



THE
INVESTMENT
ASSOCIATION

BEYOND BREXIT

A NEW PARTNERSHIP WITH THE EU FOR
THE ASSET MANAGEMENT INDUSTRY

June 2018





ABOUT THE IA

The Investment Association (IA) champions the UK-based asset management industry, helping savers access investment services, businesses secure capital and ensure infrastructure and social housing projects obtain finance across Europe.

Our 240 members range from boutique UK firms, to large global players with pan-European footprints. Our members employ 93,500 people, and collectively manage £6.9 trillion of assets, £1.7 trillion of which is for European clients and funds.

Our members have £840 billion invested in shares, accounting for over one third of the UK market capitalisation. They hold £500 billion in corporate bonds, £160 billion in commercial property, and £29 billion in significant infrastructure.



CONTENTS

FOREWORD

OUR BREXIT PRIORITIES

1. REGULATORY COOPERATION AGREEMENTS **9**
2. A TRANSITIONAL ARRANGEMENT **13**
3. PRESERVING CHOICE FOR UK INVESTORS **15**
4. A COMPREHENSIVE FTA INCLUDING FINANCIAL SERVICES **18**
5. GRANDFATHERING OF CONTRACTS
AND DISPUTE RESOLUTION MECHANISMS **20**
6. A CLEAR ROAD MAP FOR ACCESS
TO EU THIRD COUNTRY REGIMES **22**

FOREWORD



ASSET MANAGEMENT SITS AT THE HEART OF THE MODERN ECONOMY AND IS THE CONDUIT THROUGH WHICH MONEY FLOWS FROM SAVERS AND INVESTORS TO BUSINESSES AND PROJECTS IN NEED OF FINANCE. AS PROVIDERS OF PATIENT CAPITAL, OUR MEMBERS HELP REDISTRIBUTE THE FRUITS OF ECONOMIC GROWTH, DRIVING UP PRODUCTIVITY AND LIFTING LIVING STANDARDS.

The UK is, by a significant margin, Europe's largest asset management centre, and the world's second largest after the US, with an international client base that is growing.

While the UK's growth as an asset management centre has been helped by advantages like time zone, language, and legal system, it is the UK's expertise and experience that is increasingly sought by clients from around the globe.

Our 240 members now manage £6.9 trillion in assets. £2.9 trillion is for overseas investors – £1.7 trillion of which is for European clients – providing the UK with an additional economic contribution in the form of export earnings, tax paid, and jobs created.

Building on this success and ensuring the UK remains a world leader for asset management is a goal we share with the UK Government. Yet as the Brexit negotiations are now well into their crucial second phase, key uncertainties remain about how firms in the UK will be able to serve their clients across the EU beyond 31 December 2020.

A deal that works for the asset management industry is one that will benefit savers and investors across Europe. The asset management industry has benefited considerably from access to the Single Market and its frameworks for services and products. Europe is the UK industry's most

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significant source of international customers, and it is deeply integrated with European markets at every level.

Any significant reconfiguring of this relationship will not just affect how savers will be able to access services, but how businesses secure the capital they need to grow, and vital infrastructure and social housing projects obtain finance right across Europe.

It is imperative that both sides come together and provide more certainty about the UK's future relationship with the EU. This includes ensuring financial services is included in a comprehensive FTA. This is essential to both protect the integrity of the UK's financial services cluster, and ensure millions across Europe continue to benefit from the UK's expertise, deep pools of liquidity, and access to international capital markets.

While no off-the-shelf model can fully replicate the close UK/EU relationship, a more ambitious agreement can be reached on the basis of mutual recognition, underpinned by close regulatory cooperation and alignment. This would be the most beneficial outcome for savers and investors across

Europe, and it would allow access to each other's markets while each side maintained the ability to set out the conditions for such access.

The IA supports the ambition for a broad and special partnership between the UK and the EU, but the time has come to make substantial progress towards this goal. For decades, the asset management industry across Europe has helped to contribute to our shared growth and prosperity. We firmly believe that with the right framework, it can continue to do so into the future.



Chris Cummings

Chief Executive

OUR BREXIT PRIORITIES

This document sets out our priorities for the Brexit negotiations, and our ambition for a new partnership between the UK and the EU.

1 Regulatory Cooperation Agreements

The FCA should enter into discussions with its EU27 counterparts as soon as possible about Regulatory Cooperation Agreements. This is to allow delegation arrangements to continue uninterrupted and avoid a 'cliff-edge' effect post-Brexit.

These could be held through the Joint Technical Working Group between the Bank of England and the European Central Bank, a standalone arrangement between the FCA and ESMA, or bilaterally between regulators themselves. These agreements must be ready to be signed by March 2019.

2 A transitional arrangement

Both sides should build on the political agreement reached in March and provide the legal basis for transition as soon as possible.

Regulators should also now make clear how they intend to give effect to the political agreement so firms can plan ahead with sufficient certainty.

3 Preserving choice for UK investors

The UK Government must ensure that EU27-domiciled funds marketed into the UK can be bought and held by UK investors post-Brexit. Investors need clarity on this through an early announcement for newly established EU27 domiciled funds, as has been done through the temporary permissions regime.

The UK Government should seek to maintain UCITS status for UK qualifying funds and management companies (ManCos) beyond transition, or provide grandfathering for existing UK funds and ManCos.



4 A comprehensive FTA including financial services

A comprehensive FTA must be agreed that includes financial services, ensuring firms can operate on a cross-border basis without interruption. To achieve this, the FTA should provide for market access on the basis of mutual recognition, underpinned by close regulatory cooperation.

5 Grandfathering of contracts and dispute resolution mechanisms

The UK Government should provide legal certainty beyond the transition period by introducing grandfathering provisions as part of the Withdrawal Agreement, or through a separate bilateral agreement.

It will be necessary to have an agreed dispute resolution mechanism in case disputes cannot be resolved through the relationship management structures created by the FTA.

6 A clear road map for access to EU third country regimes

The UK Government should seek as an interim transitional measure, pending agreement of an FTA, a road-map for access to the MiFID II and AIFMD third country passports to be implemented immediately on Brexit.

Addressing these issues will ensure the UK retains its status as a world-leading asset management center beyond Brexit.

Due regard will also need to be given to maintaining not just the individual sectors of the UK's financial services industry, but to the overall hub effect.

The UK Government will also need to safeguard the UK as an attractive place to do business. This includes maintaining access to talent, and facilitating the seamless transfer of data.

UK INDUSTRY STATISTICS

£ **6.9** TRILLION

[£5.7 TRILLION IN 2015]

TOTAL ASSETS MANAGED IN THE UK BY THE IA'S MEMBERS AS AT DECEMBER 2016

£ **1** TRILLION

[£928 BILLION IN 2015]

FUNDS HELD BY UK INVESTORS

£ **2.9** TRILLION

[£2.2 TRILLION IN 2015]

ASSETS MANAGED IN THE UK ON BEHALF OF OVERSEAS CLIENTS

£ **1.1** TRILLION

[£1 TRILLION IN 2015]

UK-MANAGED FUNDS DOMICILED OFFSHORE

34 PER CENT

[31 PER CENT IN 2015]

UK DOMESTIC MARKET CAPITALISATION ACCOUNTED FOR BY THE IA'S MEMBERS' UK EQUITY HOLDINGS

36 PER CENT
IN 2015

[37 PER CENT IN 2014]

TOTAL EUROPEAN ASSETS UNDER MANAGEMENT MANAGED IN THE UK AS AT DECEMBER 2015 (LATEST AVAILABLE).

Source: The Investment Association - Asset Management Survey (2016/17) and additional analysis.

1 REGULATORY COOPERATION AGREEMENTS

The scale of portfolio management activity currently undertaken in the UK under delegation reflects important choices made by international firms to locate operations in the UK; and by their clients wanting to leverage that global expertise to secure the best possible returns on their investments.

- *Delegation is a global convention that allows investors to access the best portfolio management expertise, whilst enjoying high standards of protection and regulatory oversight. For example, it allows a saver in the US, in a UCITS fund registered in Luxembourg focusing on Asian equities, to benefit from the local insight of managers based in Tokyo.*

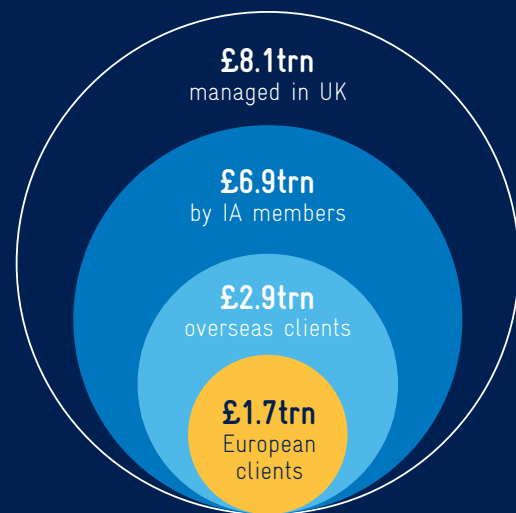
Specifically, delegation allows firms to utilise specialist staff and supporting infrastructure, wherever it is located, to the benefit of savers. These economies of scale provide investors with affordable access to the market, while ensuring they are protected by the EU's strict regulatory protections and oversight.

The high investor protection standards, diversification of international investment opportunities, and the wide range of investment expertise available via delegation have been the key factors for the success of UCITS, and it is in the interests of both sides to allow this global norm to continue benefitting investors across Europe post-Brexit.

Delegation to the UK

Both EU and UK investors reach out to UK managers for investment expertise. These include individuals, institutions such as pension funds or insurers, and corporates. They do this directly, by appointing a UK manager (a MiFID firm) to manage assets in a segregated mandate, or indirectly by investing in a UCITS or AIF that then delegates to a UK manager (again a MiFID firm).

STRUCTURE OF ASSETS MANAGED IN THE UK

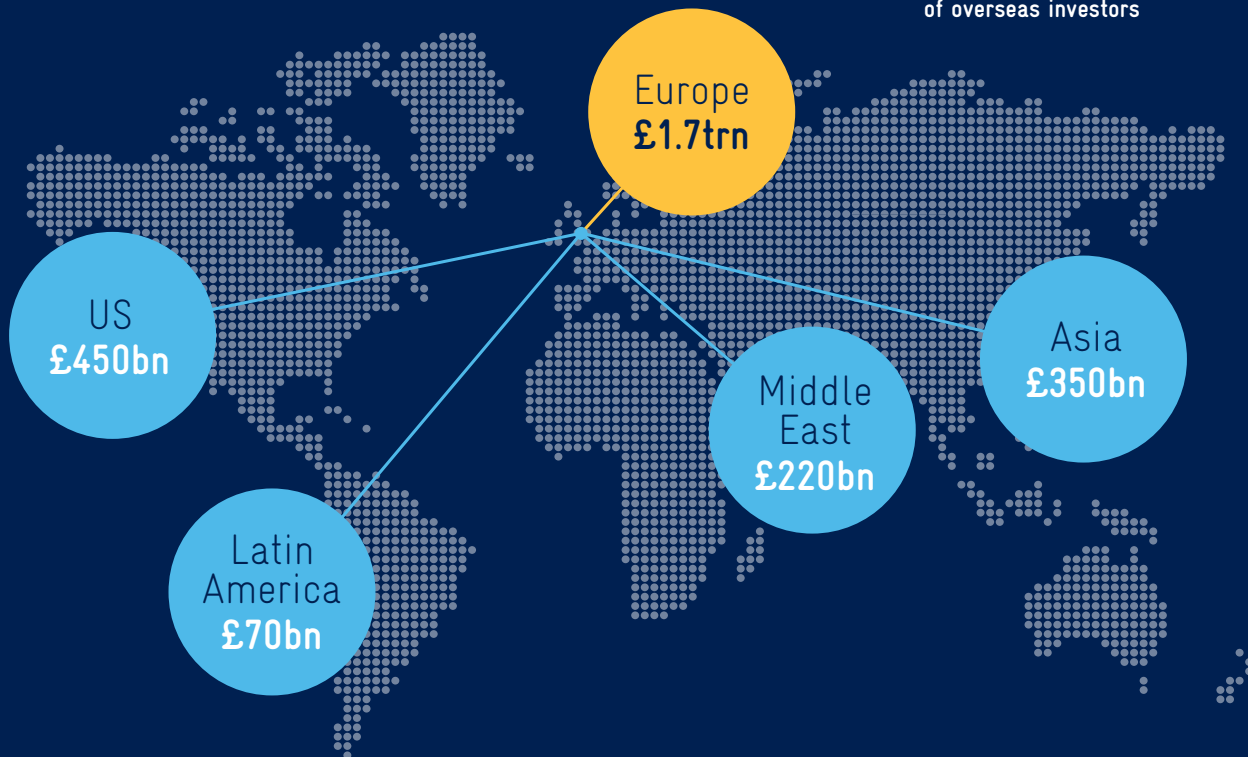


Source: The Investment Association – Asset Management Survey (2016/17) and additional analysis.

ASSETS MANAGED BY OUR MEMBERS IN THE UK

>> £2.9trn

managed in the UK on behalf
of overseas investors



Source: The Investment Association – Asset Management Survey (2016/17) and additional analysis.

There are two forms of access to portfolio management expertise. The first connection (the EU investor's direct appointment of a UK manager) falls within scope of Brexit. The UK manager must be permitted to 'passport' its services into the EU under MiFID rules in order to accept the investor's mandate.

The second connection (the investor's purchase of units in a UCITS or AIF that delegates to a UK manager) does not. UCITS and AIFs have always been free to delegate outside the EU. Indeed, delegation was a fundamental part of UCITS' original design, and has been key to its success over the last 30 years.

The role of regulators

In either scenario, the relevant EU27 Member State regulator directly oversees the entity contracting this service, as well as the delegation agreement. The decision to allow delegation is made on a case-by-case basis and can be rescinded at any time.

The decision as to whether certain functions can be delegated is subject to the regulator first being satisfied that strict conditions have been met (such as those relating to risk management), and that appropriate measures are in place to enable close regulatory cooperation and supervision.

The need for Regulatory Cooperation Agreements

For firms carrying out delegated activity from a non-EU 'third-country', this means a bilateral Regulatory Cooperation Agreement must be in place between the regulator where the delegated business is to take place, and the EU national regulator where the fund is registered, or client is located.

Like regulators in other non-EU countries, the UK's Financial Conduct Authority (FCA) needs to enter into bilateral Regulatory Cooperation Agreements with its counterparts in the EU27 Member States, such as the Central Bank of Ireland and the CSSF in Luxembourg, to allow delegation to continue to the UK post-Brexit.

Without these agreements, when the UK leaves the EU, there will be no legal basis to allow functions such as portfolio management to continue being carried out by firms in the UK on behalf of EU UCITS and AIFs, or from an EU client.

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Those firms based in the UK that rely on delegation will need to relocate these activities to entities in other jurisdictions where delegation is permitted, such as the US, Singapore, or Hong Kong, or risk being in regulatory breach.

Firms need a clear sign from authorities

Given the importance of delegation to the industry, it is essential that both sides work on agreeing Regulatory Cooperation Agreements as soon as possible and clearly communicate how and when these agreements will be negotiated before March 2019. This is both to ensure a well-regulated and supervised market continues post-Brexit, and to provide firms with the certainty they need to plan.

These discussions need to start urgently – either through the Joint Technical Working Group between the Bank of England and the European Central Bank, between the FCA and ESMA in a coordinating role on behalf of individual regulators, or directly between regulators themselves. The agreements should be ready to be signed before March 2019.

Our priority:

The FCA should enter into discussions with its EU27 counterparts as soon as possible about Regulatory Cooperation Agreements. This is to allow delegation arrangements to continue uninterrupted and avoid a ‘cliff-edge’ effect post-Brexit.

These could be held through the Joint Technical Working Group between the Bank of England and the European Central Bank, a standalone arrangement between the FCA and ESMA, or bilaterally between regulators themselves. These agreements must be ready to be signed by March 2019.

2 A TRANSITIONAL ARRANGEMENT

With the importance of transition now settled at the political level, attention must turn to the legal implementation of the agreement reached in March, how firms will be expected to operate within this new framework and how regulators will give effect to the agreement.

The need for a legal basis for transition

Firms cannot assume current market access arrangements will continue beyond March 2019. Despite political agreement on transition, this currently has no legal basis. More immediately, should a no deal Brexit scenario unfold, they would be at risk of regulatory breach and significant business disruption if they do not take steps soon to ensure they can continue serving savers and investors across Europe.

• *For those that have already activated contingency plans, early clarity about the legal basis for transition would enable them to pause or minimise those plans. For others, it may help them to avoid taking unnecessary and costly contingency measures entirely.*

Key unknowns remain on transition

In addition to uncertainty regarding the legal basis for transition, firms are also seeking clarity regarding market access after the end of 2020. In particular, firms are still faced with two key unknowns:

- » What concepts a future trading relationship between the UK and the EU might be based upon, after 31 December 2020.
- » What might happen between the end of the transition arrangement and the future agreement on trade and services, in particular the legal basis in the intervening period allowing services to be provided.

The priority must be turning the political agreement into a legally binding agreement – one that preserves existing market access mechanisms until December 2020, as well as the supporting elements that allow the industry to function such as movement of professionals, the cross-border transfer of personal data, and access to market infrastructure such as clearing institutions.

Duration of a transitional arrangement

While member firms are used to planning for multiple contingencies, the political and regulatory uncertainty surrounding Brexit negotiations is making it more difficult to plan for the longer-term.

Across the industry, there is no uniform 'cut off' date as to when a final decision on contingency plans need to have been made. Such a decision is dependent on a firm's footprint within the EU27, the location of the clients they serve, and the business model it operates.

Although the political agreement reached in March indicates the transition will run until December 2020, it is important to remember that any transition will need to allow two things:

- » Sufficient time to negotiate and then ratify the final agreement setting out the future relationship between the UK and the EU.
- » Sufficient time for firms to adapt to the new regulatory environment set out in an agreement before it takes effect.

The duration of a transition will depend on the scope of the final agreement reached with the EU. In a highly regulated sector such as asset management, the effects from substantial regulatory change would likely require a longer period to implement than for other sectors.

Our priority:

Both sides should build on the political agreement reached in March and provide the legal basis for transition as soon as possible.

Regulators should also now make clear how they intend to give effect to the political agreement so firms can plan ahead with sufficient certainty.



3 PRESERVING CHOICE FOR UK INVESTORS

A global success story

Every day, investors across the UK use EU27 domiciled funds to access international investment opportunities. It is critical that when the UK leaves the EU, investors continue to be able to access these funds and firms can market these funds into the UK.

UCITS are collective investment schemes established and authorised under a harmonised EU legal framework. The UCITS directive provides a marketing passport for any fund established within the EU that qualifies. This enables it to be marketed in any other EU Member State, following a notification between regulators.

The IA welcomes the commitment by the UK Government in its Investment Management Strategy II that in the future UK asset managers will be able to establish a fund structure based on UCITS in the UK. This means that the asset management industry will be able to continue to provide their services underpinned by a globally-renowned regulatory framework that ensures high levels of investor safeguards.

The challenge

Unless a separate agreement is reached as part of a future FTA allowing passporting of funds between the UK and the EU, UK-based UCITS management

companies (Mancos) that are currently responsible for marketing and distributing UCITS funds throughout Europe will no longer benefit from existing authorisations and will lose their EU passports. This means that they will not be able to manage or market EU27 UCITS funds.

Critically, UK funds currently granted UCITS status will no longer be able to be marketed to retail investors in the EU27 Member States and UK investors will also not be able to access EU27 UCITS funds. In particular, UK investors will be denied access to specialist fund ranges such as Exchange Traded Funds (ETFs) and Money Market Funds (MMFs).

This would limit investors' choice, together with their ability to diversify their portfolios. The EU would lose its ability to market its funds to a UK market, worth over £375 billion.

A temporary permissions regime

The IA welcomed the FCA's announcement in December that the UK Government is prepared to legislate for a Temporary Permissions Regime to apply in the UK should the UK and the EU be unable to reach agreement on Withdrawal and Transition by March 2019.

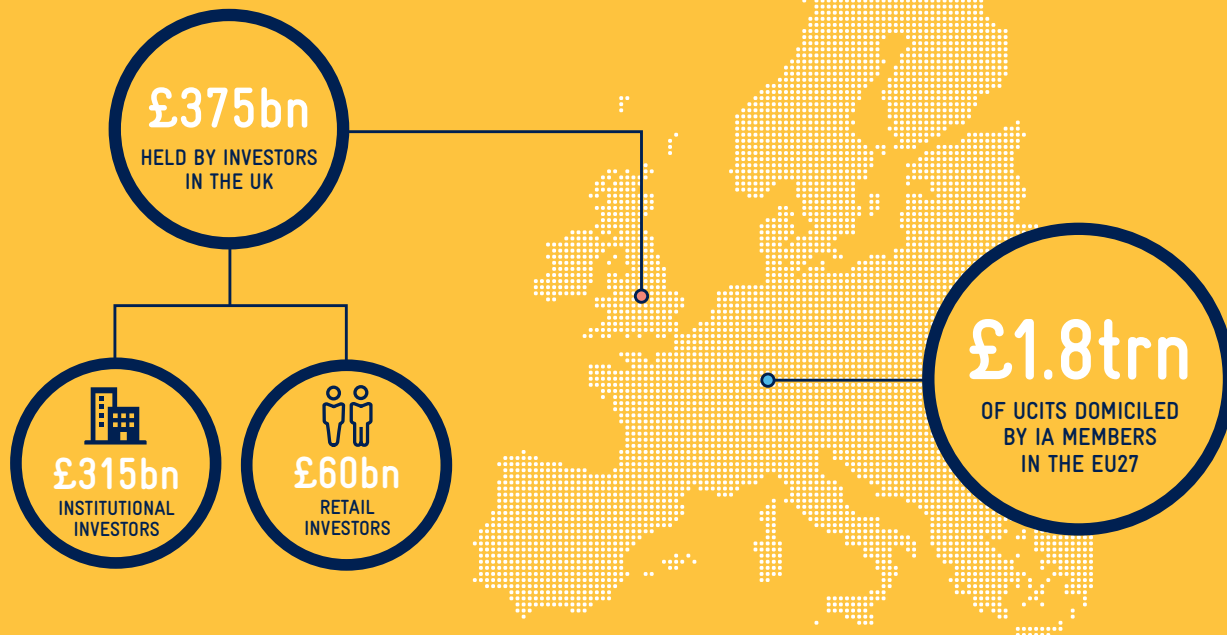
This legislation would allow firms based in the EU27, or funds domiciled in the EU27, to still be accessed by UK investors. It would enable these firms to undertake business within the scope of their existing permissions and enable them to continue meeting their contractual rights and obligations, manage existing business, and mitigate risks associated with any sudden loss of permissions.

A solution for new funds and entities

The ability of businesses to have confidence that they can continue to operate as usual post-March 2019 is crucial to the stability of the funds industry.

The confirmation that the UK is prepared to roll out a temporary permissions regime in respect of funds launched before Brexit is an important step forward.

FUNDS ESTABLISHED IN THE EU27 BY OUR MEMBERS AND THEN MARKETED AND SOLD TO UK INVESTORS



Source: The Investment Association – Asset Management Survey (2016/17)

However, it is not yet clear whether new EU27 UCITS funds established during or after any temporary permissions period would be able to be marketed into the UK post-Brexit.

Investors need reassurance from the EU27 concerning the status of UK UCITS funds and ManCos. The loss of UCITS status for UK funds, and the need to establish new Mancos in the EU without the ability to delegate portfolio management back to the UK would be disruptive for firms, as well as for investors that currently use these funds.

Towards a new fund regime post-Brexit

If a temporary permissions regime is required, the UK Government should ensure that applications to the scheme (and any successor regime to s.264 of the FSMA) can be made as efficiently as possible. The FCA should ensure that registrations could be made at umbrella level, as well as at a sub-fund level to help streamline the process and accommodate possible new funds in the future.

We would advocate a graduated approach to retaining mutual access:

- » Preserve existing UCITS passporting rights for UK funds;
- » UCITS already held by UK investors should be 'grandfathered' over at Brexit – UK authorities have already signalled they are willing to do so. The EU authorities should signal the same

in order to avoid investors on both sides of the Channel being forced to disinvest in products already held;

- » UCITS marketed to UK investors after Brexit – and UK funds marketed vice versa – should be granted free market access as long as there is a level of material regulatory convergence between EU and UK regimes;

If standards begin to materially diverge then the EU and UK should consider 'mutual fund recognition'. Such recognition should be relatively easy to agree given the common regulatory origin of UCITS and UK funds.

Our priority:

The UK Government must ensure that EU27-domiciled funds marketed into the UK can be bought and held by UK investors post-Brexit. Investors need clarity on this through an early announcement for newly established EU27 domiciled funds, as has been done through the temporary permissions regime.

The UK Government should seek to maintain UCITS status for UK qualifying funds and management companies (ManCos) beyond transition, or provide grandfathering for existing UK funds and ManCos.

4 A COMPREHENSIVE FTA INCLUDING FINANCIAL SERVICES

The UK's departure from the EU will transform the provision of asset management across Europe, with future access to the Single Market based on different political and legal terms. For UK-based firms providing services under passport, Brexit represents a significant and disruptive challenge.

We wish to see a comprehensive FTA agreed that is beneficial to both the UK and the EU. A deal that works for our industry is one that will also work for the millions across Europe who depend on our services every day. By including financial services in an FTA, the UK's financial services cluster can be maintained, and disruption to the wider European economy avoided.

Market access based on mutual recognition

No off-the-shelf model can fully replicate the close relationship that already exists between the UK and the EU. While the Transatlantic Trade and Investment Partnership (TTIP) and EU-Canada Comprehensive Economic and Trade Agreement (CETA) provide useful starting points for how services could be included within an FTA, as the basis for a longer-term relationship the UK should aim for a bolder and more ambitious agreement based on the concept of mutual recognition, underpinned by close regulatory cooperation.

The UK and the EU should take steps beyond the commitments made in existing FTAs and agree on a regime for mutual access without the need for additional authorisations to provide frictionless, cost-efficient access for financial services to each other's markets.

An FTA between the UK and the EU should ensure asset management services can be provided using all four of the 'modes of supply'. An FTA will also require a 'Prudential Carve Out', but its scope should be limited to reduce it being used to reduce future access, including introducing procedural restrictions on its operation.

FTAs can be created either on the basis of a 'positive list' or a 'negative list'. A negative list basis is when all sectors or sub-sectors that are not listed with reservations are, by default, open. The Canadian treaty is the first trade agreement where the EU has agreed to use a negative list. The negative list approach is appropriate considering the existing degree of market openness associated with the starting point of an EU-UK FTA.





Managing developments in regulatory regimes

The ability to access each other's markets will need to be based on maintaining the same regulatory outcomes, supported by a mechanism for determining proportionate consequences where they are not maintained. However, given the highly regulated nature of the industry, this would need a collaborative and objective framework that met the needs of the industry.

This could be achieved via a joint regulatory forum. The International Regulatory Strategy Group (IRSG) proposed such a forum to enable regulators to share information, proactively engage in the development of new laws and regulations (or the consistent implementation of global standards), and formally monitor divergence.

Further consideration should be given to extending such an arrangement to not just the UK and the remaining EU27 Member States, but to include other European Economic Area (EEA) states that rely on similar access to the Single Market.

Guided by international standards

Future market access should be mutually agreed, as many international firms that choose the UK as a place to do business are making use of passporting rights to provide services from other EU Member States into the UK.

Clear and transparent criteria should provide the basis for access to markets. Where existing global standards offer sufficient detail, the criteria should be based on those standards. Where there are no existing global standards, the relevant criteria should be based on the outcomes which the relevant regimes achieve.

Our priority:

A comprehensive FTA must be agreed that includes financial services, ensuring firms can operate on a cross-border basis without interruption. To achieve this, the FTA should provide for market access on the basis of mutual recognition, underpinned by close regulatory cooperation.

5 GRANDFATHERING OF CONTRACTS AND DISPUTE RESOLUTION MECHANISMS

When the UK leaves the EU, it may not be possible to service many medium and long-term existing cross-border contracts. Without an agreement that these contracts will continue to be serviced and honoured, the legal uncertainty may severely disrupt financial arrangements of UK and EU savers and investors.

Contractual certainty

Given the strong links between UK and EU markets, many existing contracts will extend beyond March 2019, and even beyond the end of transitional period in December 2020. This includes contracts between asset owners and managers, as well as between firms and the underlying providers of the market infrastructure.

Legal certainty would also help to ease clients' concerns about the need for repapering or the need for new, costly contracts. If a grandfathering provision was not included in a transition arrangement, existing contracts could be subject to legal uncertainty which would seriously disrupt business. This means that new contracts must be negotiated, which is a costly exercise for asset managers and their clients.

Dispute resolution mechanisms

It will be necessary to have an agreed dispute resolution mechanism in case disputes cannot be resolved through the relationship management structures created by the FTA.

For investors, options for dispute resolution currently include either:

- » Investor-State Dispute Settlement (ISDS) with its arbitration clause, like the one found in most bilateral investment treaties. While ISDS has had a mixed reception in the EU, the UK should not rule it out because an ISDS clause is a requirement for FTAs with countries like Japan and the United States.
- » An Investment Court System (ICS) like the one used by the EU's Canada and Vietnam treaties. ICS would be public, not based on temporary tribunals and have professional and independent judges chosen by the EU and its FTA partner. While the court is currently an untested innovation, its inclusion is a precedent showing that the EU can agree to be bound by third party determination.

However, along with portfolio investment (considered to be investments of less than 10%), dispute resolution is deemed by the CJEU to be a competence shared by the EU with its Member States – an approval process threatened by national and regional vetoes as well as gaining EU approval itself.

The alternative is to fast-track a treaty by excluding dispute resolution and portfolio investment. The absence of these provisions would both be an obstacle to developing a comprehensive EU investment policy and would not be beneficial for investors. The UK should not treat their possible absence as a precedent for the development of its future, independent trade policy.

Our priority:

The UK Government should provide legal certainty beyond the transition period by introducing grandfathering provisions as part of the Withdrawal Agreement, or through a separate bilateral agreement.

It will be necessary to have an agreed dispute resolution mechanism in case disputes cannot be resolved through the relationship management structures created by the FTA.



In the absence of an over-arching, one size fits all solution each contract will need to be individually assessed to determine if elements to be performed constitute a regulated activity no longer authorised under the EU passport rights currently enjoyed by UK firms.



6 A CLEAR ROAD MAP FOR ACCESS TO EU THIRD COUNTRY REGIMES

In the event of a no deal Brexit, the UK will need to rely on the EU's third country regimes to access European markets after Brexit. This includes both under MiFID II, as well as AIFMD. There is no third country regime for UCITS.

- *Given their limited coverage, the uncertainty of availability and the lack of crucial business safeguards, the EU's third country regimes are not sufficiently robust to allow the whole of the UK's financial services sector cross-border access post-Brexit.*

Relying on equivalence for market access

Equivalence facilitates cross-border trading between markets that recognise one another's regulatory standards. A determination by the European Commission as to whether the UK's regulatory regime is 'equivalent', however, would still need to be made upon Brexit, despite the UK's previous adherence to EU regulatory frameworks.

An initial equivalence determination could take several years to be made, and can be rescinded with just 30-days' notice. Additionally, not all EU financial legislation accepts equivalence. There is, for instance, no provision for commercial banking or primary insurance. These gaps would need to be covered to be a credible option for the wider financial services industry in the UK.

Equivalence as a possible intermediate step

Timely access to third country MiFID II and AIFMD passports could help mitigate some of the immediate transitional disruption arising from a 'no deal' Brexit. However, there are some limitations associated with a third country passport, namely the range of clients an asset manager would be able to serve, and the additional regulatory and legal complexity associated with such an approach at a national Member State level.

Beyond passporting and third country regimes

If neither passporting nor the third country regimes are available in relation to regulated asset management activity, and no bespoke agreement can be secured, it is likely that UK-based financial services firms would have only limited options available to them after Brexit to continue serving their European clients. The main options would be to:

- » Carry on cross-border activities that are permitted under local laws, including National Private Placement Regimes for AIFs.
- » Establish a subsidiary in the EU and apply for it to be authorised by the local regulator.
- » Apply to the individual EU Member States for direct authorisation of a branch.

MIFID II THIRD COUNTRY PASSPORTS

CROSS-BORDER SERVICES

Third country asset manager providing services in one EU Member State

Prerequisite: European Commission confirms equivalence

EU-MARKET ACCESS

CUSTOMER ACCESS

Limited

- ✓ Eligible counterparties
- ✓ Professional clients
- ✗ Retail clients

BRANCH

Third country asset manager providing services in one EU Member State via registered branch

Various admission requirements: Intergovernmental, legal, and company level

Full

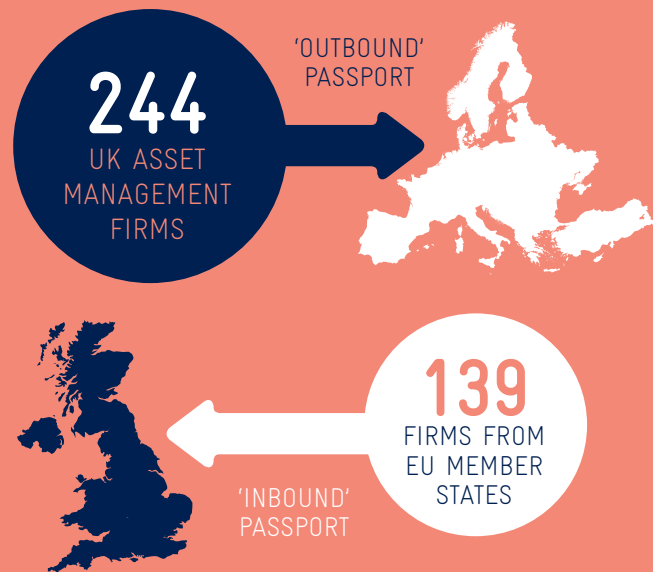
- ✓ Eligible counterparties
- ✓ Professional clients
- ✓ Retail clients

Some EU Member States permit cross-border provision of services, including EU Member States where UK asset managers have a focus (e.g. Luxembourg, Ireland, Netherlands, Germany, Finland, and Sweden). However, access is complicated by the need to understand local interpretations in the implementation of regulation.

Our priority:

The UK Government should seek as an interim transitional measure, pending agreement of an FTA, a clear road-map for access to the MiFID II and AIFMD third country passports to be implemented immediately on Brexit.

THE PASSPORTING REGIME HAS ENABLED ASSET MANAGERS TO CONDUCT REGULATED ACTIVITY IN EACH OTHER'S MARKETS



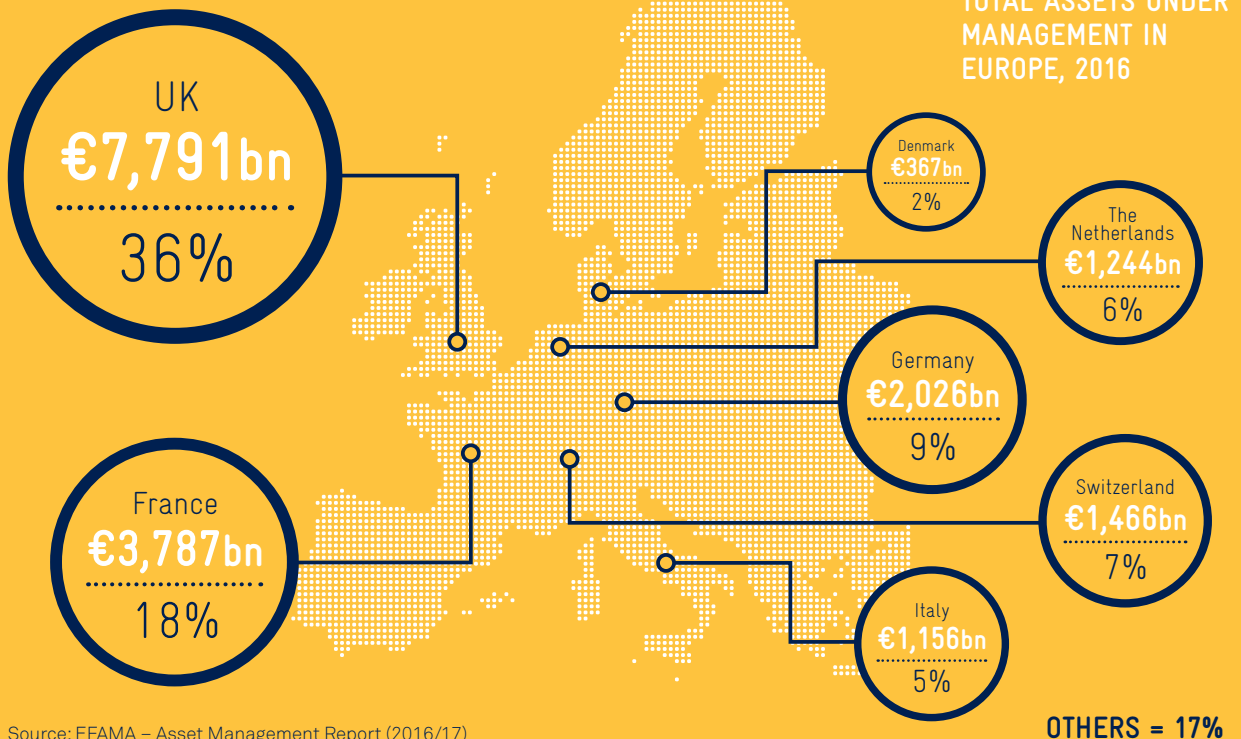
Europe Economics (2016) "FCA's Market Study and Brexit: Next Challenges for the UK Asset Management Industry".

THE EU'S LARGEST ASSET MANAGEMENT CENTRE

The UK is – by a significant margin – Europe's largest asset management centre. Of the estimated €21.5 trillion of total assets under management in Europe at the end of 2016, 36% of

this was managed in the UK, compared to 17.6% in France and 9.4% in Germany (the next two largest centres for asset management in Europe).

ASSETS UNDER MANAGEMENT IN EUROPE (MARKET SHARE, %)



Source: EFAMA – Asset Management Report (2016/17)

AN INDUSTRY THAT RELIES ON GLOBAL TALENT

The strength of the asset management industry is based on its ability to access the right skillsets from around the world. Of the 93,500 people employed across our industry, 1 in 5 are international workers, and 1 in 10 are European nationals.

With record employment rates in the UK, without access to EU workers, firms may not be able to get the talent they need to grow operations in the UK.

- *The UK Government will need to consider how it will maintain access to the highly skilled and specialist workers that our industry depends.*
- *Appropriate mechanisms will need to be in place prior to the UK's departure from the EU to promote a domestic talent pipeline, as well as which meet the industry needs to recruit from an international pool of talent.*

Labour mobility scheme in an FTA

The IA supports the UK Government's ambition for a labour mobility scheme to be included within a future FTA with the EU.

Such an arrangement would allow British workers to gain experience around Europe, and help firms with offices across Europe in the allocation of appropriate technical expertise and specialist skills according to their business needs. It would also provide firms the flexibility they need to adapt to changing market and operational demands.



Source: Analysis of IA data.

DATA PROTECTION AND INFORMATION SHARING



The free flow of data is critical in enabling the efficient functioning of the wider economy. From completing trades to conducting research and market analysis, the industry relies extensively on being able to seamlessly transfer personal information and share data cross-border.

Following the UK's departure from the EU, the UK will become a third country with the EU's General Data Protection Regulation (GDPR) prohibiting the transfer of personal data from the EU to the

UK. To be able to transfer personal data cross-border post Brexit, the European Commission will need to determine that the UK's data protection arrangements are adequate.

- *Negotiations between the UK and the EU should seek to secure an agreement that allows firms to be able to transfer personal data cross-border post-Brexit. The UK Government should seek from the European Commission a determination that the UK's data protection arrangements are adequate.*

Every day across Europe's financial markets, nearly 100 million new data points are created, the majority of which stem from the UK.



Under GDPR, securing an adequacy determination would not require a point-to-point replication of EU rules by the UK. Instead, the test would lie in whether the UK delivered the required high levels of protection for personal information.

- *Currently, Andorra, Argentina, Canada (commercial organisations), Faroe Islands, Guernsey, Israel, Isle of Man, Jersey, New Zealand, Switzerland, Uruguay and the US are recognised as providing adequate protection under GDPR to allow the transfer of personal data and information.*



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