Brexit planning: Changes to UK law

FCA CP18/29
Temporary permissions regime for inbound firms

How the temporary permissions regime will work

Why is the TPR needed?

> **No deal, no transition:** The draft agreement on the terms of the UK’s withdrawal from the EU includes a transition period up to 31 December 2020. If the deal is not finalised, then the transition will not take effect. In this event, passporting of financial services into and from the UK would end at exit day (11pm 29 March 2019).

> **Unilateral UK transition:** To prepare for this possibility, the government has introduced a temporary permissions regime (see our previous note). The TPR acts as a unilateral transition period for incoming EEA firms. EEA firms that participate in the TPR may, for a period after exit day, continue to operate in the UK on a cross-border or branch basis in accordance with their passport permissions immediately before exit day.¹

> **Home v host state rules:** In some areas of regulation, EEA firms passporting into the UK are subject to different rules to UK authorised firms. This generally happens where the EU regime gives responsibility for those rules to the home state regulator rather than the host state regulator (in this case, the FCA).

> **New status for TPR firms:** From exit day, all TPR firms will be treated as if they are UK authorised firms. The question is then: should the FCA apply the full scope of the UK regulatory regime to TPR firms (as it does for non-EEA firms) or roll over the regime as it applies today to passported firms?

> **Regulatory approach:** The FCA has now published a consultation on its approach which aims to balance these alternatives. The PRA will consult on its approach to the TPR later in the autumn, which will be of interest to EEA banks, insurers and PRA-regulated investment firms.

¹ This note focuses on the TPR as it applies to EEA firms passporting into the UK. There are similar temporary regimes for EEA fund managers, e-money institutions, payment institutions and account information service providers. We cover the impact on these firms in separate notes.

FCA, October 2018

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The potential abrupt loss of passporting rights creates risks to consumer protection and market integrity. TPR is key to reduce these risks.

FCA, October 2018
What is the FCA’s approach to the TPR?

> **Overall approach:** The FCA has said generally TPR firms will continue to apply rules which currently apply to them, either in the UK or their home state.

> **Regime for TPRs:** A TPR firm will need to comply with the following for its UK business:

  1. The FCA rules which currently apply to it
  2. Those FCA rules which do not currently apply to it because they are reserved to the firm’s home state regulator – the FCA will accept substituted compliance for these
  3. Specified additional FCA rules

> **Substituted compliance:** The FCA will apply rules to TPR firms which before exit day would have been reserved to the home state regulator. However, the FCA will deem compliance with these rules where firms can demonstrate that they continue to comply with the equivalent home state rules for their UK business. The FCA does not specify how it expects firms to evidence such compliance in practice.

> **New rules for TPR firms:** Certain FCA rules will also be applied to TPR firms. Some of these are intended to ensure appropriate consumer protection (e.g. new disclosure requirements). Others relate to funding and reporting requirements (e.g. the FSCS levy and client asset reporting).

> **PRIN:** The Principles will apply in full to TPR firms, except Principle 4 (financial prudence) which will be limited to where the TPR firm is currently subject to UK capital adequacy rules. TPR firms will need to take care to comply with Principle 11 (relations with regulators); depending on the circumstances, notifying a matter to their home state regulator may not be enough to meet this requirement.

> **CASS:** TPR firms may rely on substituted compliance to meet CASS requirements that derive from MiFID and the Insurance Distribution Directive. However, TPR firms will have to report their client asset arrangements to the FCA and disclose to their clients at exit day how their assets would be treated on insolvency. They may also need to provide the FCA with an English translation of client asset audits.

> **Individual accountability:** The FCA will continue to apply the SMCR or Approved Person requirements that apply to EEA branch firms under the TPR. The additional requirements that apply to third country branches will only apply once the firm has been granted UK authorisation at the end of the TPR.

> **Compensation protection:** The FCA proposes to extend FSCS protection to customers of EEA branches and so branches under the TPR will need to pay FSCS levies for the first time. EEA services firms will need to notify their clients that they are not protected by the FSCS.

> **Other funding requirements:** TPR firms will be required to contribute to the Single Financial Guidance Body costs on the same basis as UK authorised firms. This effectively removes the discount for EEA branches and brings EEA services firms into scope for the first time. EEA services firms will also be brought into the compulsory jurisdiction of the financial ombudsman service and so will be subject to FOS fees and complaints-handling rules.

> **Regulatory capital:** The FCA does not propose to apply additional capital adequacy rules on TPR firms.

> **Supervisory flexibility:** There will be flexibility for firms where the reduced scope of a UK rule makes it no longer practicable for a TPR firm to comply. There will also be a carve-out where compliance with a UK rule would mean breaching a home state requirement.

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TPR firms can start from the position that they should follow the same rules as those that they presently need to comply with in their home state in respect of UK business.

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What happens next?

> _Regime to be finalised before exit day:_ The FCA intends to give feedback on the consultation in early 2019. It will publish final rules shortly before exit day. The PRA is expected to announce its proposed approach in the coming weeks.

> _More consultations in the pipeline:_ The FCA will separately consult on the proposed rule changes relating to FSCS and SMCR, status disclosure requirements for TPR firms, and arrangements for Gibraltar-based firms.

> _Notification process:_ EEA firms must notify their intention to participate in the TPR to the FCA before exit day. If a no deal outcome looks likely, the FCA will open a notification window in early 2019. The notification will be made via Connect.

> _No variation in permissions during TPR:_ Firms will not be able to add new permissions while under the TPR. The firm will have to apply for new activities as part of its application for full authorisation in the UK (see the next two bullets).

> _Applying for authorisation during the TPR:_ Firms that want to continue to operate in the UK after their temporary permission expires will need to apply for authorisation as a branch or seek to rely on exemptions from licensing requirements (such as the overseas persons exemption).

> _Length of temporary permission:_ Overall the TPR is expected to last three years after exit day. Within that period, firms will be given a three-month “landing slot” during which time they will need to apply for UK authorisation and after which their temporary permission will expire. Firms will be notified of their landing slot shortly after exit day. Slots will be granted according to business type. The first landing slot will be October to December 2019.

> _Winding down UK business:_ A mechanism will be put in place for firms which do not become authorised (e.g. because their application is rejected) to wind down their UK business after their temporary permission expires. The Treasury is expected to provide more detail on this in due course.

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The TPR has been designed to allow firms that passport into the UK to continue their UK regulated activities for a limited period while working towards authorisation in the UK.

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Further resources

We have published a note on the SI that establishes the temporary permissions regime and a note on the regulators’ approach to Brexit.

We have also published a note on CP18/28 (the FCA’s first consultation on proposed changes to its Handbook and binding technical standards). CP 18/28 was published alongside CP18/29 on the temporary permissions regime.

For more information on Brexit SIs, and Brexit generally, please visit our:

> Brexit Knowledge Portal
> Linklaters Brexit homepage

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