Strategy in a politically uncertain environment

Board considerations for financial services firms

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February 2020
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Minds made for building financial services

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Introduction

With the UK's formal departure from the European Union (EU) now complete, the UK and EU have entered a new phase in the unwinding of their relationship. As well as negotiating a new UK/EU free trade agreement, the UK will be looking to revise its cross-border relationships with countries around the world. Firms operating across these geographies will be trying to anticipate what these future cross-border trading relationships will look like, amidst continuing political uncertainty both in Europe and globally.

As of 1 February 2020, the UK and EU are in a ‘status quo’ transition period, during which EU law continues to apply in the UK. Free movement of goods, services (including financial services passporting), capital and people continues, along with the implementation of new EU laws in the UK, until 31 December 2020. During this period we will see both sides trying to negotiate a new trade relationship to be ready for 1 January 2021, but time is short.

Under the UK’s Withdrawal Agreement, there is an option to extend the transition period for one or two years, but both sides must agree to such an extension by 1 July 2020. The UK Government has for now legislated away the possibility of using this formal extension mechanism, but this issue will no doubt be subject to scrutiny as we approach July and possibly again towards the end of the year via other mechanisms. In relation to financial services, both the UK and EU set out in their political declaration that they would like to conduct equivalence assessments over the other’s financial services sectors by June 2020. This is an aspiration, not a commitment, and any subsequent determination can be linked to other elements of the negotiation. Much attention has already been drawn to the fact that the political declaration sets out the mid-2020 timeframe to conclude and ratify a deal on the sharing of EU/UK fish stocks. The political declaration also sets out a similar aspiration for the EU and UK to make reciprocal data adequacy determinations by the end of 2020, to allow for the free flow of personal data between the two jurisdictions. However, again there is no legal commitment that this will be achieved.

As the clock ticks down to a new raft of negotiating, political and regulatory deadlines, firms will be thinking about their response. And this political volatility cannot be seen in isolation, with climate change, technological disruption, operational resilience and a host of other big issues facing financial services.

Our paper examines the major issues boards will face in the context of this uncertainty, as well as the lenses that can be applied to reviewing strategy. We are grateful to all those who have taken the time to contribute to our thinking and welcome the opportunity to debate and discuss the views presented in this document.

Considerations for boards should include, but not be limited to:

- How long will the transition period ultimately last and financial services passporting continue?
- Which (if any) of the EU’s forty plus equivalence assessments will be made by the end of June 2020, and will these lead to political determinations?
- Will the UK and EU negotiate any enhanced cross-border financial services terms as part of a comprehensive trade agreement?
- Will the UK seek to diverge from EU standards in financial regulation and taxation? What opportunities might this provide and what cost might there be to EU market access?
- What alignment/cross-border access might the UK agree with other third countries?
Now that the UK has left the EU, boards will want to monitor progress on the negotiation of the trade agreement and, in particular, the position of financial services, including the movement of data and people. The calendar below sets out the key dates to look out for.

**Calendar***

- **31 Jan 2020**: UK left EU
- **1 Feb 2020**: Status quo transition and negotiations on a new EU/UK relationship began
- **Feb 2020**: EU negotiating mandate expected to be published
- **11 Mar 2020**: UK budget
- **31 Dec 2020**: End of transition period (unless extended)
- **31 Dec 2022**: Last possible extension date for transition period
- **8 Feb 2020**: Irish general election
- **Early Feb 2020**: Cabinet reshuffle expected
- **End Jun 2020**: Target date for EU/UK equivalence assessments
- **EU/UK transition extension deadline**
- **1 Jan 2021**: Launch of EU seven-year budget (2021–2027)

* Subject to change
In the absence of further agreement, the UK and EU will trade on World Trade Organization (WTO) terms from 1 January 2021. That leaves 11 months for both sides to complete negotiations around a range of topics, including trade in goods, services, movement of people, security, state aid and tax.

The Political Declaration sets out a non-binding framework for how the two sides will trade after the transition period. For financial services, the relationship proposed is based on equivalent regulatory and supervisory regimes, but will be unilateral and revocable. The key clause is set out opposite. Equivalence determinations do not require a trade deal, but there is always a political element to them, meaning one or both sides could demand a broader trade agreement as a pre-condition.

The EU Commission has recently restated the political declaration commitment that: “Parties should start assessing equivalence with respect to each other under these existing frameworks as soon as possible after the UK’s withdrawal, endeavouring to conclude assessments before the end of June 2020”. The fact that the UK and EU regulatory frameworks are aligned will be a good starting point, although Commission has flagged that the higher the possible impact on EU markets and interests, the more granular the equivalence assessments. The Commission and the UK recognise that the current equivalence regimes, which are fragmented across EU financial services law, do not provide market access in a number of key areas (such as banking and payments) but the FCA believes that as “both the UK and EU are committed to open markets, there is also a strong rationale for both sides to discuss broadening their respective equivalence frameworks”.

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2 Global regulation, local solutions’, January 2020 speech by Nausicaa Delfas, Executive Director of International, FCA

Refer to ‘EU and UK Trade Agreement Protocols’ in the Annex
Strategic board considerations

Governance structure

Political and regulatory risk discussions at board level are often event focused – for example, on the outcome of an election. There can also be value in exploring deeper underlying trends and potential causes which help explain why the event occurred. This may allow boards to fully evaluate their company’s resilience to bigger, underlying shifts, rather than just focus on immediate shifts such as a change in government.

Events can be easier to describe for a risk register, but it is trends that ultimately matter most. Is the board’s view of socio-political risk analysis event-driven, or trend-driven and if the latter, how does it monitor these trends, including the speed at which they are evolving?

With the right governance in place, these questions can be answered with appropriate transparency and accountability. They can also have a significant impact on the right structure for the business moving forward, its geographic footprint and the appropriate mix and scale of branches and subsidiaries, which in turn needs governance review. Clarity around responsibilities and reporting lines of senior managers across the organisation will be essential.

How should we manage political risk?

Considerations for boards should include, but not be limited to:

- How are we incorporating assessments of political risk into our wider deliberations and strategy?
- What is our risk appetite and exposure to political risk?
- How much of our firm’s political risk profile is the board being properly exposed to?
- Are we thinking of political risk as a set of deeper and wider trends and expectations as well, rather than just a series of ‘events’ to be managed?
- What information is being presented to us on political risk to enable us to ask the right questions, and does it utilise all potential information sources?
Strategy in a politically uncertain environment

Do we have the right governance structure?

Firms need to look beyond the event and consider their governance in the light of wider regulatory and socio-political trends, factoring-in business information that brings insights from across the firm or group’s geographical scope, so that they become designed to weather more than one storm.

Regulatory and cross-border trading developments, due to an event like Brexit, pose a range of additional structural and governance questions. Considerations for boards should include, but not be limited to:

• Are reporting lines clear about who is in charge and where responsibility sits in each legal jurisdiction?
• Where do senior managers sit and is that acceptable to our regulators?
• Can we count on sufficient operational resilience across the group, for us and our regulators?
• Do we have assurance that local regulatory requirements are being met?
Client management

Client management and ensuring the right outcomes for clients has been a significant component of firms’ Brexit planning. However, clients have also been affected by other forms of uncertainty in recent times, including ring-fencing and MiFID II. The resulting outreach on each of these issues will continue through other events — IBOR replacement, for example, is a key upcoming driver.

Each event has its own nuances, and the solutions devised by firms in response will lead to different forms of outreach and client engagement. During Brexit, financial institutions have asked clients to perform a range of actions relating to cross-border mergers, Part VII transfers or/and bilateral negotiations.

As a result of this complexity, and the increasingly recurring nature of these ‘one-off’ events, there is now a significant advantage for firms who design and handle client outreach programmes in a consistent manner, building on lessons learned about controls, the technology to improve efficiency and the nature of the conversation, to handle conduct risks.

A common principle underpinning these outreach activities is ‘maintain the client franchise’. However, this recurring requirement can serve to distract from some more strategic considerations about the client base. This leads to some specific questions:

- Which clients are more profitable and over what timescale?
- When do we offboard?
- What do we consider to be the tail?
- What may reasonably be a peer’s ‘tail’ that we can prospect?

Faced with a disruptive event, it is often easiest to manage execution risk and, in doing so, not conflate the outreach requirements with bigger considerations around profitability and tail, among other issues.

However, given the fact that these programmes are occurring again and again, firms should instead consider the implementation of a the business as usual capability around client outreach. By doing so, they will be able to address new outreach events with more corporate memory, and with more confidence. As a result, they can deliver solutions more quickly, at lower risk, and perhaps even afford themselves time to consider more strategic client questions.
Regulatory compliance

Regulatory change is inescapable. While standards are constantly evolving and differing between jurisdictions, Brexit poses a different scale of challenge, and the impact of the UK and the EU diverging to an uncertain future relationship, leads to a range of additional regulatory issues for boards to consider.

Where firms have converted branches, or the provision of cross-border services, to locally authorised UK or EEA legal entities, it will be important to understand the full regulatory requirements (including prudential regulation), supervisory expectations and concerns of firms’ previous host state regulators and, for large UK banks, the ECB. Differences between regulatory approaches will need to be identified, addressed locally, understood at group level and monitored over time. Firms will also have to consider the impact of changes to their corporate structures and business models on their previous home state (e.g., UK) regulators. For example, the PRA expects firms to ‘remain mindful of the operational implications of withdrawal, ensuring they are able to maintain good governance and manage their post Brexit operations appropriately’.

For firms setting up new EEA entities, applications for local authorisation will have been submitted and plans will be in place. However, while some firms may be waiting to see what the future EU/UK relationship looks like before taking further steps to implement their plans, pressure from regulators to build up capabilities, as set out in the terms of new licences, is only set to increase.

In the EU, the European Central Bank (ECB) warned banks in November 2019, that operational risk increases when action is postponed. They cautioned that any extension to Article 50 ‘should not be misunderstood as a signal to further delay the implementation of Brexit plans’ as only by taking action will banks ensure that cliff-edge risks are mitigated rather than postponed.

Another area of concern to regulators is how reliant firms are on third parties. The ECB, for example, is aware that banks may be delaying transfers of assets (on the request of clients) and customers as well as necessary changes to their IT systems, operations and organisational set-up. As many of these actions may rely upon third parties, if banks were to leave it to the last-minute to implement large scale changes, there is a risk of ‘significant bottlenecks, leading to coordination failures.’ Hence their message that it is ‘imperative’ that banks speed up the implementation of Brexit plans to meet their end of 2020 deadlines. This is not just a message for banks: any firms that have made Brexit-related commitments to UK or EEA regulators, including implementation timelines agreed with supervisors, will be expected to follow through regardless of political uncertainty.

"If your firm has decided to make changes to how you operate, it is important that you ensure execution is managed appropriately. We look to the Board and executive management at firms to ensure this happens. We expect firms to focus on ensuring they make the necessary changes required to avoid harm to those clients who are impacted. Firms should only make changes where they are in customers’ best interests, avoiding making changes for customers who are not impacted and whose existing arrangements would be better left in place."

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3 PRA letter to CFOs of UK deposit takers and international banks, January 2020
4 FCA website, extract from ‘Brexit: considerations for UK firms’ webpage
Working to different compliance regimes

Considerations for boards should include, but not be limited to:

• Understanding, and preparing for, the differences between, for example: host and home state supervision in the EEA; the UK regimes for branches of EEA firms and third country firms and, for larger banks, PRA and ECB supervision

• Understanding future changes to EU financial services regulation – including the forthcoming changes to Markets in Financial Instruments Directive (MiFID II), Undertakings for the Collective Investment in Transferable Securities (UCITS), the Alternative Investment Fund Managers Directive (AIFMD) and the 2020 review of the Solvency II Directive – and the implications for business across the EU, and in the UK

• The implications of changes to corporate structures and business models for the UK Senior Manager Regime (for example, changes to responsibilities and/or reporting lines) and any equivalent EEA Member State regimes

• Monitoring development relating to the UK’s temporary permissions and transitional regimes, which will now be available, if needed, from the end of the transition period.5

• For firms that have group policies and procedures, identifying where local standards are more onerous and need to be cascaded across the group, either as an update to group policy or a local variation

• Ensuring clients are treated fairly in all circumstances, particularly where you may have to seize provision of a service

• Understanding diverging stress test requirements – for example, for large banks and insurers, the PRA biennial exploratory scenario in 2021 will include financial risks from climate change

• If using third-party outsourcing arrangements, such as fund administration, assessing the operational risk and potential harm to clients that could occur and continuing compliance with relevant EU and UK regulatory requirements

• Understanding the EU Intermediate Parent Company (IPU) requirements in CRDV and the implications for UK banking groups

• Where confirmed, understanding the ECB Asset Quality Review (AQR) of eurozone banks

A significant cause of uncertainty for all firms will be whether an adequacy assessment is agreed to allow data transfers from the EEA to the UK after the end of the transition period. It will be important for firms to take a broad view of data protection issues – involving data protection teams, regulatory compliance, legal and the business. This should also involve keeping a careful eye on developments in this area and the adequacy of their contingency planning.

5 Financial Services (Consequential Amendments) Regulations 2020
People

The people that make-up an organisation can be impacted, both in a personal and professional capacity, by political uncertainty. For firms, this uncertainty can impact the mobility of key personnel. It is important that the People and Talent agenda remains a priority for boards in times of political uncertainty and that they continue to challenge the management of their HR function at regular intervals.

To ensure operational efficiency and meet regulatory requirements, firms have used a number of approaches to ensure they have the appropriate skills and experience in the right place. This includes interim solutions such as short-term assignments or commuting. Whilst firms may need to consider short-term measures, particularly where there is ongoing political uncertainty which could limit long-term mobility of staff, they should also look to implement more permanent solutions such as developing local longer-term talent pipelines, investing in technology (for staff as well as business operations) and the transfer of knowledge.

For UK and EU firms, short-term business travel considerations from January 2021 are likely to be challenging given the limitations likely to be imposed on the permitted activities an EU or UK visitor (in the UK or EU, respectively) will be able to undertake – absent any mobility framework agreement or unilateral measures. This is made considerably more complex by the existing vague guidance and differences between immigration regimes – even within the Schengen area, EU member states often have different views on whether a given activity requires a work/residence permit or is permissible without a visa.

In situations where an activity requires a work permit/residence application, the company will then need to decide between:

- Changing the visitor’s activities so that they fit within the list of permissible activities for the destination country
- Applying for a work/residence permit, which often takes weeks/months and is expensive
- Not sending/bringing the visitor, and instead relying on local resources

In the UK, the end of EU free movement and the introduction of a new single unified immigration system will mean a significant change for firms as regards who and how they can hire and how individuals can travel cross-border, particularly in an EU context.

Considerations for boards should include, but not be limited to:

- Are you supporting current EEA employees working in the UK, or UK nationals working in the EEA?
- Has the organisation considered the financial impact of costs where EU nationals will require sponsorship post-January 2021?
- How do you currently manage your Business Traveller population and how will you manage this post-2021 from both a risk and operational management perspective?
- How are you managing reputational risk to the company around compliance?
- Are you looking at your global talent pool and your future workforce strategies?
Further, we expect to see the introduction, post-Brexit, of a pre-travel clearance requirement for EU citizens (and presumably other non-visa nationals), similar to the USA’s ESTA or the EU’s future ETIAS system.

While the UK Government’s immigration plans are still being drawn up, there are a few likely outcomes:

- Limited time for businesses to plan for the changes and, at least to some extent, a disruptive implementation from January 2021.
- A more straightforward application process both for sponsors and applicants, with multiple options to expedite processing times, at a price.
- More options for ‘self-sponsored’ visas, e.g., the Graduate Route (formerly Post-Study Work) and possible Temporary Work categories. Employers will need to weigh-up the pros and cons of encouraging staff to apply for a self-sponsored visa vs an employer-sponsored one.
- An overall reduction in the number of ‘low-skilled’ non-UK workers allowed into the UK. This will primarily be achieved through the ending of free movement, but there will be more targeted options for ‘low-skilled’ visas than are currently open to non-EU nationals. Limitations on the length of the visa and overall cost may still frustrate the use of these categories by employers.
- An increase to the volume of immigration applications requiring support – in the absence of any preferential arrangement (in a free trade agreement for example), new arrivals from the EU post-2021 are expected to need work visas in the same way as new arrivals from outside the EU currently do.
- Lastly, and perhaps most significantly, a considerable increase in the overall cost to employers of supporting immigration applications.

The UK’s Migration Advisory Committee report to the Government in late January 2020 (addressing salary thresholds and how the UK could adopt an Australian style points based system) should inform further detail by March, with possible interim changes taking effect in early April 2020.

The UK’s new Future Skills Based Immigration System is expected to come into force from 1 January 2021.
Strategy in a politically uncertain environment
For boards looking to apply best practice, there will be significant differences in the approach they will want to take — based on sector, structure, business model, location, staff and the particular challenges they are facing. Applying this to the future UK and EU relationship can raise interesting questions. Here we look at three fictional case studies in Asset management, banking and insurance.

**Asset management**
A UK-based asset manager with global portfolio management in the UK, US and Asia is currently providing cross-border services into the EEA. Two thirds of its customers are in the UK and one third in are the EU, and the firm employs approximately 2000 people.

Since the UK served notice to leave the EU, the firm has been revising its corporate and management company (ManCo) structures to cover both EU and UK fund ranges. It has a new Luxembourg based subsidiary which has been licenced, and it has now fulfilled the local regulator’s stipulated substance requirements. Of its 2,000 employees, 20 are now based in Luxembourg, with 10 moved from the UK and 10 hired locally.

Looking ahead to 2021, the board wants to think about how ongoing political uncertainty can be best managed from a governance, customer, regulatory and people perspective. Possibly the most important question will be whether delegation is preserved, allowing funds domiciled in Luxembourg to continue to be run by portfolio managers based in the UK. There will also be questions around whether equivalence in clearing houses and settlement facilities is maintained.
From a risk perspective, removal of delegation authorities to UK managers appears remote given the accord on supervisory coordination struck between the FCA and ESMA in January 2019. However, ongoing equivalence is less assured, with assessments expected in June and determinations subject to other aspects of political negotiation. Longer term, the board remains unsure whether the UK and EU might remain reasonably aligned, or whether there will be continued divergence that may ultimately threaten delegation.

Around their own governance, the board will want to be transparent about how they are viewing these risks, both in terms of their existing business and any new investments they are proposing to make. Credible and experienced non executive directors will provide essential external scrutiny and challenge in both the UK and Luxembourg.

Their governance structure will need further review, particularly given the dual reporting to both UK and Luxembourg regulators and the potential for conflict between the two. Again, ensuring transparency with all stakeholders and the board will be critical to ensuring open and honest conversations, and to identifying problems early in order for them to be discussed and fixed. And monitoring and understanding the interplay between the respective regulatory agenda (i.e., at a UK, Luxembourg and EU level) will become increasingly important.

For their existing customers, many will have adapted to the new structure, but the onboarding of new clients (i.e., where to do that and how to ensure that legacy issues do not create additional complications) should be a priority.

For their people, the limited moves will have meant little disruption to date, but uncertainty around future short-term business travel arrangements and a squeeze on talent, should be front of mind.
Banking

A global investment bank, headquartered in the US but with an established presence across major global centres has set up a new Frankfurt subsidiary in anticipation of the UK leaving the EU's single market. Its customers are located all over the world and served by around 130,000 employees.

Along with many of its peers, the bank quickly identified plans to ensure that it continued to serve all its customers in the event of a ‘no deal’ Brexit on 29 March 2019. At the heart of the board’s strategy was a commitment to maintain and defend the current client franchise, minimising operational change and additional capital and liquidity requirements. It identified an existing branch in Frankfurt that could be converted to a new subsidiary to provide a full set of corporate and investment banking services to the EU market. Around 200 people are now employed in the Frankfurt subsidiary, up from 30 in the original branch, with 60 of these having been transferred from the UK.

While the Frankfurt subsidiary is now fully licensed and operational, a good deal of further work is required to deliver on the commitments made to European regulators and ensure there is sufficient substance in location. The subsidiary is coming under pressure to have delivered on these commitments by the end of the EU/UK transition period, which is based on there being no enhanced cross-border access between the UK and EU.

A key challenge for the bank is completing the client migration activity. While a tail of cross-border EEA clients have been resisting migration until it is necessary, the bank is in the process of establishing a robust cross-border control framework to minimise potential capital and conduct risks arising because of client reluctance to migrate. This need to act is also, to some extent, dependent on the UK/ EU regulatory environment that will be in effect after the transition period. Both the bank’s UK and German subsidiaries see equivalence determinations across European Market Infrastructure Regulation (EMIR) and Markets in Financial Instruments Regulation (MiFIR) as a priority to ensure cross border access to CCPs and consistent application of the Share Trading and Derivative Trading Obligations. This would reduce the need for duplicated infrastructure and provide for access to larger more liquid markets. However, they are not sure when they might get certainty around this and whether they can afford to wait. Further, they would like to determine what sort of model they think is appropriate in the longer term, for their EU and UK clients and the appropriate level of investment for the region compared to others globally.

The Board wants to be transparent around how it is assessing these risks and opportunities, to ensure it has clear dates in mind when it will need to take decisions based on the prevailing political and regulatory conditions. This will feed into how rapidly it transfers assets and customers to Frankfurt. It will also feed into ensuring that IT, operations and organisational set-ups have been completed — many of which will rely on third parties given the industry wide infrastructure they need to access. Supervisors will also be keeping a keen eye on internal governance, business origination, FMI access, intragroup arrangements and booking models.

The governance structure and hierarchy will need detailed review, considering potentially conflicting requirements from the group’s different global regulators. Transparency and careful monitoring at a regional and global level will be key to early identification of issues that will impact the group’s regulators. The ECB’s supervisory tools, including AQRs and the Supervisory Review and Evaluation Process (SREP) drive actions and temporary tolerance compliance. In addition, the upcoming intermediate parent undertaking (EU IPU) requirements may be significant regulatory drivers.
Over the past few years, the bank's clients have experienced significant regulatory change. The board is concerned that some clients will be using the shifting EU/UK relationship to reappraise their banking relationships. It will be important for the bank to demonstrate their focus and reassurance on simplified change programmes.

The bank's international workforce have individually borne uncertainty throughout the Brexit negotiations. The board will want to ensure that, post transition period, short-term travel plans, visa arrangements as well as longer resourcing are clearly understood and communicated. Ensuring pipelines for future talent growth will also be a priority given mobility constraints.
Insurance

A UK-based composite insurer currently provides cross-border life and non-life insurance services across the EEA. It has also established a number of branches in the EEA on a freedom of establishment basis. Three quarters of its customers are based in the UK and a quarter in the EEA.

The insurer has set up a new subsidiary in France in anticipation of the UK leaving the EU. Approximately 300,000 policies (customers) will have to be transferred into the French subsidiary. Of the insurer’s 1,000 employees, 50 are based in France with 25 ‘double-hatting’ between the UK, France and other EEA branches (which have been restructured under the new French legal entity).

Several jurisdictions were assessed for the EU base, including Malta, Ireland, Germany, Luxembourg and France. France provided the majority of non-life policies and there was an existing local branch, whereas Italy provided the majority of life policies on a freedom of services basis. The decision was made to establish in France. The insurer has now fulfilled all local regulatory requirements in France (including obtaining French authorisation) as well as in all the EEA Member States in which branches are located. Looking ahead to 2021, the new group board in the UK wants to ensure that political uncertainty can be managed, at a UK level, from a customer, governance and regulatory perspective.

Given the large competitors in the EEA market, the insurer decided to create sponsorship and steering for ESG in the French firm. However, one of first steps was to establish the governance arrangements for the subsidiary, and the new group, and set key strategic priorities. A consolidated cross-functional steerco was established of the CIO, CUO and CRO to oversee key strategies for new entity, including ESG strategy.

Maintaining the client franchise has been key to the success of the restructuring. This has been maintained through existing third-party outsourced administrators, which have provided understanding of the local markets and language support for each of the branches. The strong local platforms have enabled the insurer to strengthen its client base, but the diverse nature of exposures (both by geography and liabilities) has required rigorous governance from the central entity in France.

A key challenge has been establishing a framework to enable the new subsidiary and each branch to fulfil their regulatory obligations. In a number of areas, while there are minimum harmonisation EU Directives, domestic variations in application and interpretation exist in Member States. These differences need to be identified when establishing compliance programmes and should be built into local policies, procedures, systems and controls. This requires a governance structure that assigns responsibility and accountability at a local level for each branch with supervision by the French firm. As for many
insurers who restructured for the purposes of Brexit, the first cycle of reporting and compliance was addressed by a diverse Brexit programme. However, with the continuing challenge of evolving and differing regulatory standards, which could be exacerbated at the end of the transition period, those roles have now been embedded in local structures.

The insurer has local staff in each EU Member State, which means little disruption for the business and a clear footprint in each jurisdiction. Their limited number of business travellers has also reduced disruption to date. However, as the insurer pursues its growth strategy, particularly in relation to the development of new products (including green products developed by the French firm), there will be a greater need to upskill and grow its talent pool. A key question to address is whether the subsidiary hires in France, from local branches, from the UK or, most likely, a combination of all three. This may increase the uncertainty around future short-term business travel and mobility between the UK and EEA and is on the management agenda.
UK trade negotiation protocol

As the UK has now officially left the EU, it can commence trade negotiations with the EU and other countries. In terms of global trade agreements, the UK Government’s current priorities include the US, Japan and Australia. However, any new Free Trade Agreements (FTAs) cannot be implemented until the end of the transition period, when the UK leaves the EU’s single market and customs union.

It is yet unclear whether the UK Parliament will have any enhanced involvement in ratifying a new EU/UK trade agreement, or whether ordinary treaty rules will apply. Under ordinary rules, the opportunity for Parliament to examine treaties lies primarily in analysing legislation which implements the terms of treaties (the ‘how’ rather than the ‘what’). The rest of this Annex will focus on the EU negotiation protocol, as information is more widely available.

EU trade negotiation protocol

EU negotiation protocol differs depending on whether the trade agreement constitutes a ‘mixed’ or ‘non-mixed’ agreement.

In a ‘non-mixed’ agreement, which consists entirely of matters within the EU’s exclusive competence, the EU can approve agreements on behalf of all member states. As listed in Article 3 of the 1957 Treaty on the Functioning of the European Union (TFEU), these matters for which the Union has exclusive competence are:

- Customs union
- The establishing of the competition rules necessary for the functioning of the internal market
- Monetary policy for the Member States whose currency is the euro
- The conservation of marine biological resources under the common fisheries policy
- Common commercial policy
On the other hand, a ‘mixed agreement’ involves matters of mixed responsibility between EU institutions and individual countries – i.e., it involves matters outside of the EU’s exclusive competence.

Article 4 of the TFEU specifically lists these matters which include social policy, environment and energy.

For such ‘mixed agreements’, in addition to requiring the approval of the EU parliament, all 27 member-states must also ratify the agreement according to their own national procedures (which may include regional parliaments). Ratification can be a lengthy process, the duration of which can be filled by activating the agreement’s provisional application. An important example of this is seen in the EU-Canada Comprehensive Economic and Trade Agreement (CETA) which, despite provisionally entering into force in September 2017, is still undergoing formal ratification.

The matters listed in Article 4 are not the only reasons for a ‘mixed agreement’. Member states can also request ‘mixed agreements’ for political reasons, if there are ‘significant social and economic implications’ and thus the expectation of debate and controversy.

When the negotiation of the EU-Singapore trade deal began to stall, there was still need for greater clarity over what ‘exclusive competence’ means in a practical sense. This led the Commission to request the Opinion of the European Court of Justice (ECJ). The ECJ acknowledged that large parts of the Singapore deal could indeed fall under exclusive competence.

This ruling could be useful for a fast EU/UK FTA. The Council even noted the possibility that, in the future, the Commission could simultaneously draft negotiating directives for FTAs covering exclusive EU competence and mixed competence.
How does the EU negotiate trade deals?
Roles and responsibilities

1. European Commission
   The Commission acts as the EU executive or ‘civil service’. It prepares, negotiates and proposes the EU’s trade agreements.

2. Council of the European Union
   The Council acts as the EU national government. The Council decides (jointly with the European Parliament) whether to approve the proposed EU trade agreements.

3. European Parliament
   The Parliament is composed of publicly-elected MEPs. These representatives work jointly with the Council to decide whether to approve the proposed EU trade agreements.
Strategy in a politically uncertain environment
EU journey to a trade deal

01 Preparing
The Commission
• Analyses a deal’s likely impact
• Consults the public
• Sets out areas to negotiate
• Requests Council authorising
The Council
• Adopts a decision authorising negotiations

02 Negotiating
Trade talks are arranged by Chief Negotiators on both sides
Commission reports to Council and Parliament after each round (and publishes texts online)
Council and Parliament consult their trade committees
At close of negotiations, Commission distributes final texts to Council, Parliament and online

05 Decision-making
Council and Parliament jointly decide whether to approve agreement
If approved, Commission immediately proceeds with signing
After both sides sign, Council examines conclusion proposal and sends agreement to Parliament for consent
Parliament’s trade committee develops a report (and holds a vote on the agreement)
Following the committee’s ‘formal advice’, Parliament then votes on whether to consent

06 Signing
Full application (‘Non-mixed’ EU only responsibility)
If Parliament consents, EU waits for partner country to also ratify the agreement

Provisional application (‘Mixed’ responsibility between EU institutions and individual countries)
If Parliament consents, EU then requires ratification of all EU member states, using their own procedures
Partner country also ratifies the agreement
03 **Finalising**
Commission and Council lawyers review and format text
The final text is signed by Chief Negotiators on either side to signal end of negotiations

04 **Signing**
Commission drafts proposals for Council decisions on the agreement and translates these into all EU languages
Proposals are checked by Commission departments
The Commission adopts the proposals and formally asks for EU signature

07 **Entry into force**
Once both parties notify the depositaries (formal keepers of the agreement texts) of ratification, the agreement enters into force
Strategy in a politically uncertain environment
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