Commission, Better Regulation Agenda, 2016, at http://ec.europa.eu/info/law/law-making-process/better-regulation-why-and-how_de and Capital Markets Union, 2015, at http://ec.europa.eu/finance/capital-markets-union/index_de.htm.

[32] CRDs: Capital Requirements Directives I - IV. CRD I: 2006/48/EC and 2006/49/EC of 14 June 2006; CRD II: Directive 2009/111/EC of 16 September 2009; CRD III: Directive 2010/76/EU of 24 November 2010; CRD IV: Directive 2013/36/EU of 26 June 2013.

Solvency II: The Solvency II Directive[33] is the centrepiece of insurance regulation for primary insurance and reinsurance companies which enables the EU-wide sale of products and services (cf. section 5.1.11 on insurance services).

PSD I und II: The Payment Services Directives (PSDs)[34] create an EU-wide single market for payment flows. Providers can supply payment services across the entire European Union via an EU passport.

2. Third-country regime

MiFID II/MiFIR: MiFID II/MiFIR – as already explained – comprises a third-country regime for financial services on the basis of an equivalence regime but which only covers some areas. Third-country financial service providers can offer professional clients investment services under simplified conditions. Article 46 MiFIR provides the possibility that the European Commission, supported by the European Securities Committee, can recognise the equivalence of the third country's supervisory regime. Under the condition that ESMA concludes a cooperation agreement with the foreign supervisory authority, EU-wide provision of such MiFID-regulated services to professional clients would be dependent only on implementation of a notification procedure ("third-country entity passport"). By contrast, no third-country regime is provided for data provision services in MiFID II/MiFIR, whereas trading venues are covered to a large extent (cf. section 5.1.5 on market infrastructure).

CRD I-IV: The CRDs provide no third-country regime for banking services. The provisions of MiFID II/MiFIR described above apply for banks' investment services.

Solvency II: Reinsurers from third countries have facilitated access to the EU market, which means no licence requirement for cross-border business in accordance with article 172 Solvency II Directive (and in Germany § 67 paragraph 1 second sentence of the German insurance supervision act (VAG)[35]), if the European Commission determines the equivalence of the solvency system (cf. section 5.1.11 on insurance services).

PSD I and II: The PSDs contain no provision for a third-country regime.

3. Recommendations

The third-country regimes of MiFID II/MiFIR and Solvency II cover only a small portion of financial services, namely investment services to professional clients and cross-border reinsurance business. Normal corporate business is consequently not covered or covered only to a very limited extent, since many services targeting companes are not captured by this (for example, risk management with derivatives in treasury, liquidity management, direct insurances). Services for private clients are not covered at all. An extension of the equivalence regime would therefore create consistency and enable more services to corporate and private clients.

[33] Solvency II: Directive 2009/138/EC of 25 November 2009 on the taking-up and pursuit of the business of insurance and reinsurance [...].

[34] PSDs: Directive on Payment Services (PSD I) and Revised Directive on Payment Services (PSD II). PSD I: Directive 2007/64/EC of 13 November 2007 and PSD II: Directive 2015/2366 of 25 November 2015.

[35] VAG: Versicherungsaufsichtsgesetz.

By contrast, the CRDs as well as the two PSDs make absolutely no provision for a third-country regime. Since the CRDs embody the European transposition of the Basel rules, this relates among other things to lending business with corporate clients. Due to the many overlaps, thought might therefore possibly be given to a common third-country regime which encompasses several legislative acts in a uniform set of rules instead of regulating individual areas separately.

The question also arises as to how the United Kingdom positions itself on still disputed European Union provisions with respect to Basel III (for instance, CVA exemption for NFCs, NSFR[36] or the use of internal models for granting credits to companies). The United Kingdom could seek here to gain an advantage for local companies with "customer-friendly" rules.

In the interaction of Brexit with MiFID II/MiFIR, the following additional questions arise:

- What happens with the commodity position reporting to be introduced from 2018 (for which banks are competent), if trading with a UK bank is involved?
- Where does the competence for limit monitoring for relevant swaps/exchanges lie? What alternatives are there?

5.1.4 Use case: Derivates

In the aftermath of of the global financial markets crisis, the G20 countries decided inter alia to make over-the-counter (OTC) trade in derivatives more transparent and more secure. To this end, the European Market Infrastructure Regulation (EMIR)[37] was created. In general, OTC derivatives are documented contractually through framework agreements recognised in the market. Brexit also has consequences for such documentation.

[36] NFC: Non-Financial Counterparty; NFSR: Net Stable Funding Ratio.

[37] EMIR: European Market Infrastructure Regulation: EU Regulation No. 648/2012 of 4 July 2012 on OTC derivatives, central counterparties and trade repositories.

EMIR

1. Overview

EMIR is a regulation which is directly applicable (i.e. without transposition into national law) in all EU/EEA countries and has been in force since 16 August 2012. EMIR is supplemented by various implementing regulations issued by the European Commission. Moreover, the Member States settled a range of implementing laws, such as the German one[38] which amended a range of laws (including KWG, WpHG, BörsG, VAG, InvG, FinDAG, FMStFG and EGInsO).

The essential content of EMIR constitutes the introduction of a clearing obligation for financial market participants regulated in the European Union (financial counterparties) but also for other (non-financial) counterparties which deploy derivatives in large volumes for purposes other than hedging of their business activity (cf. diagram 1). As a result, clearing of derivatives standardised in this way has to take place via central counterparties (CCPs). In the case of transactions which are not suitable for CCP clearing because of their structure, the parties have to meet special risk management requirements, including collateralisation (as well as higher regulatory capital requirements under CRR[39]). In addition, there is a notification obligation for OTC derivatives to a transaction register (TR), with ESMA exercising oversight of these transaction registers. Lastly, EMIR also contains provisions on the requirements for authorisation and ongoing supervision of CCPs as well as on stronger cooperation between supervisory authorities.

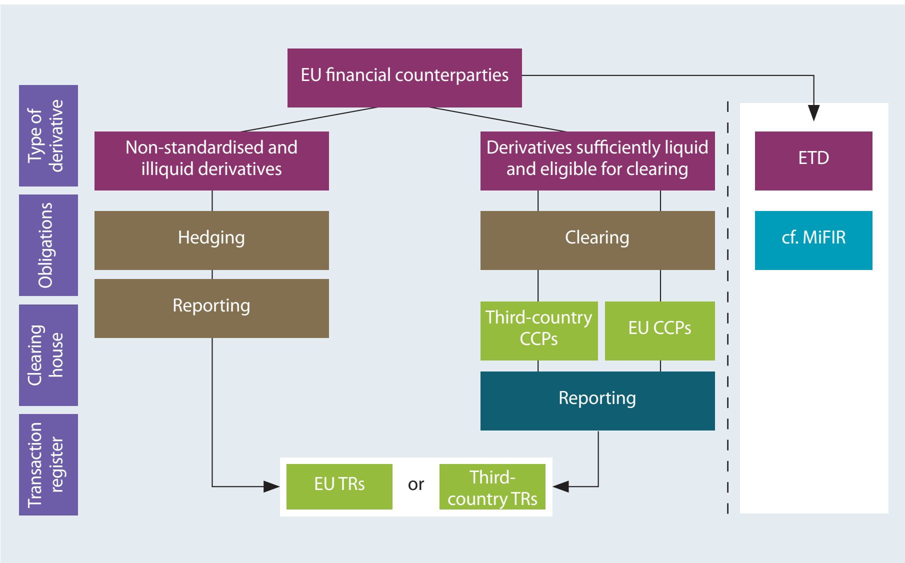


Diagram 1: EMIR requirements for financial counterparties

[38] EMIR implementing law of 13 February 2013, BGBl. I page 174.
[39] CRR: Capital Requirements Regulation: Regulation (EU) No. 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms and [...].

2. Third-country regime

EMIR also comprises third-country regimes for TRs and CCPs. They will assume particular importance in the context of what are termed euro clearings (of cash, securities, derivatives, etc.). In 2011 ECB argued that this was the only way to ensure that it could fully mobilise in the event of CCPs malfunctioning. CCPs would be key components of the financial system, in particular since credit and liquidity risks are concentrated therein. Since disruptions could lead to systemic crises, euro clearing would have to take place in the Eurozone. However, in 2015 the European General Court (EGC) ruled that ECB could not require euro clearers to be established in the Eurozone (a case which had been driven by the British government).[40] ECB has already articulated its concern that, in the event of Brexit, the quality of supervision of UK CCPs would be weakened.[41] It is therefore very improbable that UK clearers would be allowed to continue to transact such deals under EMIR's third-country rules.[42] For the authorisation of TRs established in third countries, article 77 EMIR provides for a special procedure which inter alia requires the European Commission to recognise the equivalence of the foreign supervisory regime.

Under EMIR, a British CCP would have to submit an application to a national supervisory authority in the European Union. If this were successful, it would be deemed a "qualifying CCP" (QCCP) everywhere in the European Union, also under CRR. This means that the EU banks clearing via such a QCCP could treat the QCCP's corresponding counterparty failure risk like that of an EU CCP when calculating its own capital for regulatory purposes. If that were not possible, a British CCP would be at a considerable competitive disadvantage. To be granted an EU authorisation as third-country CCP, British CCPs would have to meet the following conditions (article 25 EMIR):

- The European Commission must confirm that the United Kingdom's competent supervisory regime is equivalent to that of the European Union; inasmuch, there is a requirement of reciprocity.[43]

- The British CCP must be effectively supervised in the United Kingdom.

- There has to be a cooperation agreement between ESMA and the competent national British supervisory authority.

- The United Kingdom must maintain anti-money-laundering systems equivalent to those under EU law.

[40] Cf. EGC, ruling of 4 March 2015, T-496/11.

[41] Cf. ECB, Draghi letter, Frankfurt, January 2017, at https://www.ecb.europa.eu/pub/pdf/other/170111letter_beres.en.pdf?b83bafcc0913440d0e00fdfbbc07087d.

[42] Cf. CNBC, ECB's Coeure warns on challenging future for London's euro clearing business post-Brexit, January 2017, at http://www.cnbc.com/2017/01/20/ecbs-coeure-warns-on-challenging-future-for-londons-euro-clearing-business-post-brexit.html.

[43] The Commission has already confirmed this for a number of countries: Australia, Hong Kong, Japan, Canada, Mexico, Switzerland, Singapore, South Africa, South Korea and the USA.

A CCP authorised in the European Union under EMIR's third-country regime can also ask for access to EU trading venues (reciprocity does not have to be given).

Independently of the CCP requirements set out above, it is particularly EMIR's TR provisions which will be important in practice as a consequence of Brexit due to the notification obligations applicable to all market participants. The general process here is analogous to the process described for CCPs.

3. Recommendations

In the short term, it is important to ensure the continuing applicability of existing infrastructures of CCPs and TRs (affected: DTCC Europe) for EU clients. For this, it would be advisable to have a clarifying rule that CCPs/TRs already authorised by ESMA are "grandfathered". EMIR's functionality would be jeopardised, if all those affected had to find new solutions, which cannot be in the interest of the European Union either.

In the long term, an opening clause as in the Swiss financial market infrastructure law (FinfraG) is needed which prevents a double recording of OTC transactions for jurisdictions with comparable regulation (a necessity in both directions). Cross-border OTC transactions already notified under EMIR (or another regime recognised as being equivalent) then no longer also have to be notified additionally in Switzerland, if certain conditions are met.

In the EMIR review due this year one of the things being discussed is the idea of generally entrusting banks with the reporting for customers. Insofar as such a bank were licensed in the United Kingdom, it could in future no longer be able to carry out this reporting due to its establishment in a third country. Whereas this problem is still uncertain for EMIR, it will definitively come into play in other regulatory instruments: for instance, the reporting procedure for commodity derivatives, emission allowances and their derivatives under MiFID II as well as for the reporting on repos and other securities financing transactions (SFTR).[44] In both regulatory instruments, the bank established in the European Union has been enshrined as the responsible party. If companies had to take over these notifications themselves, considerable additional costs would be generated, in part because the relevant formats diverge from the current EMIR reporting system. Another solution could be delegation of the reporting obligation to an EU bank.

General contract law, in particular ISDA

1. Overview

Cross-border derivatives transactions are usually documented under the master agreement of the International Swaps and Derivatives Association (ISDA), but also partially

[44] SFTR: Securities Financing Transactions Regulation: Regulation (EU) No. 2015/2365 of 25 November 2015 on transparency of securities financing transactions and reuse and [...].

under the German Master Agreement for future contracts (DRV[45]) and also in certain markets under other master agreements (for example, the European Federation of Energy Traders (EFET) or the European Master Agreement (EMA)). In the case of the ISDA Master Agreement, English or New York law can be agreed, in the case of the DRV German law, and in the case of the EMA and EFET the law of various European countries.

Broadly speaking, no immediate consequences for the ISDA master agreement can be expected as a result of the United Kingdom leaving the European Union. A corresponding adaptation is likely only after the new regime enters into force. In this respect, the following problem areas in particular should be taken into account:

- Recognition of jurisdiction (Brussels I Regulation).
- Choice of applicable law (Rome I and II Regulations).
- Effects of national insolvency law, since uniform European provisions will no longer be applicable.
- Enforceability of rulings by UK courts.

2. Adaptations necessary due to Brexit?

Today these master agreements mostly already comprise standardised amendments which ensure that the parties in question meet all EMIR requirements, for instance through agreement of the ISDA EMIR protocol under the ISDA Master Agreement and the EMIR annex under DRV. For the case of Brexit, the EU Derivatives Regulation will no longer be applicable in the United Kingdom. It can be assumed that it will be superseded by British regulation which corresponds to the standard agreed in international committees. Any adjustments that may be necessary could be made through adjustment of standard contracts.

3. Recommendations

Since contractual relations are based on bilateral legal relationships, the adaptation must also be made separately for each individual contractual relationship. ISDA facilitates contract adaptation in the form that a contracting party by acceding to one ISDA protocol automatically includes it in all ISDA master agreement relationships. By contrast, legal relationships based on conclusion of DRV have to be individually adapted. From the market viewpoint, it would therefore be desirable that there is derivatives regulation which allows the continued existence of existing contracts (and is not prevented by EU law) following Brexit. We assume that this is also in the interest of market participants from the United Kingdom.

[45] DRV: Deutscher Rahmenvertrag.

Under general contract law aspects, Brexit prompts numerous questions of detail, for example:

- Choice of law clause: British law loses some of its attractiveness.
- Jurisdiction clause: London courts could lose some of their attractiveness due to the possibility of more difficult recognition for enforcement in the European Union.
- Arbitration clauses: Increasingly in demand.
- Miscellaneous standard clauses (material adverse change, force majeure, tax clauses, events of default) will have to be verified to see whether Brexit triggers unwanted legal consequences in individual cases.

5.1.5 Use case: Market infrastructure

Access of EU financial market infrastructures to clients from the United Kingdom – and vice versa – is of enormous importance, since London will continue to play a leading role as a financial centre also post-Brexit. Maintaining close cooperation with the United Kingdom will therefore be very important.

EU law will continue to be applicable in the United Kingdom during the exit negotiations. Until the definitive exit from the European Union, companies authorised in the United Kingdom will have the right to provide services such as clearing activities within the entire European Union. Following Brexit, access to the EU single market will be determined in accordance with third-country regimes in place and presupposes equivalence decisions by the European Commission and/or ESMA.

Both the European Union and the United Kingdom follow international standards.[46] Furthermore, the United Kingdom transposes EU rules, which already exist or are in implementation. The essential rules for financial market infrastructure providers are:

- MiFID II/MiFIR (will be implemented by the European Union and hence also in the United Kingsom from the start of 2018).
- EMIR (already implemented by the European Union and the United Kingdom).
- Central Securities Depositories Regulation (CSDR)[47] (currently in the process of implementation in the European Union and the United Kingdom).

In theory, therefore little stands in the way of an equivalence decision in favour of financial market rules from the United Kingdom.

---

[46] Cf. CPMI-IOSCO Principles for financial market infrastructures, which is transposed in the European Union through EMIR; the principles can be downloaded at http://www.bis.org/cpmi/publ/d101a.pdf, 2012.

[47] CSDR: Central Securities Depositories Regulation: Regulation (EU) No. 909/2014 of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and [...].

Trading venues, clearing houses and transaction registers (RMs, MTFs, OTFs, CCPs, TRs)

1. Overview

Trading venues (MiFID II/MiFIR): The fundamental mechanisms for European trade in financial instruments will be comprehensively regulated through MiFID II/MiFIR from 2018 onwards. Essential elements of MiFID II/MiFIR are the obligation on financial institutions to use trading venues when executing financial transactions as well as comprehensive transparency requirements on traders (cf. diagram 2). Furthermore, MiFIR places comprehensive governance and stability requirements on financial market infrastructures.

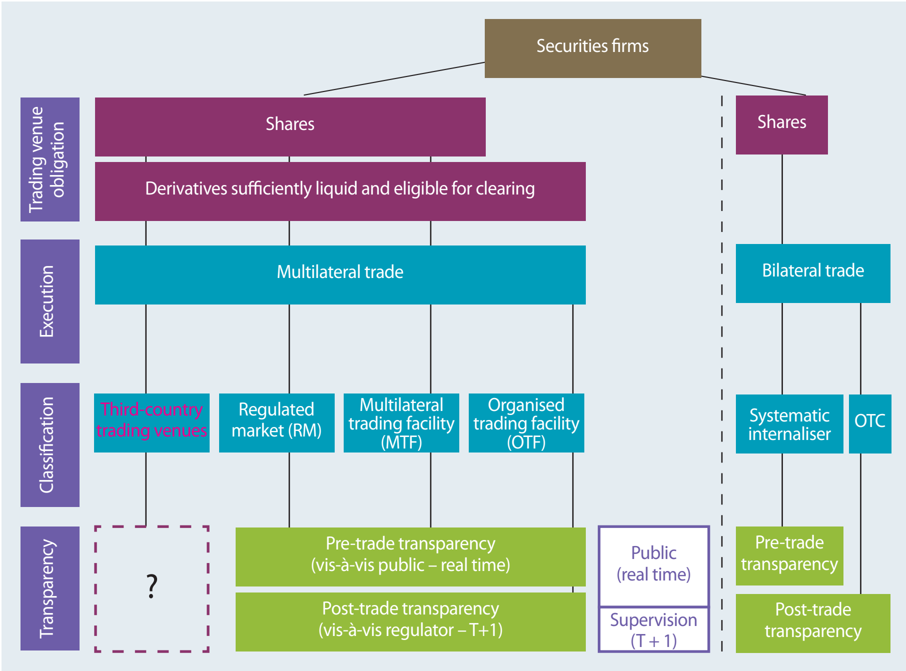


Diagram 2: Trading venue obligation and transparency requirements for shares and derivatives for trading participants under MiFID II/ MiFIR

Data provision services (APA, ARM and CTP)[48]*:* With the introduction of MiFID II, new transparency mechanisms for companies covered by the directive are introduced (cf. diagram 3). In addition, the reporting and transparency obligations currently applicable only for shares are extended to almost all financial instruments.

[48] APA: Approved Publication Arrangement; ARM: Approved Reporting Mechanism; CTP: Consolidated Tape Provider.

Diagram 3: Transparency mechanisms under MiFID II/MIFIR

Clearing houses and transaction registers (EMIR): The G20 objectives and the global CPMI-IOSCO Principles for financial market infrastructures are transposed at European level through EMIR and are accordingly also implemented by the United Kingdom. Moreover, the restructuring and settlement mechanisms of CCPs are currently extensively regulated by the European Commission so that the United Kingdom should be compatible with the EU rules until Brexit also in relation to these provisions.

2. Third-country regime

Trading venues (MiFID II/MiFIR): MiFID II/MiFIR provides a third-country regime for trading venues via an equivalence regime (cf. explanations on MiFID II/MiFIR in section 5.1.3)

Data provision services (APA, ARM and CTP): However, by contrast with trading venues, MiFID II provides no third-country regime for data provision services. Meaning that such infrastructures would have to be authorised and supervised both in the European Union and in the United Kingdom following Brexit.

Clearing houses and transaction registers (EMIR): EMIR provides a third-country regime for CCPs and TRs (cf. explanations on EMIR in section 5.1.4).

3. Recommendations

Trading venues (MiFID II/MiFIR): The complexity of the market for securities trading could increase markedly as a result of Brexit. As a third country, the United Kingdom could sidestep these complex market structures through regulatory arbitrage so that highly regulated European trading venues would be in competition with more lightly regulated trading venues from the United Kingdom for meeting the trading venue obligation. In order not to jeopardise the regulator's objective of making markets more stable and more transparent, it must therefore be very carefully verified whether the provisions in non-EU countries are implemented in an equivalent manner. For example, the list in annex 1 contains a series of rules which should be verified in the framework of equivalence decisions in relation to MiFID II/ MiFIR in order to prevent regulatory arbitrage between the European Union and the United Kingdom. But since the United Kingdom will also implement the requirements of MiFID II/MiFIR, the danger is currently manageable. At the time of Brexit, the United Kingdom is likely to be closer to the European rules than Switzerland and the USA.

Data provision services (APA, ARM und CTP): The existing regime requires third-country data provision services in the European Union to have their own authorisation. It should be borne in mind that compliance with all relevant provisions by the provider is verified during the authorisation process in order to achieve a level playing field.

Clearing houses and transaction registers (EMIR): In the context of EMIR, the complexity of the clearing market will also increase through Brexit. Here, too, the United Kingdom could try to create, through corresponding measures, a competitive advantage for British CCPs and TRs. Those could then be used more often by European market participants to meet their regulatory obligations. It should therefore be ensured that EU CCPs and TRs are not competing with less strictly regulated CCPs and TRs from the United Kingdom (for example: lower capital adequacy requirements for UK CCPs). To ensure that there is no regulatory arbitrage, the relevant areas of EMIR (cf. list in annex 1) should be verified in detail in the framework of the equivalence decision. As a reaction to Brexit, the European Union and the ECB will probably insist that clearing of euro-denominated derivatives is processed within the European Union after the United Kingdom will have left, in order to safeguard its supervision and intervention possibilities for system-relevant derivatives transactions. This would considerably restrict the third-country regime mentioned above and could lead to a relocation of clearing business in euro-denominated derivatives into the European Union.

Central depositories (CSDs)

1. Overview

Central securities depositories (CSDs[49]) offer central infrastructure functions for capital markets by ensuring that securities and securities transactions are recorded, deposited and settled. In this so-called post-trading area, various practices and provisions have over a long time led to unnecessarily high costs and risks in EU/EEA countries for cross-border transactions. In order to have uniform standards and rules across Europe, an EU Central Securities Depositories Regulation (CSDR) was adopted which is directly applicable in all EU/EEA countries.

Under the provisions of CSDR, central depository services authorised in the European Union may be provided across the entire territory of the European Union, inter alia through creation of a branch establishment. By contrast with the passporting mechanism for trading and clearing activities whereby an authorisation in one Member State directly confers the right to provides services anywhere in the European Union, a central depository must inform the supervisory authority of its home Member State of the intention to provide services in another Member State and make extensive information available (article 23 paragraph 3 CSDR). As a rule, there is only one CSD in most Member States.

2. Third-country regime

CSDR contains a third-country regime. Under article 25 paragraph 1 CSDR, CSDs have the possibility to continue to transact business across borders or establish branches in the European Union/European Economic Area, insofar as it has successfully completed the procedure in accordance with article 25 paragraphs 4 to 11 CSDR. The provision of cross-border services by CSDs or the creation of branches will be authorised by ESMA, if a comparable level of supervision exists in the country in which the services are provided or in which the headquarters are located. In concrete terms, ESMA will have to verify the following in the framework of the third-country regime:

- Confirmation of the equivalence of the national provisions then applicable in the United Kingdom with those of CSDR through a decision of the European Commission.
- The concerned CSD from the United Kingdom is properly authorised and supervised/monitored there.
- A cooperation between ESMA and the competent national British supervisory authority exists.

[49] CSDs: Central Securities Depositories.

Should it be necessary, the CSD in question must take all necessary steps to enable its users to comply with the applicable national rules of the EU/EEA countries. That can be important because CSDR contains supervisory requirements but no (substantive) securities law requirements, an area which so far has been reserved for the Member States alone. The corresponding EU regulation project (SLL)[50] has not moved forward in recent years (because of disagreement between countries with a securities system governed by property law, such as Germany, and those with a system governed by contract/trust law, such as the USA or Switzerland), a situation which could however change in the framework of the EU Capital Markets Union. In this case, it would be important that the content of this reform is constructed on the basis of the Geneva Securities Convention.

Nevertheless, a third-country authorisation for CSDs resident in the United Kingdom would go hand in hand with a considerable administrative, cost and time effort which would not be offset by any increased security on securities markets. The procedure for authorisation of a CSD resident in a third country alone can take up to six months (cf. article 25 paragraph 6 sentence 7 CSDR). That is also a difficult threshold for CSDs from the United Kingdom targeting a third-country regime, as in accordance with article 69 paragraph 3 CSDR they can only submit an application within six months, calculated from the later of either (i) entry into force of a particular RTS or (ii) a European Commission's implementing decision on equivalence (article 25 paragraph 9 CSDR).

3. Recommendations

Against this background, consideration could be given to protecting existing British CSD authorisations in the European Union/European Economic Area following Brexit (for example in the exit agreement), insofar as the United Kingdom continues to ensure a level of supervision corresponding to CSDR.

5.1.6 Use case: Funds

1. Overview

The existing regulatory regime in the United Kingdom for asset management is based essentially on EU directives, in particular the Directive on Undertakings for Collective Investment in Transferable Securities (UCITS)[51], MiFID II/MiFIR and the Directive on Alternative Investment Fund Managers (AIFMD)[52].

Given their function as intermediaries, asset managers are essential components of a functioning capital market ecosystem, in particular for the structuring and distribution of liquidity/capital.

---

[50] SLL: Securities Law Legislation. Cf. for example at http://ec.europa.eu/smart-regulation/impact/planned_ia/docs/2009_markt_050_securities_law_en.pdf.

[51] Directive No. 2014/91/EU of 23 July 2014 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) [...].

[52] Directive No. 2011/61/EU of 8 June 2011 on alternative investment fund managers [...].

Since the United Kingdom will probably review its provisions as a result of Brexit, it is very important for the upcoming negotiations and for the transition process that the fiduciary asset management activities which take place between the United Kingdom and other European countries can continue as far as possible in the interest of investors.

This is also in the common interest of the European financial market. For instance, UCITS funds are regarded as a globally recognised synonym for harmonised EU provisions in asset management which meet the highest standards and are successfully established internationally. Even if large portions of these funds are domiciled in Luxembourg or Ireland, the issue of market access for all asset managers active in the European Union is relevant.

With regard to the high market share of UK companies in the trade in financial instruments in the entire European Union, it is important for asset managers across Europe to preserve the necessary access to the UK market and the large number of market participants from the United Kingdom. There is otherwise a risk of negative consequences for the necessary transactions of asset managers with other market participants, in particular to ensure the best possible execution of transactions for the benefit of clients.

2. Third-country regime

In addition to possible equivalence regimes in particular under MiFID II/MiFIR, there is the possibility for the European Commission under AIFMD to grant a third-country passport. In this regard, the European Commission's decision is built on a recommendation from ESMA which evaluates the regulatory regime of the third country in question. A number of countries have already gone through this process, and ESMA has given the European Commission a positive recommendation, e.g. for Canada, Guernsey, Japan, Jersey and Switzerland. However, the European Commission has not yet granted the third-country passport under AIFMD. Conversely, UCITS does not yet comprise any third-country regime.

A further post-Brexit scenario could be that UK-based asset managers which want to continue selling their products to EU investors under private placement provisions, relocate the seat of the investment fund and the sales platform into an EU country (for example Luxembourg or Ireland) with the possibility of delegating management to their operations centre in the United Kingdom.

3. Recommendations

The existing third-country regimes under MiFID II/MiFIR and AIFMD must actually be put into practice and must not remain a theoretical construct. In addition, thought should be given to implementing a comparable equivalence regime for UCITS.

5.1.7 Use case: Securities prospectuses

General points on prospectus and stockmarket admission law as well as issuer access to primary and secondary markets

1. Overview

Issuers which offer securities publicly in the European Economic Area or want securities to be listed for trading on a stockmarket in the European Economic Area are essentially required under the provisions of the Prospectus Directive and the national prospectus law (e.g. the German securities prospectus act WpPG[53]) to draft a prospectus, gain approval of the component EEA authority and publish it. The securities prospectus must correspond to Europe-wide harmonised requirements of the current Prospectus Regulation. Efforts are currently being made to reach a more profound harmonisation of requirements on prospectuses, the approval procedure and exemptions from the prospectus obligation in the framework of the EU Capital Markets Union via adoption of a new Prospectus Regulation which is intended to replace the current Prospectus Directive, the current Prospectus Regulation and parts of the national provisions (such as the German WpPG).

A securities prospectus which has been approved by a competent EEA authority can be notified in other EEA countries and used there for a public offering or a stockmarket listing without further examination by the authority of the receiving country (passporting). For instance, the IPO prospectus of a German issuer which has been approved by the German financial regulator BaFin can be notified to the authority of the United Kingdom.

However, if implementation of the new Prospectus Regulation is not transformed into UK law before current EU law is disabled by the "Great Repeal Act", differences between the corresponding EU and UK provisions could arise within a very short time.

2. Third-country regime

If the United Kingdom leaves the European Union, companies resident there will be treated as third-country issuers. In Germany the WpPG contains a third-country regime which provides that BaFin can approve a third-country issuer's prospectus for a public offering or a stockmarket listing in Germany (discretionary decision), provided that it has been drawn up in accordance with the rules applicable for third-country issuers and corresponds to IOSCO disclosure standards. Moreover, the applicable information obligations have to be equivalent to the requirements of WpPG and the prospectus regime, also in relation to financial information. Inasmuch, German law already comprises a possibility, in theory at least, for UK issuers to apply for approval in Germany of a prospectus based on the then applicable British provisions also post-Brexit, and then to notify the prospectus approved also in other EEA countries.

Nevertheless, no use has so far been made of this regime in practice. Rather, third-country issuers have drafted prospectuses for offerings and stockmarket listings in

[53] WpPG: Wertpapierprospektgesetz.

Germany, which from the outset correspond to the requirements of WpPG and the prospectus regime, since this has been the more rapid and legally certain route. In addition, this regime only offers a way for UK issuers into the European Union, but not a way for EU issuers into the United Kingdom. Lastly, this regime also does nothing to alter the fact that two separate approval procedures are necessary, if a UK issuer wanted to carry out a public offering both in the United Kingdom and in Germany. Similarly, EEA issuers which offer securities publicly or gain a stockmarket listing in the United Kingdom would have to carry out a separate approval procedure there (unless the United Kingdom recognises EEA-approved prospectuses).

3. Recommendations

The European debt and equity capital markets are strongly shaped by UK investors. Many financially strong institutional investors are resident exclusively in the United Kingdom or have their European headquarters there. This means that access to the UK capital market for EU issuers is of great importance, in particular for the take-up of debt through bond issues. For that reason, it must be an overarching objective of the negotiations in particular to structure access to the UK capital market for EEA issuers in the least complicated way possible. Access to the EEA capital market for UK issuers is also desirable.

We discuss in more detail below access to the UK capital market for EEA issuers, then access to the EEA capital market for UK issuers, and lastly examine the prospectus requirements as such.

Access to the UK capital market for EEA issuers

1. Overview

Passporting of prospectuses into the United Kingdom has not been of particular relevance for European issuers in practice. Most public offerings of equity or debt capital instruments by issuers are not notified in the United Kingdom. Instead, e.g. German issuers (and the accompanying issuing banks) regularly use exemptions from the prospectus obligation (in particular for placements exclusively with institutional investors and so-called qualified investors). The most important exemptions (including the exemption for placements with institutional investors) are in practice often jointly classified under the heading of "private placements". These exemptions are uniformly specified in the Prospectus Directive and in the new Prospectus Regulation and have been established over many years of practice. On the basis of these exemptions, German issuers have simple access to UK investors.

Inter alia, important exemptions include:

- Offerings to qualified investors in the United Kingdom.
- Offerings to fewer than 150 non-qualified investors in the United Kingdom.
- Denominations of 100,000 euros or more.

- Offerings which provide for a minimum amount of 100,000 euros per investor.
- Offerings to employees.

2. Third-country regime

The EU third-country regime contains stipulations only for access of third-country issuers into the European Union but not vice versa. EEA issuers which want to offer securities or be listed on a stockmarket in the United Kingdom must therefore carry out a separate approval procedure – unless the United Kingdom in future recognises EEA-approved prospectuses (cf. also the explanations on third-country regimes for prospectuses in previous sections).

3. Recommendations

From the angle of providing companies with capital and hence financing innovation and jobs, it would be ideal, if the current uniform prospectus regime including passporting were maintained. There may possibly be certain exceptions or special constellations in which passporting into the United Kingdom is of particular interest for EU issuers. Accordingly, there is at least a considerable interest in the requirements on prospectus content in the United Kingdom running parallel to requirements in the EU post-Brexit.

If this is not possible, it is of considerable importance for EU issuers that at least the exemption regime for institutional placements and other placements exempted from the prospectus obligation in the United Kingdom remain in force post-Brexit to the extent possible. This encompasses the relevant exemptions from the prospectus obligation and the relevant terminology of these exemption provisions. It is desirable that the current concepts and definitions are maintained so that internal guidelines, IT systems and established practices of issuing banks do not have to be adapted in order to meet a separate and different UK standard in addition to the EEA standard. It seems quite natural that the United Kingdom would also want to preserve this exemption regime to a large extent in order to maintain the current possibilities for UK investors post-Brexit.

Access of UK issuers to EEA capital markets

1. Overview

In practice, passporting of UK issuers for example into Germany does not play an important role. There may possibly be certain exceptions or special constellations in which passporting from the United Kingdom into Germany or other EEA countries (e.g. Luxembourg) is of particular interest. At the same time, it seems quite natural that the United Kingdom will have an interest in the exemption regime (in particular for placements with institutional investors) continuing so that UK issuers have access to institutional investors within the EEA.

2. Third-country regime

See earlier explanations regarding third-country regimes for prospectuses.

German law for example comprises a possibility for UK issuers to apply for approval in Germany of a prospectus drawn up in accordance with the then applicable British provisions also post-Brexit, and then to have the prospectus notified also in other EEA countries (cf. the associated conditions for this procedure in earlier sections). Lastly, this regime also does nothing to alter the fact that two separate approval procedures are necessary, if a UK issuer wanted to carry out a public offering both in the United Kingdom and in Germany.

3. Recommendations

From the angle of providing companies with capital and hence financing innovation and jobs, it would be ideal, if the current uniform prospectus regime including passporting were maintained (cf. the explanations on prospectus law in earlier sections). An interest on the part of the United Kingdom in preserving passporting (e.g. to Luxembourg) and the exemption regime can be used in the framework of the negotiations.

Requirements on the content of securities prospectuses

1. Overview

The Prospectus Directive (in future: the new Prospectus Regulation) establishes a uniform disclosure standard for securities prospectuses in the EEA. This uniform disclosure standard is the basis for passporting.

2. Third-country regime

Following Brexit and after withdrawal from the agreement on the EEA, this uniform disclosure standard will no longer be automatically applicable in the United Kingdom. The consequence would be that a divergent disclosure regime could develop in the United Kingdom. The basis for passporting would then also cease to apply; in addition, liability risks for EU issuers which make institutional placements in the United Kingdom on the basis of prospectuses could arise due to meeting only the EEA prospectus disclosure standard which will then be divergent. As such, the German WpPG third-country regime described above offers no solution for this problem because it presupposes equivalence of disclosure obligations in the third country but offers no instruments for creating or ensuring this equivalence (cf. also the explanations on third-country regimes for prospectuses in earlier sections).

3. Recommendations

There is an essential interest among EU issuers that the prospectus disclosure standard continues to be uniform also in the future. Even if the EEA prospectus is not notified, EEA prospectuses are often used in the framework of institutional placements in the United Kingdom. A uniform disclosure standard would protect EU issuers from increased liability risks due to divergent disclosure standards which could arise. In addition, the continuation of equivalence in disclosure standards would help to ensure that EU issuers have simpler market access for public offerings and stockmarket listings in the United Kingdom, if passporting ceases to apply post-Brexit. Equivalent disclosure standards would make it easier for EU issuers to gain prospectus approval not only from their national supervisory authority but also additionally from the United Kingdom authority in the future.

Nevertheless, it seems likely that disclosure standards will develop broadly in parallel even without an explicit agreement on equivalence in the framework of the negotiations. An international disclosure standard based on the materiality principle has developed so that, for example, institutional placements in the United States are regularly carried out on the basis of EEA prospectuses (prepared by means of EEA disclosure standards).

5.1.8 Use case: Transparency regime

Transparency obligations for listed companies

1. Overview

The Transparency Directive[54] aims to improve the information that has to be made available to investors via issuers of securities which are authorised for trading on a regulated market in the EEA. The Transparency Directive and the national provisions adopted for their implementation (e.g. the German securities trading act WpHG[55]) require EEA issuers in particular to publish regular financial information. In addition, they provide publication obligations with respect to voting shares for issuers. The national implementing rules of the home country are applicable and the competent supervisory authority in the home country monitors compliance with these provisions. For German issuers whose shares are listed on the regulated market of a German stockmarket, WpHG is applicable and BaFin is the competent supervisory authority.

2. Third-country regime

An explicit third-country regime does not exist; rather, the transparency obligations also relate to issuers from third countries in predefined constellations (a particular criterion here is the authorisation of the third-country issuer's financial instruments on a regulated market within the European Economic Area). Third-country issuers are granted

[54] Directive 2013/50/EU of 22 October 2013 amending Directive 2004/109/EC, Directive 2003/71/EC and Directive 2007/14/EC.
[55] WpHG: Wertpapierhandelsgesetz.

a permit to issue securities and/or derivatives only if they also comply with associated transparency and other provisions. For persons or companies in the United Kingdom which hold notifiable instruments in relation to German publicly listed issuers, the Transparency Directive's notification obligations in relation to voting rights also continue to apply because these obligations are applicable irrespective of the geographical residence of the person or company in question.

Whereas the validity of the Transparency Directive lapses for the United Kingdom with Brexit, the associated implementing law remains unaffected. Overall, we assign only minor importance to the theme for example for German issuers because, on the basis of publicly available information, there appear to be only a few German issuers whose shares are authorised both on a stockmarket in Germany and on a stockmarket in the United Kingdom. For EU issuers with an authorisation only in the European Union, nothing will change post-Brexit; they continue to fall under the regime of the Transparency Directive. Nevertheless, EU issuers with an additional stockmarket authorisation in the United Kingdom will be subject to a transparency regime which will then be divergent post-Brexit. In spite of this, this is likely to be of secondary importance in practice, in part because there are only a few issuers with a dual listing in the United Kingdom and in part because these issuers have hitherto already been subject to special UK listing rules, since stockmarkets in the United Kingdom usually have their own comprehensive authorisation rules (which also encompass post-listing disclosure obligations in particular). In our view, this aspect could nevertheless gain particular relevance if, post-Brexit, the United Kingdom introduces stricter disclosure rules for EEA issuers whose bonds are listed on a stockmarket in the United Kingdom.

3. Recommendations

From the angle of EU issuers with a stockmarket authorisation also in the United Kingdom, it is desirable that the European transparency regime also continues to be applicable in the United Kingdom. Nevertheless, this point seems to us not to be very important for the reasons set out above. The minimum objective should be that the United Kingdom undertakes not to place any stricter transparency obligations on issuers with authorised bonds on UK stockmarkets than those laid down in the Transparency Directive. However, since the British government has announced an easing rather than a tightening of rules, the danger of such a tightening appears small.

Obligations to notify voting rights of issuers, whose shares are listed on a regulated market

1. Overview

Persons or companies holding voting rights in issuers, whose shares are listed on a regulated market in the EEA, must issue voting rights notifications to issuers and the competent supervisory authority when they reach, exceed or fall below certain threshold values. This also applies for certain derivative instruments which relate to the shares of these issuers.

2. Third-country regime

An explicit third-country regime does not exist. Rather, the obligations to notify voting rights in the Transparency Directive also continue to apply for persons and companies in the United Kingdom which hold instruments eligible for notification in relation to German stockmarket-listed issuers because these provisions are applicable irrespective of the geographical residence of the person or company in question.

Conversely, the applicability of the Market Abuse Regulation (MAR)[56] for the United Kingdom lapses with Brexit. Local market abuse rules will have to be followed in the case of investments in financial instruments listed on British stockmarkets. (cf. section 5.1.9 on market abuse).

3. Recommendations

For EU issuers, it is desirable that the European voting rights notification regime also continues to be applicable in the United Kingdom (i.e. EU holders of instruments eligible for notification in relation to UK issuers continue to be subject to the Transparency Directive's notification obligations in relation to voting rights). Nevertheless, this point does not seem to be very important, because it is ensured anyway post-Brexit that the voting rights notification obligations of UK investors in relation to EEA issuers continue to be based on the Transparency Directive.

Should the United Kingdom introduce its own disclosure regime in relation to voting rights in UK issuers, this would affect EU investors with instruments eligible for notification in relation to UK issuers; they would then have to comply with the separate UK rules. Nevertheless, we do not assess the resulting additional requirements or disadvantages as very serious because the national EEA regimes already diverge in many details from each other – even though they are based on the same directive – so that EU institutional investors either are already familiar with the particularities of the UK transparency regime for voting rights or have to contact UK legal advisers.

5.1.9 Use case: Market abuse

Market abuse, insider rules, market manipulation, ad-hoc publicity

1. Overview

The Market Abuse Regulation will broadly also continue to be applicable post-Brexit to UK investors and market participants that trade in securities which are listed on a regulated market or a MTF in the European Union. This relates in particular to the insider regime and the market abuse regime. Protection of market integrity through these provisions will not be directly impaired.

[56] MAR: Regulation (EU) No. 596/2014 of 16 April 2014 on market abuse and repealing [...].

2. Third-country regime

An explicit third-country regime does not exist. The provisions of the Market Abuse Regulation on ad-hoc publicity and on directors' dealings are applicable to all issuers (i.e. also to third-country issuers) – independently of where they are established – whose securities are listed on a regulated market in the EEA or a MTF (in future also an OTF) which has been listed with the consent of the issuer. Hence, the Market Abuse Regulation already provides a regime for third-country issuers which will also be applicable post-Brexit to issuers from the United Kingdom with such "EU" listings, as it is already applicable to other third-country issuers.

3. Recommendations

For EU issuers, it is desirable that the European market abuse regime continues to be applicable in the United Kingdom. It is probable that the United Kingdom's market abuse rules will diverge from the EEA regimes with the passage of time. Such a development would lead to EEA investors and issuers with a UK listing having also to comply with the UK regime as well as the EEA regime. Nevertheless, we expect that the fundamental substance will remain unchanged. However, it should be borne in mind that this could in future result in conflicts between British and European data protection rules, for instance in the framework of holding insider lists in accordance with the provisions of the Market Abuse Regulation (inter alia inclusion of personal data).

By contrast, this point is hardly important for EU companies for a listing in the EU market, because the EEA market abuse regime will continue to be applicable to UK investors trading in securities of EEA issuers post-Brexit and issuers from the United Kingdom with an EEA listing will then continue to be subject to the ad-hoc and directors' dealings regime of the Market Abuse Regulation.

Market Sounding

1. Overview

The Market Abuse Regulation comprises provisions for market sounding, which is approaching selected persons ahead of capital market transactions, in order to assess the prospects of a transaction being successful. Compliance with these provisions protects banks which carry out market sounding against the infringement of insider bans. The market sounding rules are detailed and require standardised documents, policies and practices.

2. Third-country regime

The MAR does not contain any specific third-country regime in relation to market sounding. Rather, the market sounding provisions of the Market Abuse Regulation are applicable, if the market sounding relates to an issuer, whose financial markets are listed on a regulated market, a MTF or (in future) OTF within the European Economic Area. If this condition is met, the market sounding provisions of the MAR apply regardless of the jurisdiction in which or with which investors the market sounding is carried out. Market sounding activities in relation to transactions of German issuers are often conducted specifically with UK investors. In this case, the market sounding provisions of the Market Abuse Regulation will still have to be followed post-Brexit. Nevertheless, a special UK regime for "UK-inbound" market soundings could develop post-Brexit which might possibly diverge from the MAR regime or even be incompatible with it.

3. Recommendations

From the angle of EU market participants, it is desirable that uniform market sounding provisions continue to apply also post-Brexit in the European Economic Area and the United Kingdom. Market sounding has become an established component of successful capital market transactions and is therefore of considerable importance for issuers and issuing banks. For EU issuers, it is an essential success factor for issuing banks to be able to conduct market soundings also in the United Kingdom. Issuing banks must develop standardised policies, documentation and practices in order to be abl to ensure compliance. A divergent regime in the United Kingdom which places requirements for market soundings on European issuers which go beyond the MAR or they are incompatible with it would further increase compliance costs, the associated effort and the risk of an infringement.

5.1.10 Use case: Benchmarks

1. Overview

The EU regulation on indices used for financial instruments and contracts as benchmarks or to measure the performance of an investment fund (Benchmark Regulation[57]) becomes applicable from 1 January 2018. The European Commission proposed the Benchmark Regulation in September 2013 as a consequence of the Libor manipulation scandal. The regulation is intended to improve the functioning and the management of the benchmarking process and to ensure that benchmarks defined and used in the European Union are robust, reliable, representative and appropriate, and cannot be manipulated.

2. Third-country regime

The Benchmark Regulation contains different possibilities for benchmark providers from third countries which provide their indices inside the European Union.

[57] Regulation (EU) 2016/1011 of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds [...].

In order that benchmarks of companies in the European Union and originating in third countries can be used, the principle also applies under the Benchmark Regulation that the European Commission must first issue a positive decision on the equivalence of the third country's system (equivalence decision) and that the third-country benchmark provider must be registered with ESMA. Since it cannot be assumed that Brexit will be completed before the Benchmark Regulation becomes applicable in January 2018, the United Kingdom should have implemented the Benchmark Regulation at national level by then and a basis for an equivalence decision in favour of the British regulatory regime should be a given. Nevertheless, the decision with regard to equivalence lies within the European Commission's discretion and could also be politically influenced depending on how the exit negotiations between the European Union and the United Kingdom evolve. In addition, there is a danger that the European Commission can revoke an equivalence decision at short notice at any time so that it is questionable whether this route constitutes a real alternative to an EU passport (cf. explanations on third-country regimes in section 5.1.2). However, the Benchmark Regulation also provides temporary measures for the period leading up to an equivalence decision by the European Commission (namely recognition and endorsement) in order to prevent disruptions through a possible abrupt suspension of the use of benchmarks originating from a third country in the European Union.

The recognition procedure allows benchmark providers to provide their indices inside the European Union, if they demonstrate vis-à-vis the competent authority of the Member State that its indices comply with the IOSCO principles as a global standard for preparing benchmarks and the latter are therefore equivalent to meeting the various requirements under this regulation. The Benchmark Regulation also introduces an endorsement mechanism which allows benchmark providers established in the European Union to endorse benchmarks which originate from a third country so that they can be used in the European Union. For this, the component authority checks whether compliance with the IOSCO principles is equivalent to compliance with this regulation for the benchmarks to be endorsed.

For instance, consequences of Brexit arise for Libor quotations which in future constitute third-country benchmarks so that their applicability inside the European Union depends on confirmation of equivalence by ESMA (cf. article 3 paragraph 1 number 24 Benchmark Regulation).

3. Recommendations

In order to safeguard the use of UK benchmarks also in the future, we recommend a consistent application of the third-country regime of the Benchmark Regulation under the condition that the United Kingdom continues to ensure a supervisory and legislative framework equivalent to the European stipulations.

5.1.11 Use case: Insurance services

1. Overview

The Solvency II Directive gives branches of EU insurance companies the possibility of home-country authorisation and control – for both direct insurance and reinsurance.

The United Kingdom had a considerable influence on the development of the Solvency II Directive and CRD IV, so that it can be assumed that the future supervisory regime for insurers should broadly correspond to the EU standard

2. Third-country regime

With Brexit, branches of EU insurers lose the privilege of recognition of home-country recognition and control. Rather, they will then need local authorisation and be subject to the full extent of British supervision. In some cases, this may also encompass meeting local capital requirements.

British subsidiaries of European insurers will continue to be covered by group supervision also after Brexit. Conversely, recognition by the British regulator as group supervisor of a German subsidiary of an insurance group with seat in the United Kingdom presupposes that the European Commission or, in some cases, the national authority recognises the equivalence of the supervisory regime. In addition, British subsidiaries will be subject to the future UK supervisory law.

UK reinsurers will preserve easier access to the EU market, if equivalence of the UK solvency system for reinsurance is recognised by the European Commission as being equivalent to the EU standard. The licence requirement for cross-border business lapses in this case in accordance with article 172 Solvency II Directive (and in Germany § 67 paragraph 1 sentence 2 VAG) (cf. also section 5.1.3 on financial, banking and securities services).

3. Recommendations

We recommend an extension of the scope of the Solvency II Directive to include direct insurances to allow not only a limited portion of private and corporate business to be covered. In addition, the existing third-country regime for reinsurance should also be implemented consistently.

5.2 SUPERVISION

5.2.1 Problem definition

The Transparency Directive, the Prospectus Directive and the Market Abuse Regulation provide for close cooperation between the various EU regulators and supervisory authorities. However, with Brexit, these instruments and others will no longer apply in the United Kingdom. Cooperation will therefore no longer be obligatory but will be at the discretion of the various supervisory authorities.

In addition, the United Kingdom will no longer be part of the ESAs or the EU Supervisory College. This also leads to the question of where to relocate the headquarters of EBA. Frankfurt would be a logical choice here, since there would then be a geographical proximity to ECB and to EIOPA. However, other EU Member States have also positioned themselves on this question. European Parliament rapporteur Sylvie Goulard and others spoke in favour of the single location of Frankfurt am Main for all European financial supervisory authorities as long ago as 2010.[58]

5.2.2 Recommendations

Close cooperation between national supervisory authorities and the ESAs with the British supervisor is of great importance after Brexit. Only in this way can be ensured that sensible solutions for EU companies and investors are identified or developed. Establishment of such close cooperation should be a core demand of the European Union.

For example in Germany, BaFin could agree a memorandum of understanding with the UK supervisor (as has already been agreed with other supervisory authorities in third countries). However, this is only possible for national authorities like BaFin, if the stage has been set at EU level. In addition, such cooperation is a fundamental condition for the applicability of third-country regimes.

In order for such cooperation to be possible, supervision standards must be as equivalent as possible (no negative competition between supervision rights), there must be no discrimination against "foreign" companies and the greatest possible approximation of systems must be the aim in order to facilitate recognition.

[58] Cf. European Parliament's Committee on Economic and Monetary Affairs, draft report of 10 February 2010 on the proposal for a regulation on community oversight, 2009/0140 (COD).

6 COMPANY LAW

In company law, a relatively high degree of legal harmonisation and flexibility in cross-border legislative flows has now been secured on the basis of freedom of establishment as one of the four fundamental EU freedoms as well as through harmonising EU legislative acts. In the case of Brexit, these achievements run the risk of being lost in relation to the United Kingdom.[59]

6.1 RECOGNITION OF COMPANIES ESTABLISHED IN THE UNITED KINGDOM

6.1.1 Problem definition

In the case of Brexit without the involvement of the United Kingdom in the European Economic Area and without a special transitional regime, the freedom of establishment enacted in Union law will lapse in relation to the United Kingdom. In this case, under the "seat theory" that among others prevails in Germany and France[60], the corresponding national law would be applicable to companies which have a British legal form but whose main business activities and administrative headquarters are in one of these countries. As a result, in the absence of recognition of the British legal form of the respective entity (for instance the legal form of an Limited Liability Company), in Germany for example these companies would have to be treated as a legal form present under German company law, such as e.g. a German GbR or a German oHG.[61]

➜ **One of the consequences would be unlimited liability of shareholders vis-à-vis third parties, even for inherited liabilities. In the area of taxation, both taxation of the change of form as such and a modification of current taxation could be necessary.**

The scenario described above relates to companies whose business activities are primarily in Germany and which are accordingly de facto German businesses, even if they use a British legal form. It is not only these companies and their company members that are affected by this scenario but also those companies which are associated with these companies within a corporate group or have business relations with these companies.

---

[59] However, Brexit offers a good opportunity to reorganise international company law in Germany. This would be generally welcome, independent of Brexit, first and foremost with regard to partnerships (Personenhandelsgesellschaften) whose legal situation is currently completely unclear. However, this issue is not further examined here.

[60] Other EU member states also deploying the seat theory are for example Luxembourg, Austria, Portugal, Spain and Italy. In the following German examples will be used to describe the difficulties arising in countries deploying the seat theory.

[61] The British company becomes an oHG, if the conditions set out in § 105 HGB in conjunction with §§ 1 and 2 HGB are met. Otherwise, it becomes a GbR.

6.1.2 Details and examples from corporate practice

Even following the reform of law regulating the German corporate form of GmbH[62] in 2008 through MoMiG[63], the legal form of the British limited company continues to enjoy great popularity for undertakings active in Germany.

In early 2016 almost 9,000 undertakings were recorded in German trade registers in the legal form of a British limited company ("Limited") and around 2,800 undertakings in the legal form of a "Limited & Co. KG".[64]

For many of these undertakings, it can be assumed that they have their real administrative seat and the core of their business activities in Germany. This high number of Limiteds and Limited & Co. KGs in Germany shows that there clearly continues to be a need for this flexible legal form in business flows. This applies not only for very small and weakly capitalised businesses which want to avoid the costs of founding a GmbH. There are also well regarded larger undertakings which make use of a British legal form although their de facto seat and centre of activities are not in the United Kingdom but in Germany.

In German law, the question of the legal treatment of a company in Germany arises against the background that the German Federal Court (BGH[65]) represents the so-called "seat theory" whereas ECJ represents the so-called "incorporation theory":

- Under the seat theory, it is assumed that the question of which legal form a company has is determined under the law of the State in which the company has its real administrative seat. For instance, if a Limited (which has effectively been founded in England) relocates its real administrative seat to Germany, its legal form is determined in accordance with German law by German courts due to the relocation of seat. Without the influence of European law (freedom of establishment) – as it will be the case after Brexit – this company would be treated as a partnership under civil law (this means in particular with personal liability of company members) due to failure to meet the foundation provisions for a German GmbH in Germany.

- By contrast, under the incorporation theory, the legal form of a company is oriented on the law of the State in which the company was legally founded, complying with legal provisions in force there. Relocating the real administrative seat across the border does not have the consequence that the legal capacity already acquired is lost through the relocation of seat. For instance, if a British Limited (which has effectively been founded in the United Kingdom) relocates its real administrative seat to another EU Member State, its legal form and capacity are determined from the perspective of British company law before and after Brexit by the law of the incorporation state, i.e. British law.

[62] GmbH: Gesellschaft mit beschränkter Haftung.
[63] MoMiG: Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchenn (German act to modernise the law on private limited companies and combat abuses), 23 October 2008.
[64] Cf. Kornblum, GmbH Act 2016, page 692.
[65] BGH: Bundesgerichtshof.

Under ECJ case law, the state of destination has to recognise the legal capacity of the incoming company.[66] ECJ justifies this by reference to preserving the freedom of establishment enshrined in articles 49 and 55 TFEU. As a result, the incorporation theory applies across the European Union and thus displaces the seat theory in Germany. This means that a British Limited relocated to Germany is recognised as such in Germany as long as the United Kingdom is a member of the European Union.

With the United Kingdom's departure from the European Union, the British companies in question with their headquarters in Germany will no longer fall within the scope of the incorporation theory. BGH ruled in 2008 on the relationship between Germany and Switzerland that the legal capacity of companies which have been founded in a third country which neither belongs to the European Union nor is equivalent with respect to establishment on the basis of treaties (for instance the European Economic Area) should be assessed under the seat theory.[67] If we transpose BGH's case law to the Brexit scenario, this means that British companies would have to be treated under the law of the state in which they have their real administrative seat so that a British Limited would have to be treated as a German GbR or oHG. This would lead to personal liability of the Limited's shareholders which should actually be avoided through the foundation of a Limited.

A comparable legal situation would arise for British companies also in the other Member States applying the seat theory in cases where the incoming company has been founded in a state outside the European Union or the European Economic Area.

In the case of an Einmann-Limited, i.e. a Limited, which has just one company member, a further result would probably be the legal transfer – often cross-border – of the assets and obligations of the company dissolving with Brexit through a so-called "accretion" to the sole shareholder.

In addition to this often unwanted outcome another factor is that the legal situation looks completely different from the angle of British law in cases of doubt. There, an Einmann-Limited would continue to be effectively recognised on the basis of the incorporation theory so that nothing at all happens from the viewpoint of British law and the assets continue to be assigned to the Limited (and not to its sole company member). The consequences are therefore contradictory legal assignments of ownership of and liability for the assets and obligations in question.

6.1.3 Recommendations

It would be advisable to agree the continuing validity of the incorporation theory (i.e. recognition of companies effectively founded in the state of incorporation) in the framework of the exit agreement with the United Kingdom. Inspiration for this could be drawn from the example of the 1954 "Treaty of friendship, commerce and navigation" between the Federal Republic of Germany and the United States of America in which it was agreed that compa-

[66] Cf. especially ECJ Vol. 1999, I-1459 "Centros" and Vol. 2002, 9919 "Überseering".
[67] Cf. BGH ruling of 27 October 2008 – II ZR 158/06 "Trabrennbahn".

nies constituted under the applicable laws and regulations within the territory of one party are deemed as companies thereof: Thus, their legal status is recognised in the territory of the other party.[68] It is important at least to agree a "grandfathering" provision, i.e. protection of the continued existence of companies which already exist at the time of the United Kingdom's exit from the European Union.

In addition, thought should be given to the recognition of the British company within the European Union being made dependent on the United Kingdom continuing to orient itself on the stipulations of harmonising legislative acts of EU company law in British company law, similarily to the equivalence principle. In this way, the United Kingdom could possibly have an incentive to maintain the status quo of legislative harmonisation and not to trigger a "race to the bottom" with regard to company law requirements on the protection of creditors and minority shareholders (so-called "Delaware-effect"). If this approach is followed, ECJ would have to be given the final competence to reach decisions on whether the requirements of such an equivalence principle are being met by the United Kingdom in cases of doubt.

6.2 CROSS-BORDER MERGERS

6.2.1 Problem definition

The EU legislator has opened up the possibility for a cross-border merger between limited liability companies with the Mergers Directive.[69] In this regard, the Mergers Directive and its transposition e.g. into the German act for the transformation of companies (UmwG[70]) specify the condition that the companies in question are located in the European Union/European Economic Area. In the case of Brexit, this possibility of a simplified cross-border merger of companies would lapse with respect to the United Kingdom insofar as no divergent provisions are agreed in the framework of the exit negotiations.

6.2.2 Details and examples from corporate practice

The Mergers Directive was transposed by the German legislator in §§ 122a – 122l UmwG. Employee participation is oriented in Germany on the act on co-determination of employees in a cross-border merger (MgVG[71]). The directive and the provisions on employee participation were transposed in the United Kingdom through the Cross-Border Merger Regulations.[72] These provisions enable the cross-border merger of limited liability companies via a procedure which is at least largely harmonised. The procedure markedly simplifies the merger of companies and the streamlining of organisational structures.

[68] Cf. article XXV fifth paragraph of the Treaty on friendship, commerce and navigation, 1954.
[69] Directive 2005/56/EC of 26 October 2005 on cross-border mergers of limited liability companies.
[70] UmwG: Umwandlungsgesetz.
[71] MgVG: Gesetz über die Mitbestimmung der Arbeitnehmer bei einer grenzüberschreitenden Verschmelzung.
[72] The Companies (Cross-Border Mergers) Regulations of 2007.

Cross-border mergers definitely play a weighty role in legislative flows with the United Kingdom. An evaluation carried out for this position paper of entries in the British Companies House[73] and the publication "The Gazette"[74] found that there was a total of 39 cross-border mergers involving British companies as ceding or absorbing businesses in 2016 alone; of these, 16 cases of cross-border mergers with German companies and mainly mergers originating in the United Kingdom with German target companies (13 cases). What this reveals is that, from the viewpoint of EU companies, there is clearly a practical need to maintain this EU-wide harmonised form of cross-border restructuring in relation to the United Kingdom.

Furthermore, the legislative instrument of the cross-border merger of regulated companies from the financial sector with company seat in the United Kingdom and with establishments in the other EU Member States could help reacting to a possible cessation of the EU passport following Brexit. It could enable these companies to transfer their business activities into other EU Member States, from a British legal entity to a new legal entity with seat in one of the other EU Member States via a universal succession. Hence, the legislative instrument of the cross-border merger constitutes an important component in the emergency planning of regulated companies in the financial sector for reacting to the cessation of the EU passport. However, the time aspect of such a prolonged cross-border merger needs to be taken into account. Insofar as this facilitates financial companies' move from the United Kingdom to Germany, maintenance of this legislative instrument would also be in the interest of EU Member States in their capacity as financial centres.

However, it should be pointed out by way of clarification that it should as a rule be necessary prior to a relocation of banking business to continental Europe via a cross-border merger to divide the banking business initially concentrated in one British legal entity between two British legal entities; namely one for British banking business and the other one for the continental European banking business. The British legislative instrument known as "Part VII Transfers" is available for this division insofar as the relevant banking business comprises deposits business. Only after separation of the banking business into two legal entities would the legal entity with the continental EU banking business then be merged into a new legal entity with seat in the European Union.

6.2.3 Recommendations

In order to avoid a loss of provisions on cross-border mergers as a consequence of Brexit in relation to the United Kingdom, the European Union can agree with the United Kingdom that the continuing applicability of this legislative instrument is secured also after Brexit in order not to question again the level of legislative harmonisation already achieved. However, such an agreement would have to be reached by the European Union and all Member States because it would require adjustments to all national restructuring laws.

[73] Cf. Companies House, at https://www.gov.uk/government/organisations/companies-house.
[74] Cf. The Gazette, at https://www.thegazette.co.uk/.

Alternatively, provision should at least be made for an appropriate transition period for the continued applicability of provisions on cross-border mergers in relation to the United Kingdom. This would make it easier for regulated companies in the financial sector to adjust to the new legal environment after the EU passport lapses. In order to safeguard the uniformity of implementation of the legislative instrument of cross-border mergers in relation to the United Kingdom, the United Kingdom would have to continue to be subject to ECJ's case law, at least for the duration of the transition period. Nevertheless, from the opinions expressed to date by the British government, it is clear that bringing ECJ's competence to an end constitutes one of the central objectives of Brexit so that this point would likely trigger a need for special discussions.

6.3 EUROPEAN COMPANY (SE)

6.3.1 Problem definition

The EU legislator has created the largely harmonised legal form of the European Company (Societas Europaea, SE) with the SE Regulation[75] which enjoys steadily increasing popularity. With Brexit, the legal basis for this legal form will lapse in the United Kingdom so that it could no longer be used there insofar as no divergent agreements are made in the framework of the exit agreement. Correspondingly, the possibility of a simplified cross-border transfer of seat as provided for in the SE Regulation would also lapse for European Companies.

6.3.2 Details and examples from corporate practice

Details of law governing stock companies which go beyond the legislative framework created in the SE Regulation have been implemented in Germany through SEAG.[76] The stipulations of the Directive on Employee Involvement[77] were transposed in Germany through SEBG.[78] In the United Kingdom, the supplementary company law themes and employee involvement are regulated together in the SE Regulations[79].

Following an initially hesitant acceptance of this new legal form, the SE now enjoys great popularity. There are now 2,670 European Companies in the European Union, including 412 in Germany and 46 in the United Kingdom.[80]

[75] Regulation (EC) No. 2157/2001 of 8 October 2001 on the statute for a European company (SE).
[76] SEAG: SE Ausführungsgesetz: Act on implementation of Council Regulation (EC) No. 2157/2001 of 8 October 2001 on the statute for a European company (SE).
[77] Directive 2001/86/EC of 8 October 2001 supplementing the statute for a European company with regard to the involvement of employees.
[78] SEBG: SE Beteiligungsgesetz: Act on the participation of employees in an SE.
[79] The European Public Limited-Liability Company Regulations von 2004.
[80] Cf. European Trade Union Institute's European Company (SE) Database (ECDB).

Part of the advantage of the SE is that it creates a largely harmonised legal form for listed and unlisted companies with a “European identity”. It is therefore suitable for a parent company (listed or not) and for a subsidiary within cross-border corporate groups. Well known German parent companies with the legal form of a European Company include Allianz SE, ARAG SE, Axel Springer SE, BASF SE, Bilfinger SE, E.ON SE, Fresenius SE & Co. KGaA, ProSiebenSat.1 Media SE, PUMA SE, SAP SE, Sixt SE and Zalando SE. Conversely, the legal form of the European Company is occasionally used in the United Kingdom to bundle the European activities of non-European groups, as can be seen from examples such as Chub Insurance Company of Europe SE, Olympus Europa Holding SE and PAYPAL SE.

Moreover, the SE Regulation enables a cross-border transfer of the SE’s seat from one EU Member State to another, without loss of identity and without the necessity to close down the old legal entity or to found a new one.

The legal instrument of a cross-border transfer of seat could help regulated companies from the financial sector with a company seat in the United Kingdom and with branches in the other Member States of the European Union to react to any cessation of the EU passport following Brexit. Via this instrument, regulated companies could bundle their business activities which they conduct in the other EU Member States from the United Kingdom in a British SE and then relocate them in one of the other EU Member States via a transfer of seat. The legal form of the SE and the cross-border transfer of seat it enables therefore constitute an important component in the emergency planning of regulated companies in the financial sector in order to allow a reaction to the cessation of the EU passport. Insofar as financial companies’ move from the United Kingdom to Germany would be facilitated, preservation of this legal instrument would also be in the interest of the EU Member States in their capacity as financial centres.

6.3.3 Recommendations

In order to avoid a lapse of the SE provisions and cross-border transfer of seat as a result of Brexit in relation to the United Kingdom, the European Union can agree with the United Kingdom that the continued applicability of this legal instrument is ensured also after Brexit in order not to question again the level of legal harmonisation achieved hitherto.

Alternatively, provision should be made at least for an appropriate transition period for the continued applicability of the SE provisions and cross-border transfer of seat in relation to the United Kingdom. This would make it easier for regulated companies in the financial sector to adjust to the new legal environment after the European passport lapses.

In order to safeguard the uniformity of implementation of the legislative instrument of the SE provisions and cross-border transfer of seat in relation to the United Kingdom, the United Kingdom would have to continue to be subject to ECJ’s case law, at least for the duration of the transition period. Nevertheless, from the opinions expressed to date by the British government, it is clear that bringing ECJ's competence to an end constitutes one of the central objectives of Brexit so that this point would likely trigger a need for special discussions

6.4 EMPLOYEE INVOLVEMENT IN THE SE

6.4.1 Problem definition

With Brexit, the question arises for EU SEs with employees and subsidiaries in the United Kingdom as to how this will impact on employee involvement of British employees, in concrete terms the continued presence of British members in the SE workers council.

6.4.2 Details and examples from corporate practice

The stipulations of the Directive on Employee Involvement were transposed e.g. in Germany through SEBG. This provides that negotiations are to be conducted between the management of the companies participating in the foundation of a SE and a special negotiating committee of European employees on the involvement of employees in the SE. If the negotiations fail to produce a result, the provisions of §§ 22 to 38 SEBG on the SE workers council and employee involvement in the supervisory or administrative body of the SE apply as a rule.

In the statutory provisions on the SE workers council (§§ 22 to 33 SEBG) no arrangements are included as to how the departure of a Member State from the European Union impacts on the membership of employees from the Member State in question in the workers council of a German SE. It can be assumed that SE involvement agreements also generally contain no such provisions.

6.4.3 Recommendations

To avoid legal uncertainty for the affected SEs and their workers councils, it would be advisable for the European Union to agree with the United Kingdom that British members of SE workers councils of European SEs should retain their positions until the regular end of their term of office unless otherwise provided in the relevant SE involvement agreement.

6.5 MERGER CONTROL NOTIFICATIONS IN THE CASE OF M&A

6.5.1 Problem definition

The EC Merger Regulation (ECMR)[81] determines that no notification of a merger between companies is regularly necessary or possible in individual Member States but only to the European Commission (Directorate General Competition), if certain turnover thresholds are exceeded ("one-stop shop"). Under these rules, ECMR is applicable when the following alternatively applicable combinations of worldwide and Europe-wide turnover thresholds are reached:

Alternative 1:

- Aggregate worldwide turnover of all undertakings concerned is more than 5 billion euros, and
- aggregate union-wide turnover of each of at least two undertakings concerned is more than 250 million euros.

or

Alternative 2:

- Aggregate worldwide turnover of all undertakings involved is more than 2.5 billion euros,
- combined aggregate turnover of all the undertakings concerned in at least three Member States is more than 100 million euros, with at least two undertakings generating at least 25 million euros, and
- aggregate union-wide turnover of at least two undertakings concerned is more than 100 million euros.

This does not apply, if the undertakings concerned each generates more than two thirds of their aggregate union-wide turnover in one and the same Member State.

An individual union-wide notification of a merger is a facilitation for many undertakings since otherwise, in an extreme case, a notification has to be made in each individual Member State and every Member State has a decision-making competence.

The United Kingdom is an important market for EU companies which generate high turnovers there. Should the United Kingdom be removed from the aggregate EEA-wide market for the purposes of turnover calculation, the turnovers generated there would not be union-wide turnovers and would no longer play a role in the calculation of the threshold values for ECMR. It is therefore to be feared that EU companies in the case of mergers would less often fall within the scope of the ECMR regime, since they would no longer reach the union-wide

[81] Regulation (EC) No. 139/2004 of 20 January 2004 on the control of concentrations between undertakings.

turnover threshold values and neither threshold turnovers in the individual EU countries. As a result, fewer mergers could in future benefit from the one-stop shop offered by the ECMR regime.

In addition, the preference for European merger control over national merger control in the United Kingdom would in future lapse so that the latter would generally be applicable in addition to a notification in Brussels. Important transactions with implications for the UK market would be regularly notified in order to gain legal certainty and to avoid the risk of a subsequent prohibition, because the European Commission's clearance decisions would then no longer relate to the United Kingdom.

6.5.2 Details and examples from corporate practice

There were 337 merger control notifications to the European Commission in 2015. The figure increased to 362 notifications in 2016.[82] By contrast, the UK supervisory authority received only 62 requests between April 2015 and March 2016.[83]

6.5.3 Recommendations

In an ideal case, the current Europe-wide ECMR regime would exist also after a departure of the United Kingdom. But since that would also involve recognition not only of the European Commission's decisions but also acceptance of the rulings of European courts, it is improbable that the United Kingdom would agree to this. British Prime Minister Theresa May has made it clear on several occasions that the United Kingdom will no longer be subject to the rulings of European courts following Brexit.

ECMR should therefore be amended such that the turnover thresholds (union-wide turnover) are reduced so that individual notifications to the European Commission continue to be realistic. Whether this is feasible depends on whether a substantial number of the transactions that currently have to be notified in Brussels would in future have to be notified at national level through the exclusion of turnovers generated in the United Kingdom. As an alternative, consideration could be given to recommending that the referral to the European Commission at the request of the undertakings concerned in accordance with article 4 paragraph 5 ECMR should be restructured, so that Member States have no right of veto or rather a referral to the European Commission can only be prevented in the event of objection between all/a majority of the competent Member States.

82 Cf. European Commission, at http://ec.europa.eu/competition/mergers/statistics.pdf.

83 Cf. British Competition and Markets Authority Merger, Inquiry Outcome Statistics, at https://www.gov.uk/government/publications/phase-1-merger-enquiry-outcomes.

6.6 M&A – TAKEOVER LAW

6.6.1 Problem definition

The intention of the Takeovers Directive[84] was to create a European level playing field for takeovers of listed companies, i.e. in particular to establish a high degree of equality of arms between the companies involved, even if this has not been achieved by one hundred percent.[85] This level of legal harmonisation could once more be lost through the exit of the United Kingdom from the European Union insofar as, for locational reasons, the United Kingdom was to decide post-Brexit for an easing of requirements on for example the protection of minority shareholders or defence mechanisms for the target company or to introduce extended state defence and intervention rights in order to increase attractiveness as a location for European holding companies through such protection against takeover.

6.6.2 Details and examples from corporate practice

Among other things, the Takeovers Directive regulates the obligation to make a bid when control is acquired, to ensure financing of the bid, a neutrality obligation on management and administrative bodies, the requirement to treat shareholders of the target company equally, a ban on market distortions through manipulation of bidder and target-company securities and a time-limited ban on impeding the target company's business activity.[86]

While the British Takeover Code serves to transpose the Takeovers Directive into national law, it was at the same time a model and thus exerted a considerable influence on the draft directive.[87] The British Takeover Code enjoys broad recognition for public takeovers in the United Kingdom, therefore substantial changes seem unlikely for the time being. Nevertheless, it cannot be ruled out that the provisions of the Takeover Code could be amended following a departure from the European Union to bring them closer into line with both British and global market conditions (and interests). A first consultation on the takeover rules has been announced for this year. Prime Minister Theresa May's statements with regard to the takeover of Cadbury by Kraft Foods in 2010 and the (ultimately unsuccessful) takeover of AstraZeneca by Pfizer in 2014[88], the Prime Minister's announcement that the government wants to grant stronger intervention rights with regard to public takeovers and first examples from corporate practice make provisions, which aim at stronger protection of British companies against takeovers from abroad, very likely. At the same time, there is a danger that the restrictions on existing intervention rights of national authorities (for instance due to the fundamental freedoms or the ECMR) will lapse following the departure of the United Kingdom from the European Union.

---

[84] Directive 2004/25/EC of 21 April 2044 on takeover bids.

[85] Cf. Pötzsch in: Assmann/Pötzsch/Schneider: WpÜG, introduction margin note 95. Cf. Rieder in: Baums/Thoma WpÜG, introduction margin note 1.37.

[86] Cf. Pötzsch in: Assmann/Pötzsch/Schneider: WpÜG, introduction margin note 102 et seq.

[87] Cf. Louise Gullifer und Jennifer Payne in: Corporate Finance Law 2011, page 571.

[88] Cf. speech by Prime Minister Theresa May, We can make Britain a country that works for everyone of 11 July 2016, at http://press.conservatives.com/post/147947450370/we-can-make-britain-a-country-that-works-for.

6.6.3 Recommendations

It remains to be seen how British takeover rules and the intervention rights of state bodies will look like post-Brexit. However, it is recommended in the interest of German companies that negotiators should press for preservation of the level playing field for takeover bids in order to secure harmonised framework conditions for public takeovers in the European Union and in the United Kingdom also in the future and to prevent a disproportionate migration of companies and parent companies into the United Kingdom – either through active relocation of the seat in a quest for more effective takeover protection or as a result of successful takeovers by British companies.

7 CONCLUSION

In all probability, the United Kingdom's exit from the European Union will have a major impact on European economy and society – in other words also on companies, consumers and investors. The concrete consequences depend on the outcome of the Brexit negotiations.

The objective of this paper is to identify how negative effects on the affected national economies can be minimised. In this regard, we pointed in particular to the importance of transitional arrangements – more time for affected parties to adjust structures, processes and contracts. We then highlighted critical aspects in capital and financial markets law as well as company law, emphasising the importance of a bilateral agreement between the European Union and the United Kingdom based on an extension and adaptation of existing third-country regimes.

It is now up to the lead negotiators on both sides to find a constructive and adequate solution for the future relations between the European Union and the United Kingdom, which strengthens European capital and other markets and minimises the negative fallout of Brexit. Deutsches Aktieninstitut and its members are available to act as competent discussion partners at any time.

Annex

ANNEX 1:

Overview of the relevant MiFID II/MiFIR and EMIR provisions for financial market infrastructure operators with regard to potential effects of Brexit

Legislation		Issue	Impact
MiFID II / MiFIR			
Market Structure	OTF category	• Strict rules on the operation of an OTF.	• Potential loopholes for certain derivatives and bond instruments issued in UK.
Market Structure	Transparency waivers	• Strict rules on when to grant waivers for transactions on trading venues.	• Lighter waiver regime in UK.
Market Structure	Trading obligation for derivatives	• Obligation for derivatives to be traded on RMs, MTFs and SIs. • ESMA to calculate, which set of instruments is liquid enough to qualify for the obligation.	• Difficult for EU derivatives to be traded on UK trading venues? • Calculations on liquidity will no longer be relevant as UK data no longer to be included.
Market Structure	Clearing obligation for ETDs	• Trades on a RM must be cleared by a CCP.	• Difficult for EU derivatives to be traded on UK trading venues?
Market Structure	Trading obligation for shares	• All shares admitted to trading should be traded on a RM, MTF or SI, and all investment firms with internal matching systems must be authorised as an MTF.	• Difficult for EU shares to be traded on UK trading venues?
Market Structure	Reasonable commercial basis	• Obligation to make post trade data available on a reasonable commercial basis (RCB).	• No change for EU trading venues.
Calibrations	Liquid market definitions	• Calculation for the determination of 'liquid markets' within EU. • Calculation method to determine the liquid market based on objective criteria.	• Lack of EU data would refocus liquid market back to home market.
Calibrations	Transparency thresholds	• Calibration of thresholds for equity and non-equity instruments traded in the EU.	• Thresholds no longer relevant without UK data.
Calibrations	Double volume	• Calculation of Double Volume Cap for transparency waivers for equity trading.	• Thresholds no longer valid without UK trading activity.
Calibrations	Position limits	• Obligation to have strict position limits based on ESMA calibrations.	• UK could not impose strict limits on all contracts but only the main contracts. • Limits could be set less stringently than ESMA methodology.
Calibrations	Position reporting	• Obligation to make public a weekly report on the aggregate position held by categories of persons.	• No such reports from UK trading activity.
Calibrations	Tick Sizes	• Obligation for objectives determination of relevant tick sizes per instrument.	• UK could undercut EU tick sizes.
Information & data exchange	Transaction reporting	• Obligation to report all transactions to NCAs, who must make them available to ESMA upon request.	• Gap in UK transaction reporting for supervisors.
Information & data exchange	Reference data	• Obligation for NCAs to provide all reference data to ESMA (part of ESMA data project).	• UK no longer part of ESMA data project.
Information & data exchange	Consolidated tape providers (CTPs)	• Obligation to consolidate and make available to the public all data from EU trading venues.	• Less data for European CTP but would not fully reflect European trading.
Information & data exchange	Reports and Review	• There will be a significant number of reports and review of key provisions in the years immediately after the application of MiFID II / MiFIR.	• Reports and reviews of MiFID II will need to take into account the withdrawal of UK market.
Information & data exchange	Supervisory cooperation	• Obligation to share information on a regular basis between home and host member state.	• UK will no longer be subject to legally binding cooperation and information sharing arrangements.

Access & Clearing	Access to benchmarks	• CCPs and trading venues should be allowed non-discriminatory access to relevant details and licenses of a benchmark.	• Benchmark access will still be implemented in EU.
	CCP and trading venue access	• CCPs shall accept to clear on a non-discriminatory and transparent basis. • Trading venues shall provide trade feeds on a non-discriminatory and transparent basis to CCPs.	• CCP access will still be implemented in EU.
	Clearing & Settlement arrangements	• RMs based in EU only allowed to enter into clearing arrangement with CCPs in another MS.	• UK CCPs placed at a disadvantage.
Third Country Regime	Access for third country CCPs and trading venues	• COM may only allow a request for access, if the CCP or trading venue has equivalent rules for allowing foreign access to their CCPs and trading venues.	• UK CCPs only to be able to have access if deemed to be equivalent, therefore, no lowering of standards for access.
	Cooperation with third countries	• MS and ESMA may cooperate with third countries as long as data privacy rules are equivalent.	• This can be resolved.
	Third country regime	• Application of common third country regime prioritising the G20 commitments and IOSCO principles. • Third country regulatory and supervisory framework must achieve adequate and regulatory affects and meet the same objectives as EU law.	• To be determined by COM.
EMIR			
Market Structure	Clearing obligation	• Clearing obligation applies to transactions between EU and third country counterparties, and between third country counterparties, if the contact has a significant effect on the EU or is being used to evade EU rules.	• Third country rules would apply to UK and determined by UK.
	Instruments subject to clearing obligation	• ESMA to determine class of instruments to be subject to clearing obligation (based on volume & liquidity).	• UK data no longer taken into account for clearing obligation. • Current calculations will need to be amended.
	Capital requirements	• CCPs to have initial 7,5 million capital requirements.	• UK could introduce lower requirements.
Information & Cooperation	Reporting obligation	• Obligation to report all details of the conclusion, modification or termination of the contract.	• UK will no longer be obligated to report the relevant data.
	Transparency & data availability	• TRs must make data available to ESMA, ESRB, NCAs, third country NCAs.	• UK would no longer be part of this cooperation.
	Cooperation between NCAs	• CCPs to cooperate with each other, ESMA and ESRB.	• UK would no longer be part of this cooperation.
Third Country Regime	Recognition of a third country CCP	• CCP must be recognised by ESMA	• To be determined by ESMA.
	Third country regime	• Third country CCPs must be equivalent.	• To be determined by COM.

ANNEX 2:

EU passporting and third-country regimes in EU financial and capital markets law

Legal basis/ issue	EU passport	Other provision	Equivalence regime with EU passport	Other third-country regimes
MiFID II/MiFIR	Yes, for financial and investment services and branches (of investment firms).		Yes, but only investment services for professional and selected clients; this comprises no private client business and only a small portion of corporate client business.	Establishments optional for EU countries.
	Yes, for trading venues (inter alia clearing/trade in shares and derivatives).	Trading venues have non-discriminatory access to CCPs, and benchmarks.	Yes, but restrictions are expected for euro clearing.	
	Yes, for data provision services.		No.	
CRDs	Yes, for banking services as well as branches (of banks).		No, not for banking services or branches. For investment services compare MiFID II/ MiFIR.	Third-country equivalence for special aspects (e.g. risk weighting) possible, but contains no market access or EU passport.
PSDs	Yes, for payment services.		No.	
EMIR	Yes, for CCPs.		Yes.	
	Yes, for TRs.		Yes.	
		CCPs and trading venues have non-discriminatory access to each other.	No, but compare MiFID II/ MiFIR.	
CSDR	Yes, for services and branches (but national regulator has to be informed).		Yes.	
UCITS	Yes, for management and marketing of collective forms of investment.		No.	
AIFMD	Yes, for the management and marketing of alternative funds to professional clients.			Non-EU providers can manage alternative funds EU-wide and market them to professional clients via ESMA recommendation and authorisation by the European Commission.
Prospectus Directive/ Regulation	Yes, for issuers' securities prospectuses.		Yes.	
Transparency Directive		Applies for all issuers with EU listing.		Yes. Applies independent of the seat for all issuers with EU listing.
Market Abuse Regulation		Applies for all issuers with EU listing.		Yes. Applies independent of the seat for all issuers with EU listing.
Benchmark Regulation	Yes, for benchmark providers.		Yes.	Temporary recognition of third-country benchmarks until equivalence decision is taken, if compliance with IOSCO principles is equivalent to those of the regulation.
Solvency II Directive	Yes, for insurers and reinsurers.		Yes, but only for reinsurers.	

Contact

Dr. Franz-Josef Leven
Deputy Managing Director
Phone + 49 69 92915-24
leven@dai.de

Sven Erwin Hemeling
Policy Advisor Capital Markets Law
Phone + 49 69 92915-27
hemeling@dai.de

Michaela Hohlmeier
Advisor to the Board of Management
Head of Capital Market Trends and
Innovation
Phone + 49 69 92915-31
hohlmeier@dai.de

Deutsches Aktieninstitut e.V.
Senckenberganlage 28
60325 Frankfurt am Main
Phone + 49 69 92915-0
Fax + 49 69 92915-12
www.dai.de

ISBN 978-3-934579-79-8

www.dai.de