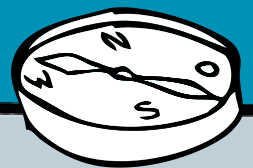
EXIT NEGOTIATIONS BETWEEN THE EUROPEAN UNION AND THE UNITED KINGDOM:

MINIMISE BREXIT RISKS AND STRENGTHEN THE EUROPEAN CAPITAL MARKET

Recommendations of Deutsches Aktieninstitut
3rd Position paper



Deutsches Aktieninstitut

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

September 2018
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ISBN 978-3-934579-87-3

For download see www.dai.de

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3rd Position paper of Deutsches Aktieninstitut e.V. on the Brexit negotiations
Version: 17 September 2018

Foreword

It is becoming increasingly clear: The United Kingdom's withdrawal from the European Union will have a considerable impact on the European economy and society. However, it is still not possible to predict the consequences in detail, since the negotiators have not yet been able to reach agreement on a number of important, critical core elements.

Notwithstanding, the remaining weeks until 29 March 2019 23.00 UK time when Brexit becomes a reality are passing rapidly. The time for the parties affected to make preparations is running out, even if they still have no idea for which situation they should put measures in place. In the end, all they can do is prepare for the worst-case scenario, a hard Brexit – with all its negative consequences for the economies and citizens of the European Union.

Deutsches Aktieninstitut therefore calls once more on the negotiating partners to strive for constructive and practical solutions in order to minimise the negative impact of Brexit on the affected economies. The economy and the society ask for technically sound and rational decisions reached by weighing up all positive and negative consequences.

To support the lead negotiators at regional, federal, and EU level, Deutsches Aktieninstitut has put in place an interdisciplinary project. Members of Deutsches Aktieninstitut have provided input from their specific experience and expertise in order to define topics of special importance for the negotiations. Concrete possible solutions that can minimise the negative impact on the affected economies are highlighted. I take this opportunity to warmly thank all members of the Brexit project for their excellent and time-consuming work.

This third position paper complements the first two papers from 2017 and identifies problem areas which companies cannot address with their own measures alone. The documents are focused on current issues at the time of publication. Future developments can and will make it necessary to adapt observations to the respective state of the negotiations.

This position paper is divided into two parts: Part I describes general, overarching considerations that should be taken into account in the framework of the Brexit negotiations. Part II looks more closely at three use cases and shows why companies cannot solve all problems arising as a result of Brexit through their own measures.

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

Frankfurt am Main, September 2018

Dr Christine Bortenlänger

Executive Member of the Board
Deutsches Aktieninstitut e.V.

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List of Abbreviations

AIFMD	Alternative Investment Fund Managers Directive
BaFin	Bundesanstalt für Finanzdienstleistungsaufsicht
BDSG	Bundesdatenschutzgesetz
Brexit	Exit of the United Kingdom from the European Union
CCP	Central Counterparty
CE	Communauté Européenne
CRA	Credit Rating Agency
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CSDR	Central Securities Depositories Regulation
EBA	European Banking Authority
EC	European Community
ECC	European Commodity Clearing
EEA	European Economic Area
EMIR	European Market Infrastructure Regulation
ESAs	European Supervisory Authorities
ESMA	European Securities and Markets Authority
EU	European Union
EU27	Remaining 27 EU Member States after the exit of the UK
FC	Financial Counterparty
FCA	Financial Conduct Authority
GDPR	General Data Protection Regulation
ISDA	International Swaps and Derivatives Association
LCH	London Clearing House
LME	London Metal Exchange
MiFiD	Markets in Financial Instruments Directive
MiFIR	Markets in Financial Instruments Regulation
NFC	Nonfinancial Counterparty
OTC	Over-The-Counter
PSD	Payment Services Directive
UCITS	Undertakings in Collective Investments in Transferable Securities
UK	United Kingdom
USA	United States of America

Executive Summary

The United Kingdom's withdrawal from the European Union (Brexit) in March 2019 poses considerable challenges on both sides. Never before has an EU Member State left the community of European countries. The situation is characterised by great uncertainty for all those involved.

Within the framework of its Brexit project, Deutsches Aktieninstitut has identified the essential issues with relevance for financial and capital markets, which deserve particular attention due to their significance for business and society in connection with the Brexit negotiations. The results have been fed into two position papers.

The purpose of Deutsches Aktieninstitut's position papers on Brexit is to highlight how the negative impact of Brexit on the affected economies can be minimised.

The position papers published in 2017 focused on the two thematic areas of capital and financial markets law as well as company law. In addition, they addressed overarching issues which constitute the decisive basis for the economy and society in Europe independent of specific fields of law and sectors and thus need to be taken into account in the negotiations. This third position paper of September 2018 complements those findings and makes clear that companies cannot solve all problems arising as a result of Brexit through their own measures – either due to a shortage of time or because the regulatory, supervisory, or market-related frameworks do not (yet) permit.

Deutsches Aktieninstitut emphasises for the withdrawal negotiations:

1. A disorderly and hard Brexit is the worst case scenario for ALL

The clock is ticking! Although an agreement has now been reached on a range of topics, a number of critical questions has still not been clarified. At the same time, the remaining days are flying by and a "hard Brexit" in March next year looks ever more likely. Given the close interdependence between the European Union and the United Kingdom, the associated consequences for business and society would be immense.

Even if the affected parties are preparing for such a situation, the time remaining is far too short to avert the negative consequences – if it is even possible to avert them. The negotiating partners therefore have to hurry striving for constructive and practical solutions.

2. Parties affected cannot solve all problems alone

Moreover, there are areas which cannot be dealt with by companies alone without the involvement of regulators and/or supervisors. The reasons for this are various. For instance, there is currently no comparable offer within EU27 countries for certain products and services. Or contracts are valid for a long period and cannot be transferred smoothly into the European Union, just as existing infrastructure cannot be relocated overnight.

Quite apart from the absence of supervisory and regulatory requirements for the period following Brexit: Supervisors are also dependent on the outcome of the Brexit negotiations. All "better" scenarios have to be decided at political level, for which supervisory authorities are "policy takers" and therefore largely play only an advisory role.

Based on the examples customs and product authorisations as well as data protection, and derivatives, this paper shows what companies can do to solve these problems. However, it also clarifies why companies cannot solve all issues without the involvement of regulators and supervisors.

3. Gain more time for necessary adjustments with transitional arrangements

As already repeatedly emphasised, given the great time pressure as well as the large number of open questions, transitional arrangements are the key to avert drastic damage following Brexit. The players concerned – business, society and authorities – are coming under even greater time pressure with their preparations, without having any idea of what situation lies ahead. All they can now do is prepare for the worst case, a disorderly, hard Brexit. With all the associated negative consequences.

However, even if companies gear their structures for a hard Brexit, the time remaining is just not long enough for such far-reaching changes. Due to time pressure and great uncertainty, emergency plans usually encompass only the most necessary precautions. Their purpose is to prevent a collapse of large parts of business.

For these reasons, the United Kingdom plans for example its own transition period for financial services, if no withdrawal agreement is reached. EU market participants can continue to provide their services in the United Kingdom for a maximum of three years while they await their permit. A comparable fall back solution in form of a transition period is also indispensable for the European Union, especially for existing business.

This position paper sets out the ideas of the Brexit project of Deutsches Aktieninstitut at this point in time and complements the first two position papers from 2017.[1] It does not claim that the list of topics to be addressed is complete nor that the proposed approaches are definitive. As the negotiations unfold, the document may be expanded, elaborated, and updated as and when necessary.

[1] Deutsches Aktieninstitut's two position papers on Brexit from 2017 can be found at https://www.dai.de/en/what-we-offer/studies-and-statistics/studies.html.

Part I: Brexit – overarching considerations

1 BREXIT NEGOTIATIONS GOING ROUND IN CIRCLES

With increasing probability, the United Kingdom's (UK) withdrawal from the European Union (EU) in March 2019 will have far-reaching effects on the European economy and society. For example, the concrete consequences for companies, consumers, and investors continue to be difficult to predict, since they depend essentially on the final withdrawal scenario, which has to be negotiated at political level.

Time is running out! Although some agreements have now been reached on a range of topics, a number of critical questions has still not been clarified. Thus, it appears almost impossible to avoid a hard border on the Island of Ireland and at the same time not to be subject to the requirements and restrictions of a customs union. In addition, the framework for the future economic cooperation is still open. Nobody knows whether and to what extent products and services can continue to circulate barrier free between the United Kingdom and the remaining EU27 Member States in the future and the corresponding rules. The positions of the negotiating parties are still far apart, not to mention the internal political disagreements between supporters and opponents of Brexit in the United Kingdom.

The remaining days are flying by and a "hard Brexit" in March next year looks ever more likely. The associated consequences for business and society would be immense. The belief of some British politicians that no deal is a better deal under some circumstances lacks all objective logic. Given the close interdependences between the European Union and the United Kingdom, not only of an economic nature, such a non-solution would result in the greatest possible negative consequences of Brexit.[2]

[2] Cf. the findings in Deutsches Aktieninstitut's first two position papers on Brexit from 2017.

HARD BREXIT:

In this paper, the term "hard Brexit" stands for the situation where negotiators fail to reach a timely agreement for the future relationship between the European Union and the United Kingdom and at the same time no agreement on transitional arrangements will be concluded. In that case, the British would not only leave the single market and the customs union but there would also be no bilateral agreements on future relations or transition periods. The United Kingdom's withdrawal will apply on 29 March 2019 23.00 UK time with immediate effect. The terms "cliff-edge Brexit" or "disorderly Brexit" are also often used for this situation.

In her White Paper "The Future Relationship between the United Kingdom and the European Union" of July 2018, the British Prime Minister Theresa May made an attempt to take this situation into account.[3] However, her rather pro-European approach led to instant controversies at home and the resignation of several known Brexit hardliners including Foreign Minister Boris Johnson. The extent to which she can maintain this approach and how the European Union reacts to the proposals remain to be seen. According to initial assessments, the White Paper offers a good basis for the ongoing negotiations.[4] Yet the EU's chief negotiator Michel Barnier has also made clear that the European Union for example will not give up customs processing.[5] Many further details, questions regarding feasibility and in particular of whether the proposals amount to "cherry-picking", also remain unclear. Both negotiating parties have already published guidance on the official position, the corresponding requirements, and what support those affected can expect in the event of a hard Brexit.[6]

For a long time, the parties affected from business and society played a waiting game and have held back from public criticism. The closer March 2019 comes, the louder concerns about the slow pace of negotiations and the associated dangers for both sides are articulated. Companies increasingly warn about the consequences for markets, jobs, and Europe's international competitiveness. At the same time, the evaporation of trust is leading to an intensification of work on emergency plans and new structures following a hard Brexit. Because only one thing is certain: These plans must be in place and ready for rollout by the end of March 2019.

The next section looks at companies' internal preparations and indicates where and why they reach their limits.

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[3] Cf. HM Government, The future relationship between the United Kingdom and the European Union, 12 July 2018, at https://www.gov.uk/government/publications/the-future-relationship-between-the-united-kingdom-and-the-european-union.

[4] Cf. European Commission, Michel Barnier: Brexit-Weißbuch hat konstruktive Elemente, wirft aber auch Fragen auf, 20 July 2018, at https://ec.europa.eu/germany/news/20180720-michel-barnier-brexit-weissbuch_de.

[5] Cf. European Commission, Statement by Michel Barnier at the press conference following his meeting with Dominic Raab, UK Secretary of State for Exiting the EU, 26 July 2018, at http://europa.eu/rapid/press-release_SPEECH-18-4704_en.htm.

[6] Cf. European Commission, Brexit preparedness, 2018, at https://ec.europa.eu/info/brexit/brexit-preparedness_de. Department for Exiting the European Union, 23 August 2018, at https://www.gov.uk/government/collections/how-to-prepare-if-the-uk-leaves-the-eu-with-no-deal.

2 BUSINESS IS PREPARING ITSELF

Behind closed doors, companies are working intensively on emergency plans for a hard Brexit. From a risk management perspective, every corporate management team must show responsibility by preparing for the worst-case scenario and planning accordingly. Whereas a few companies have waited in vain for the negotiations to deliver results, others began at an early stage to prepare for market disruptions and to position themselves for the period after Brexit. In this regard, they seek not only short-term solutions for spring 2019 but are also planning a fundamental restructuring of processes and structures (e.g. supply chains, contractual partners, competences, human resources, or other location-related capacities).

Many companies have had no choice but to accept the effort associated with restructuring as well as permanently less favourable cost structures. If a free-trade agreement were still to be concluded at some time after a hard Brexit, a further adjustment of processes will be less likely due to the path dependence of economic development. For companies, it will be only partly possible to abandon the route they have chosen and once more accept the costs of reversing the changes. Yet at the same time, this will also reduce the possible benefits of a comprehensive agreement. The willingness to strive for such an agreement could even be weakened, creating a self-fulfilling prophecy. This vicious circle must be avoided!

After initial hesitation, the financial sector, which faces drastic changes through the loss of the EU passport for financial services out of and into the United Kingdom, has become the forerunner in preparations for Brexit. At the latest since the British White Paper published in July 2018, it is clear that the EU passport will cease to exist without replacement, because financial services are not mentioned as a primordial component of the future agreement. As a result, proposals such as "mutual recognition" seem to be off the table. On the side of the European Union, such a framework was unacceptable from the beginning. Instead, the British propose that the current third-country regime is used as the basis and extended to areas which are not currently covered. To this end, mutual recognition and withdrawal of equivalence shall be placed on a more stable footing (withdrawal periods) in order to create greater certainty for market participants. However, the prospects for success of this proposal are unclear, not to mention whether the process can be completed in time.

A broad scope, ease of implementation, and adequate transition periods for withdrawal of equivalence enhance the attractiveness of EU financial and capital markets for companies from third countries.

This approach of using the third-country regime as a "blueprint" and expanding it corresponds to Deutsches Aktieninstitut's proposals for regulation of crossborder financial and capital markets services, as set out in the first two position papers.

Even independent of Brexit, we recommend that the issue of third-country regimes is addressed. A broad scope, ease of implementation, and adequate transition periods for withdrawal of equivalence enhance the attractiveness of EU financial and capital markets for companies from third countries. This assessment relates exclusively to the British proposals for financial services. The other proposals in the White Paper will not be considered further here. Yet it has to be clear: We firmly reject cherry-picking. Brexit must not jeopardise the unity of the EU27 countries. Similarly, a deregulation race or tax dumping must be prevented and fair competition ensured. The overarching objective must nevertheless be to arrive at technically sound and rational decisions reached by balancing positive and negative consequences.

Given the slow pace of negotiations and the increasing probability of a hard Brexit, supervisory authorities on both sides have criticised the shortage of progress in the Brexit preparations of many companies. For example, the European Banking Authority (EBA) complained in June of this year that many banks are not adequately prepared for a hard Brexit and that the time for taking the necessary measures is running out.[7] Similarly, in July the European Securities and Markets Authority (ESMA) called on regulated market participants to submit their authorisation requests to national supervisory authorities and/or ESMA as rapidly as possible.[8] The Bank of England in April has also invited financial market participants with cross-border activities between the United Kingdom and the European Union to finalise their emergency plans by July 2018.[9]

Even if companies adapt their structures for a hard Brexit, there is simply not enough time left for such far-reaching changes.

Even if companies adapt their structures for a hard Brexit, there is simply not enough time left for such far-reaching changes. Furthermore, it is important not to make the mistake of considering emergency plans as ideal solutions. Due to time pressure and the high level of uncertainty about the future framework, these plans usually encompass only the most necessary precautions. Their purpose is to prevent a collapse of large parts of a business. Yet, that does not mean that directly after Brexit all customer groups will continue to have access to the market, that prices will remain stable, and that the diversity of supply will be maintained. In the long term, most problems can be eliminated. In the short term, however, there will be disruptions and shortages in some markets. The exact extent cannot yet be predicted and will vary from sector to sector (see use cases in Part II). For instance, high-value technical products, which are partially manufactured

[7] Cf. EBA, Opinion of the European Banking Authority on preparations for the withdrawal of the United Kingdom from the European Union, EBA/Op/2018/05, 25 June 2018, at http://www.eba.europa.eu/-/eba-publishes-opinion-to-hasten-the-preparations-of-financial-institutions-for-brexit.

[8] Cf. ESMA, Timely submission of requests for authorisation in the context of the United Kingdom withdrawing from the European Union, ESMA42-110-998, 12 July 2018, at https://www.esma.europa.eu/sites/default/files/library/esma42-110-998_public_statement_on_authorisation_applications.pdf.

[9] Cf. Bank of England, Contingency planning for the UK's withdrawal from the European Union, 7 April 2018, at https://www.bankofengland.co.uk/prudential-regulation/letter/2017/contingency-planning-for-the-uk-withdrawal-from-the-eu.

in the United Kingdom, comprise thousands of individual components which have to be repeatedly transported across the EU-UK border. Delays at the border, customs, and product authorisations would cause immense additional costs and time losses.

Emergency plans do not offer ideal solutions. They do not guarantee that directly after Brexit all customer groups will continue to have access to the market, that prices will remain stable, and that the diversity of supply will be maintained.

Moreover, there are issues, which cannot be dealt with by companies alone without the involvement of regulators and/or supervisors. The reasons for this are diverse. For instance, there is currently no comparable offer within EU27 countries for certain products and services. An example are British trading venues for metal derivatives, which are often used by resource rich industries and for which there is no (liquid) EU counterpart. In this regard, it is currently unclear whether British providers will be given recognition of equivalence in time, if provisions are made in the relevant laws. Or contracts are valid for a long period and cannot be transferred smoothly into the European Union, just as existing infrastructure cannot be relocated overnight. In addition, clear supervisory and regulatory requirements for the period after Brexit are largely lacking.

For this reason, companies work intensively in coordination with supervisory authorities on their plans for future structures and the permits needed. Yet, they can currently only initiate concrete steps based on a hard Brexit. If one of the "better" scenarios materialised, some hard Brexit adjustments would theoretically have to be reversed, which would then possibly entail high (and unnecessary) costs. However, supervisory authorities also face comparable problems. The only scenario for which they can plan and advise with certainty is a hard Brexit and third-country status for the other party. All "better" scenarios have to be decided at political level, for which supervisory authorities are "policy takers" and can therefore largely play only an advisory role. Hence, they too are dependent on the outcome of the Brexit negotiations.

Given the many open questions and imponderables, the United Kingdom is planning its own transition period, if a hard Brexit without withdrawal agreement materialises. EU market participants can then continue to provide their services in the United Kingdom for a maximum of three years while they await their UK permit.[10] The condition is a prior notification to the British supervisory body.

No comparable solution in the European Union is yet been planned. However, the consequences of such a hard line could be fatal. Many companies, in particular small and medium-sized enterprises, will not have fully completed their measures by March 2019 for the stated reasons. Numerous "regulatory breaches" are therefore expected. It is questionable how supervisors and regulators can and should act in such a situation.

[10] Cf. Bank of England, Temporary permissions and recognition regimes, 27 July 2018, at https://www.bankofengland.co.uk/news/2018/july/temporary-permissions-and-recognition-regimes.

A fallback solution in the form of a transition period in the event of a hard Brexit should also be created on the EU side.

A comparable fall back solution in the form of a transition period, during which third-country companies can still provide financial services in EU countries for a certain period in case of a negative or still missing equivalence decision, should also be planned in the European Union. Such a solution has to be recommended especially for existing business, in order to first relocate new business legally certain. Those concerned, whether from businesses, society, or supervisors, need additional time to adjust comprehensively to the new regulatory and supervisory requirements of the third-country relationship with the United Kingdom. With such a transition period, at least the worst distortions and disruptions could be mitigated.

If such a European regime should not be possible, the German legislator and the competent supervisory authorities need to find practical and effective transition solutions for Germany. Deutsches Aktieninstitut recommends that preparations are made immediately for this need and that transitional arrangements, grandfathering guarantees, and other necessary instruments should be drawn up for the event that no EU provisions are agreed. In this way, the attractiveness of Germany as a financial center would also increase, thanks to foreseeable costs and planning certainty

This has also been recognised by the German Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht, BaFin) which, together with the European Central Bank is preparing emergency solutions for a hard Brexit such as temporary permits and time-limited acceptances.[11] At the same time, BaFin President Hufeld has urged for a political solution on European level, since the issue of derivatives and insurances in particular cannot be addressed by individual financial market participants or supervisory authorities alone. [12]

[11] Cf. FAZ, BaFin plant Notmaßnahmen für harten Brexit, 30 August 2018, at http://www.faz.net/aktuell/brexit/bafin-plant-notmassnahmen-fuer-harten-brexit-15763244.html.

[12] Cf. Bloomberg, BaFin Says All Major Banks Preparing for `No Deal' Brexit, 30 August 2018, at https://www.bloomberg.com/news/videos/2018-08-30/bafin-says-all-major-banks-preparing-for-no-deal-brexit-video.

Part II: Regulatory aspects of Brexit in detail

3 FLOWS OF GOODS, SERVICES, AND DATA

In the event of a hard Brexit, companies can take a range of measures to counterbalance the consequences on their business activities – at least in parts. However, this is not possible for all areas (see explanations in Part I). Deutsches Aktieninstitut's Brexit project therefore wants to support negotiators at regional and federal level in Germany as well as at EU level with concrete indications of problem areas drawn from practice.

Three use cases, which companies cannot tackle alone without the involvement of regulators and/or supervisors and which are of particular delicacy for business and hence also for society, are examined in greater detail below.

3.1 USE CASE: CUSTOMS, CUSTOMS FORMALITIES, AND PRODUCT AUTHORISATIONS

3.1.1. Overview

With Brexit, deliveries which were originally intra-Community deliveries between the United Kingdom and the European Union will become imports and exports. As a result, customs duties and other costs for cross-border trade will occur, for instance for administrative tasks, time losses, authorisations, or additional warehousing. Furthermore, mutual recognition of national product and service authorisations will cease to apply.

Customs and customs formalities:

Every time a product or a component crosses the EU-UK border, customs duties will become payable. Since customs duties are not deductible as an input tax, they constitute real costs. Yet, the main concerns of companies do not relate to the level of customs duties but above all to the administrative effort within companies and the time needed for clearance at the border. This requires both additional human resources and changes to processes and systems. It is also questionable how quickly qualified personnel will be available. In the area of customs processing, the necessary training period takes years.

A longer and unpredictable waiting time at the border can lead to production delays, render just-in-time solutions more difficult, and increase warehousing costs, thereby tying up resources. Not only time losses generate risk but also the possible loss of important suppliers or customers.

In addition, deliveries are subject to the authorisation requirements imposed by customs offices. This means that export rules also have to be taken into consideration. For instance, the export of dual-use goods from the European Union to third countries – which the United Kingdom will then be – is subject to special rules (Dual-use Regulation).[13]

The future "rules of origin" are important for value chains, i.e. the question of the country and therefore the customs regime to which a particular product should be assigned. For a product to qualify as an EU product, a certain value must have been added inside the European Union. However, this value is not set on a uniform basis but is agreed inter alia in the European Union's trade and customs agreements with third countries. In other words, the assessment cannot be made overall but has to be accomplished for each individual product and export country. This makes it very time-intensive both for companies and for responsible authorities.

The changes are relevant not only for the sale of goods but in particular also in the framework of international value chains. Intermediate products are often produced in a number of countries, incorporated into larger components in another country, then assembled into the end product in another country, and sold in yet other countries. In particular, if the United Kingdom performs an intermediary function as a production location in the value chain, this would lead to (at least) two border crossings and the associated additional costs, time losses, authorisations, and other additional bureaucratic effort. For example, Airbus manufactures the wings for various models in the United Kingdom, Siemens produces wind park modules, and BMW builds the MINI on British soil. Such high-value and complex products comprise thousands of individual parts. For instance, a passenger car consists of around 30,000 parts, most of which do not originate from the United Kingdom and have to be imported.[14] According to a survey, a time loss of 30 to 60 minutes per truck at the border causes extra costs of around 100 euro. For a company with 10,000 border crossings annually a cost increase of one million euro has to be financed.[15]

[13] Dual-use goods can be used either for civil or for military purposes. Regulation (EC) No. 428/2009 of 5 May 2009 setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items.

[14] Cf. Berthold Busch, Institut der deutschen Wirtschaft Köln, Produktions- und Lieferverflechtungen zwischen britischen Branchen, der EU und Deutschland, W-Trends, Year 44 No. 2, 25 July 2017, at https://www.iwkoeln.de/fileadmin/publikationen/2017/342202/IWTrends_2017_2_Produktionsverflechtungen.pdf.

[15] Cf. COBCOE, Brexit – the Voices of European Business, 2017.

Product authorisations:

Mutual recognition of national product authorisations such as CE marking will broadly cease to apply for goods trade between the European Union and the United Kingdom. As a result, separate registration and/or authorisation of products will be necessary. As with the issue of customs, adjustments to processes and an increase in administrative human resource capacities will be necessary.

Moreover, it should be borne in mind that not only technical rules but also the EU Directives on environmental protection and waste management, as well as on chemical substances (producer and dealer authorisations) have to be taken into account. The automotive, chemical, and pharmaceutical sectors are particularly affected by this. For example, substances produced in the United Kingdom can be marketed in the European Union only with an additional registration. This obligation will in future hit EU importers with all the associated additional costs and conditions for fulfilling the relevant requirements.

Above all, high risks would arise from non-acceptance of existing product standards and authorisations. This would cancel the permit to sell into the market in question. Such a situation would affect not only the products themselves but also the sales organisation and value/supply chains. Dual authorisation processes would be necessary at the very least, even special product lines in the worst case.

3.1.2. Measures by companies

Businesses which provide services across borders must prepare for possible customs duties and formalities in the event of a hard Brexit. The more customs processing is time-intensive – technical, physical, and human resource capacities – the more important is the analysis of process chains. Among other things, delivery and production times, warehousing, production cycles, and logistics (e.g. freight volumes) have to be reviewed. In order to recognise the loss of individual suppliers at an early stage, a supplier analysis and a search for possible alternatives are important. The same applies for major customers and other important customer groups.

In addition, businesses must find out about any registration obligations. If certificates are missing or cease to be valid, new capacities for tests and applications may need to be developed. Moreover, additional service and sales organisations may be necessary. However, not only the validity of product authorisations has to be constantly verified but also the legality of the associated service offer. The test must be carried out for each individual product and is therefore time-intensive for both companies and the responsible authorities.

Furthermore, contracts must be adjusted to reflect assumptions underlying the contract such as customs, trade embargoes, export control provisions, etc.

Bookkeeping and documentation systems also need to be aligned at an early stage on the fact that deliveries between the United Kingdom and the European Union will become imports and exports following Brexit. Inadequate record keeping runs the risk, inter alia, that exemption from turnover tax will be refused.

Companies cannot influence the processes and capacities or even stipulations of authorities, customs, or other external costs, for instance for customs clearance and certification. Whether and under which circumstances a change of suppliers is feasible also continues to be dependent on the individual case. Increasing human resources can also founder not only because of the costs but also because of a shortage of qualified applicants. Companies therefore need practical solutions from public authorities to avoid serious market distortions.

3.1.3. Recommendations to supervisors and legislators

With Brexit, deliveries between the United Kingdom and the European Union will become exports with all the associated consequences for cross-border goods flows already described. Deutsches Aktieninstitut therefore calls on the negotiators on both sides to take action as early as possible.

First, a practical solution has to be found for customs clearance and border controls, which takes account of the dimension of EU-UK trade flows. The British White Paper says that the United Kingdom wants to leave the customs union, meaning there will be customs. However, in order to avoid a hard border on the Island of Ireland, different customs rates would apply depending on whether the goods are destined for the United Kingdom itself or for onward distribution in the European Economic Area (EEA). EU customs would be collected by the British for the European Union. The European Union has rejected this proposal, so that there is still no solution acceptable to all sides in sight. Since staying in the single market is not currently an option for the British, an agreement on the lowest possible customs duties and streamlined clearance procedures based on random sampling is important. The feared lorry queues at borders and the associated risks and costs for companies and their customers could be minimised in this way. This would also help to address the "Irish issue".

Second, the aim should be to ensure continuity in existing product standards and authorisations. The British government's White Paper states that the United Kingdom wants to continue to comply with the European Union's common rulebook for product standards and authorisations for goods that need to be checked at the border. This would create continuity for companies. However, this selective compliance with EU law for product standards and goods authorisations is very difficult to match with the principle that the EU fundamental freedoms are indivisible. In addition, the EU side takes a critical stance on the proposal that the United Kingdom only wants to comply with the requirements of the common rulebook which have to be checked directly at the border. According to chief negotiator Barnier, this means for instance that the British would no longer have to meet requirements for pesticides and genetically modified food.[16] Should a continuation of the free movement of goods end due to the European Union's objections and the British red lines, the negotiating partners should nevertheless ensure that the continuation of existing product standards and authorisations is agreed in the framework of an enhanced regulatory dialogue.

In addition, both the European Union and the United Kingdom should appoint additional officials for customs processing and make changes to processes and systems.

[16] Cf. European Commission, Press statement by Michel Barnier following the July 2018 General Affairs Council (Article 50), 20 July 2018, at http://europa.eu/rapid/press-release_STATEMENT-18-4626_en.htm.

Depending on the complexity of the rules, considerable new capacities are needed in order to ensure that there are no long and economically costly waiting times. The same applies for product authorisations. This is the only way to avoid loss-generating time delays and excessive administrative costs for companies from both sides of the English Channel.

3.2 USE CASE: DATA PROTECTION

3.2.1. Overview

From the angle of data protection, the question arises as to how the United Kingdom should be classified with regard to the level of data protection and transfer of personal data between EU Member States and the United Kingdom after withdrawal from the European Union. With Brexit, the United Kingdom will become a third country with respect to data protection. This entails far-reaching consequences for future transfer of personal data from the European Union to the United Kingdom.[17] All relationships with British companies or companies with UK locations where personal data are transferred would have to be reviewed and new agreements concluded. A contract on the processing of personal data in accordance with § 62 BDSG[18] or article 28 GDPR[19] (data processor) is no longer sufficient.

With the classification as a third country, the same conditions would initially apply for the United Kingdom as for other third countries such as the USA or China: Until the recognition of equivalence by the European Commission, the level of data protection will be deemed to be less secure than inside the European Union independent of the actual design of the system. The stricter requirements laid down in GDPR for transfer to third countries would then have to be met for transfers of personal data across the European border in order to safeguard an adequate level of data protection.

GDPR sets out different conditions under which an adequate level of data protection is ensured for a third country transfer and the transfer of personal data to the United Kingdom is possible:

- An adequacy decision by the European Commission could put the United Kingdom on the level of a "secure" third country and enable straightforward data transfer.

- If an adequacy decision has not been issued when the United Kingdom withdraws, companies residing in the European Union, which want to continue to

[17] Cf. European Parliament, The future EU-UK relationship: options in the field of the protection of personal data for general processing activities and for processing for law enforcement purposes, August 2018, at http://www.europarl.europa.eu/thinktank/de/document.html?reference=IPOL_STU(2018)604976.

[18] BDSG: Bundesdatenschutzgesetz (Federal Data Protection Law) of 30 June 2017, BGBl. I page 2097.

[19] GDPR: General Data Protection Regulation: Regulation (EU) 2016/679 of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing directive 95/46/EC.

transfer personal data to companies with British seat, must themselves become active at an early stage and take measures to create the conditions for third-country transfer.

This concerns not only companies which transfer personal data to service providers (e.g. cloud, IT, or payment providers) and other UK based contractors but also all companies which exchange personal data with a group company with UK seat, be it the parent company or a subsidiary. Specifically in the case of a transfer within a group considerable consequences for the entire business model or even the location question must be considered at an early stage.

Furthermore, companies of all sectors process personal data to a greater or lesser extent, often also across borders, in areas including logistics, human resources management, clinical and other studies, insurance and bank contracts, travel, customer care, etc. The list continues. Consequently, virtually every company that is active in the United Kingdom in any way is affected. This means that everyday business traffic such as forwarding an email to colleagues in an UK branch would no longer be possible without a justification under data protection law. Bearing in mind the level of liability and sanctions which the GDPR contains, the legal uncertainties weigh particularly heavily.

3.2.2. Measures by companies

Even without an adequacy decision, a transfer of data is not completely impossible. Article 46 (1) GDPR makes a transfer without an adequacy decision possible, provided that appropriate safeguards are in place. Article 46 (2) sets out how these safeguards can be established:

- Conclusion of EU standard data protection clauses with the company residing in the United Kingdom.

- Alternatively, conclusion of so-called binding corporate rules within a group. A legal framework for the transfer of data within a group to a company of the same group with its seat in a third country is created by internal data protection provisions. However, such binding corporate rules need to be endorsed by the competent supervisory authority, which might take a long time.

- Alternatively, the consent of the persons whose data are to be transferred. The hurdles which GDPR places on effective consent are high, and consent does not offer a workable and reliable basis, specifically for businesses dealing with the general public or for the transfer of employee data to group companies.

The possibilities for data transfer without an adequacy decision are consequently very cost- and time-intensive for companies and hence are often not practical. They allow data transfer for day-to-day business transactions – either within a corporate group or with third parties – just with a certain amount of effort. Consequently, supervisory authorities and legislators are invited to create a functional basis for the processing and transfer of personal data between the European Union and the United Kingdom.

3.2.3. Recommendations to supervisors and legislators

To ensure the secure transfer of personal data between the European Union and the United Kingdom also after Brexit, regulators and supervisory authorities on both sides must create legal certainty for companies with regard to the conditions for continuing data transfer already before March 2019.

The United Kingdom made it clear in its White Paper that it does not plan to depart from the level of protection provided under current EU data protection law. It proposes to establish a data protection mechanism which would prevent a fundamental watering-down of the current level of protection through a regular regulatory exchange. The proposals have been positively received on the EU side but this does not mean that there will be an automatic adequacy decision by the European Commission.

Deutsches Aktieninstitut therefore recommends that both negotiating partners work together to put in place as rapidly as possible the conditions for adoption and maintenance of an adequacy decision at the point of Brexit. In this way, companies and authorities alike can continue to transfer personal data with legal certainty.

If an adequacy decision (currently) is not possible, companies transferring personal data to companies with UK seat must know under what conditions this transfer continues to be possible following Brexit. For this, they need the corresponding guidance and assistance from the competent authorities.

3.3 USE CASE: DERIVATIVES

3.3.1. Overview

Nonfinancial and financial companies use derivatives for risk management purposes as well as for trading activities. In the risk management of nonfinancial companies, OTC derivatives[20] in particular are a strategic necessity to hedge against interest rate, currency, and commodity price fluctuations. Financial companies use derivatives above all for hedging purposes, market making, and portfolio management. The explanations below focus on OTC derivatives with and without clearing obligation as well as on commodity derivatives of nonfinancial companies.[21]

[20] Over-the-counter derivatives (OTC derivatives) are derivatives which are not traded on an exchange but directly between market participants.

[21] In order to simplify, the fact that companies do not as a rule trade or clear directly but effect these transactions via clearing members is not explained in greater detail in the subsequent text. Further information can be found in the clearing conditions of relevant CCPs or trading venues.

OTC derivatives with or without clearing obligations under EMIR[22]

In line with the rules adopted as a reaction to the 2008 financial crisis, it is obligatory to hedge OTC derivatives in certain cases in order to reduce the systemic risk of derivatives transactions for financial markets. This includes in particular documentation and notification obligations as well as collateralisation obligations. Furthermore, the European Market Infrastructure Regulation (EMIR)[23] defines which EU companies have to hedge which of their OTC derivatives transactions additionally via a central counterparty (CCP) (clearing). In this regard, EMIR distinguishes between three categories of company:

- Nonfinancial counterparties (NFC-) are companies whose derivatives transactions serve hedging purposes and are therefore not deemed to be particularly risky for financial stability. In this respect it is decisive that the volume per class of derivatives, which do not serve a hedging purpose, is below the EMIR clearing threshold. NFC- are currently not obliged to clear under EMIR. For OTC derivatives which are not defined by ESMA as being subject to the clearing obligation, no collateralisation is needed. The great majority of companies in the real economy falls into this category.

- (2) NFC+ and (3) financial counterparties (FC): Both company categories are obliged to clear under EMIR. This does not apply for all derivatives transactions but only for the derivative types defined in the ESMA implementing regulation.[24] NFC+ exhibit a higher risk profile for the financial system than NFC-, since their volume in derivatives, which do not serve as hedging, is above the EMIR clearing threshold. The same applies for FCs due to their strong integration in the financial system.

Derivatives business after Brexit

With Brexit, the possibility to provide cross-border financial services in exercise of the EU single market freedoms under simplified conditions out of or into the United Kingdom ("EU passporting") will disappear. This means:

- The offer of derivatives contracts out of the United Kingdom into the European Union using an EU passport will no longer be possible in accordance with EMIR and MiFID II/MiFIR[25]. This does not mean that old contracts will automatically become unauthorised business.

- In addition, UK trading venues which are currently authorised under MiFID II/MiFIR will become third-country trading venues with the consequence that the

[22] Detailed explanations about clearing in the context of Brexit can be found in Deutsches Aktieninstitut's second position paper on Brexit of October 2017.

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

[24] Cf. ESMA, Clearing obligation and risk mitigation techniques under EMIR, 2018, at https://www.esma.europa.eu/regulation/post-trading/otc-derivatives-and-clearing-obligation.

[25] MIFID II: Revised Markets in Financial Instruments Directive: Directive 2014/65/EU of 15 May 2014 on markets in financial instruments and [...].
MiFIR: Markets in Financial Instruments Regulation: Regulation (EU) No. 600/2014 of 15 May 2014 on markets in financial instruments and [...].

trading obligation in accordance with MiFIR can no longer be met via these UK trading venues.

- UK clearing houses will also lose their EMIR authorisation and will become third-country CCPs with the consequence that EU companies may no longer clear their OTC derivatives via these UK CCPs.

However, EU law comprises so-called third-country regimes for certain services and service providers. These give companies from non-EEA countries uniformly regulated access to EEA markets under certain conditions. These third-country regimes will also be applied to the United Kingdom after Brexit, if no other bilateral arrangement is agreed. For instance, EMIR and MiFID II/MiFIR contain rules on recognition of CCPs and trading venues established in third countries. Third-country financial service providers can also offer securities services to professional clients and hence derivatives after recognition by the European Commission.

These third-country regimes are conditional on recognition of the equivalence of the third country's legislative and supervisory framework with EU requirements by the European Commission. This procedure is very unwieldy and the United Kingdom can start this process only after Brexit. At the same time, these rules have the drawback that they can be revoked at relatively short notice. As a result, they are not a reliable basis for the continuation of the high volume of derivatives business between the European Union and the United Kingdom. This means that EU market participants have a very large incentive to relocate their new business and, in case of doubt, also their existing business to the European Economic Area.

Existing derivatives contracts will not automatically become unauthorised business. Yet, they must be checked to see whether, alongside the payment elements which are still allowed, they also contain services which may no longer be provided from the United Kingdom following Brexit. It is important to clarify (i) the extent to which contractual obligations or (ii) obligatory regulatory life cycle events (inter alia under EMIR) legally restrict the status as existing business. Under some circumstances, market participants may also prefer to relocate all contracts to one entity in order to avoid two active portfolios per financial institution.

The proposals for amending EMIR (EMIR review[26]) discussed in this context could make clearing via third-country CCPs even more difficult for EU market participants. Systemically relevant CCPs not established in the European Union should in future fall under additional ESMA supervision. If ESMA and the European Commission come to the conclusion that supervision outside the European Union is unenforceable and the CCP is of particular systemic relevance, the European Commission has the possibility of not recognising this CCP. The question of equivalence would be irrelevant in this case. If UK CCPs were no longer recognised after Brexit, a relocation of clearing for European NFC+ and FCs to an EEA CCP or recognised third-country CCP would be necessary.

[26] EMIR Review: Proposal for a regulation amending regulation (EU) No. 648/2012 as regards the clearing obligation […], 2017/0090 (COD) of 4 May 2017.

Several clearing alternatives are available in the European Union for interest rate derivatives. For instance, Eurex Clearing together with several large banks started a partnership programme in 2017 in order to avoid the risks of an obligatory relocation, in particular of euro clearing.[27] The objective of the partnership programme is to stimulate development of an alternative, liquid service offer for clearing interest rate derivatives in the European Union. In June 2018 the average cleared daily volume of euro-denominated interest rate derivatives was 67 billion euro, and the outstanding nominal volume was 7.2 trillion euro. This means that Eurex Clearing now holds a share of around 8 percent of the worldwide euro-denominated interest rate derivatives market, which was previously settled almost exclusively by the London Clearing House (LCH).[28] However, EEA CCPs do not yet offer all currencies cleared on LCH for interest rate derivatives. As a result, not all interest rate derivatives can currently be relocated to the European Economic Area due to an absence of alternatives.

By contrast, NFC- which are not subject to the clearing obligation are hardly affected by the relocation of OTC derivatives clearing. However, Brexit could have negative consequences for those NFC- which trade commodity derivatives via UK trading venues. The disappearance of the authorisation for British trading venues without a simultaneous third-country recognition would lead to commodity derivatives currently traded on an exchange to be classified as OTC derivatives. If these commodity derivatives are used to hedge against commodity price fluctuations, they continue to be irrelevant for calculating the clearing thresholds. Conversely, all other commodity derivatives which are not defined as hedging derivatives would have to be credited to the threshold values for the clearing obligation on NFC-. The classification of previously exchange-traded commodity derivatives as OTC derivatives would force companies with a high volume of commodity derivatives not classified as hedging instruments[29] to reduce their trading volume or relocate parts to an EEA or recognised third-country trading venue. They could otherwise be subject to a binding clearing and collateralisation obligation at high costs. Reduced liquidity and increasing prices for these commodity derivatives would be possible consequences. This in turn could cause problems with the risk controlling of all nonfinancial companies which use commodity derivatives as part of their risk management.[30]

Currently, there is no clearing or trading alternative within the European Economic Area or a recognised third-country alternative for all commodity derivatives. For electricity and gas derivatives, there is the possibility of clearing via EEA trading venues, e.g. European Commodity Clearing AG (ECC). The same is not the case for metal derivatives on the London Metal Exchange (LME), which is the only liquid trading venue worldwide for trading and clearing of metal derivatives.

For companies which trade derivatives on UK trading venues and/or clear them via UK CCPs and for which there is no alternative in the European Economic Area or no recognised third-country provider, a particularly precarious situation arises in the event of a hard Brexit. For British trading venues and CCPs, there will not yet be any recognition at the time of Brexit.

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[27] Cf. Eurex Frankfurt AG, Partnership Program gains traction, 3 July 2018, at http://www.eurexchange.com/exchange-en/about-us/news/Partnership-Program-gains-traction/3437184.

[28] Cf. European Central Bank, European CCPs after Brexit, 20 June 2017, at https://www.ecb.europa.eu/press/key/date/2017/html/ecb.sp170620.en.html.

[29] This relates above all to commodities but also to futures and options with the underlying interest rates and currencies.

[30] The same issue exists theoretically for other derivatives but in practice is of secondary relevance (small share of stock exchange trading).

At the same time, there is no alternative for a relocation. As a result, trading will hardly still be possible for certain derivatives. Simultaneously, under the terms of the Capital Requirements Regulation (CRR[31]), British CCPs will become "non-qualified CCPs", which would entail an immense increase in capital requirements – hence also for existing business – for regulated EU market participants.[32]

Non-European market participants who currently make up the major portion of market liquidity would not be affected by the loss of the EU authorisation of CCPs and trading venues. They would therefore possibly have no incentive to relocate parts of their business activity. In addition, European market participants could also relocate parts of their business activity to recognised third-country CCPs such as CME in the USA. This could lead to a fragmentation of certain derivatives markets.

3.3.2. Measures by companies

The consequences of Brexit for derivatives business with or without clearing obligation faces market participants with major challenges. Companies must verify whether and how a relocation of OTC derivatives as well as the associated clearing is possible. There are large differences between the effort and the possibilities for a relocation of new business and existing business.

OTC derivatives business without clearing obligation

With a positive equivalence decision from the European Commission in the framework of the third-country regime under MiFID II/MiFIR, nonfinancial companies, categorised as professional clients, could theoretically keep their derivatives business in the United Kingdom after Brexit. Provided that their counterparts are covered by the equivalence decision. Since equivalence is unlikely to be recognised at the time of Brexit and as it offers little certainty, they will very probably relocate their derivatives contracts to an EEA financial institution anyway. This applies in particular for new business. In addition, companies must check whether existing derivatives contracts should also be relocated to EEA countries. In any case, new framework contracts will have to be concluded between the financial institution in the European Economic Area and the nonfinancial company. Subsequently, existing and/or new contracts can be relocated to the EEA financial institution.

Existing business: Even if existing derivatives contracts do not automatically become unauthorised business, they must still be checked as to whether they contain services which may no longer be provided from the United Kingdom after Brexit. It is important to clarify (i) the extent to which contractual obligations or (ii) obligatory regulatory life cycle events (inter alia under EMIR) legally restrict the status as existing business.[33] In other words, which life cycle events such as changes to the notional amount, contract duration, novations, portfolio compression/unwinds, or exercise of options, count

[31] CRR: Capital Requirements Regulation: Regulation (EU) No. 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms and [...]

[32] Cf. findings set out in Deutsches Aktieninstitut's second position paper on Brexit of October 2017.

[33] Cf. ISDA and afme, Contractual Continuity in OTC Derivatives Challenges with Transfers, July 2018, at https://www.afme.eu/globalassets/downloads/publications/afme-isda-contractual-continuity-in-otc-derivatives-challenges-with-transfers.pdf.

as new business and which local licensing requirements might be triggered? Some of these cases will not be relevant, since they will be dealt with in practice by termination of the old and conclusion of a new transaction.

New business: By analogy with existing business, new business must be relocated to the EEA entity after new framework contracts are agreed.

OTC derivatives business with clearing obligation

If UK CCPs are not given third-country recognition in the European Economic Area, companies should check whether and how a relocation of clearing to an EEA and/or a recognised third-country CCP is possible. It is also conceivable that UK CCPs will relocate to the European Economic Area.

Existing business: A relocation of existing business will hardly be possible in many cases: Among other things, it is not only necessary to close and newly establish the relevant clearing transactions, the deposits provided will also have to be transferred and reorganised. This would affect not only the direct relationship between clearing members and CCPs but also clearing members' customer relations: As a result, not only would there have to be a new link-up of clearing members to alternative CCPs and the re-establishment of previously closed positions with this new CCP. Furthermore, all contractual relations between clearing members and their customers would also have to be re-organised and then the transactions underlying the cleared transactions would have to be newly established between the clearing member and the customer. This would be extraordinarily challenging legally and operationally and would entail considerable risks, such as disproportionate cost increases for market participants, inefficiencies, and/or a decline in market liquidity.

New business: New business also faces the challenge of a relocation. Even though the EEA CCPs would be technically and operationally in the position to extend the necessary infrastructure fairly rapidly for many products, a relocation cannot be envisaged immediately. European market participants' current need for clearing service offers cannot be substituted immediately elsewhere with a corresponding product coverage, since the capacities needed for a functioning clearing market and the necessary market liquidity must first be developed. Moreover, no alternative (liquid) service offer for certain asset classes or currencies exists. The build-up takes time and thus, in some circumstances, is only possible in the medium or long term.

Commodity derivatives of nonfinancial companies

Existing business: If British trading venues lose their EU authorisation with Brexit and will not be granted immediate third-country recognition, commodity derivatives traded on these British trading venues would be classified as OTC derivatives. As a result, they have a direct influence on the threshold values for the clearing obligation of NFC-, if these derivatives are not being used exclusively for hedging. Affected NFC- must consequently review their commodity derivatives volumes and if necessary reduce their exposure or relocate transactions to an EEA or recognised third-country trading venue – if this is possible.

New business: By analogy with existing business, affected NFC- must check whether new exchange-traded commodity derivatives have to be traded via EEA or recognised third-country trading venues in order to not exceed the clearing threshold.

3.3.3. Recommendations to supervisors and legislators

For many market participants, derivatives and clearing possibilities are of central importance for their risk management but also for trading. In addition, short-term changes to the clearing infrastructure involve considerable risk due to the concentration of large derivative volumes on certain markets, which have developed historically. The overarching objective must be to safeguard the stability of European financial markets but at the same time to maintain the efficiency of the market and take the interests of EU market participants into account.

As already set out in the two previous position papers, it is essential to eliminate the identified gaps in the existing third-country regimes under MiFID II/MiFIR and EMIR. This should be done not only in the context of Brexit but also in the longer term in the review of the third-country regime planned by the EU institutions.

To prevent market turbulence and disadvantages for European market participants, grandfathering of existing derivatives contracts is particularly important. These contracts are typically of long duration. Thus, around 40 percent of transactions on the London Clearing House have a duration of more than two years, over 30 percent a duration of longer than five years.[34] Even though old contracts will not automatically become unauthorised business, certain life cycle events or constellations could be classified as new business and require a relocation. As already pointed out, since individual market participants cannot solve the issue, BaFin is also pushing for a political solution for derivatives contracts.

For the transfer of derivatives contracts into the European Economic Area, an appropriate transition phase with grandfathering of existing contracts should be foreseen – even if no withdrawal agreement in concluded. In this way, a large portion of derivatives contracts would expire automatically on the basis of their initial duration. This would create free capacities for companies to give priority to implementing a relocation of new business with legal certainty. The draft text adopted by the European Parliament on the EMIR review calls for such a transition period for the relocation of clearing to an EEA or recognised third-country CCP. For new business, an appropriate transition period is also needed for certain products and segments (above all for trading venues and clearing service providers), if no EEA or recognised third-country alternative exists. This would mean that business activities can be continued until the British service providers are recognised by the European Commission or an alternative service provider has established itself in the market.

In addition, it is necessary to have clarity about supervisory practice in the European Union during this transition period and to create corresponding incentives for non-European market participants to clear in the European Union in order to increase market liquidity. Appropriate supervisory monitoring of derivatives contracts and of clearing must be ensured during this transition period.

[34] Data based on official information from LCH as a proportion of the total volume, 27 April 2018, at https://www.lch.com/services/swapclear/volumes.

4 CONCLUSION

The United Kingdom's withdrawal from the European Union is coming closer and will lead to major changes in Europe. What these will look like continues to be unclear and depends on the outcome of the Brexit negotiations.

This third position paper shows that there are many problem areas which are of particular delicacy and which companies cannot solve exclusively through their own measures, either due to a shortage of time or because the regulatory, supervisory, or market-related framework conditions do not (yet) permit.

It is up to the negotiators to find constructive and practical solutions as rapidly as possible in order to minimise the negative effects of Brexit on the affected economies. Business and population alike want technically sound and rational decisions reached by balancing out all positive and negative consequences.

As competent discussion partners, Deutsches Aktieninstitut and its members remain at the disposal of the negotiators and other interested parties to examine the issues discussed above.

Annex:

EU passporting and third-country regimes in European financial and capital market 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 parts 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 through the EMIR Review.	
	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, but restrictions are expected through the EMIR Review.	
	Yes, for trade repositories		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.	
CRAs	Yes, for rating agencies.		Yes, but only for third-country companies and if no systemic relevance for EU financial stability (certification).	CRAs which cooperate closely with an EU CRA and are subject to a comparable regime can be endorsed by an EU CRA (endorsement). Yet, ESMA considerably tightened the requirements.

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ISBN 978-3-934579-87-3

www.dai.de