

Brexit: our approach to EU non-legislative materials

The purpose of this guidance

1. This guidance sets out the FCA's approach to non-legislative material produced by the EU and, in particular, the European Supervisory Authorities (ESAs).
2. This guidance is relevant to firms, financial institutions and other market participants operating, or intending to operate, in the United Kingdom.

What are non-legislative materials?

3. The European Supervisory Authorities (ESAs) were established in 2011 to strengthen the coordination between national regulators of financial markets within the European Union (EU) and ensure the consistent application of EU financial legislation. They have the power to produce non-legislative-material, either individually or through their Joint Committee. This includes Guidelines and Recommendations on the application of EU law, 'Questions & Answers' documents and Opinions. Similar material was also produced by other EU bodies in the past, including the ESAs' predecessors¹ and, in some instances, adopted by the ESAs.

ESA Guidelines and Recommendations

4. Each of the three ESAs – the European Securities & Markets Authority (ESMA), the European Insurance & Occupational Pensions Authority (EIOPA) and the European Banking Authority (EBA) - has the power to issue non-legally binding 'Guidelines and Recommendations' ('Guidelines') under their respective ESA Regulations as tools to promote the consistent application of EU law across jurisdictions.
5. These Guidelines are directed to competent authorities, financial market participants and financial institutions.² Competent authorities, and in some circumstances other market participants, notify the relevant ESA(s) of their intention to comply, or explain why they do not propose to comply. This is commonly called the 'comply or explain' process, under which the addressees are expected to 'make every effort to comply' with the Guidelines.
6. The ESAs maintain a record of Guidelines published and corresponding 'comply and explain' responses by the competent authorities, including those of the FCA.

¹ The Committee of European Securities Regulators, the Committee of European Banking Supervisors and the Committee of European Insurance and Occupational Pensions Supervisors.

² For ease of reference the rest of this guidance refers simply to 'financial market participants' or 'market participants'.

Other EU non-legislative material

7. The ESAs also publish other non-legislative material which includes:

- Opinions
- 'Questions & Answers' documents
- supervisory briefings
- peer-review analyses
- best practices and statements to help build a common supervisory culture and consistent supervisory practices within the EU
- warnings (e.g. around the risks associated with particular complex products).

What is happening to non-legislative EU material in the UK post-exit?

8. Under the EU (Withdrawal) Act 2018 (EUWA), the broad range of non-legislative material produced by the ESAs or their predecessor bodies (for example, CESR) has not been incorporated into UK law. However, the EU-derived law to which the non-legislative material relates has largely been retained. Therefore, we consider that the EU non-legislative material will remain relevant post-exit day to the FCA and market participants in their compliance with regulatory requirements, including provisions in our Handbook.

What is the FCA's expectation in relation to the application of pre-exit EU non-binding material?

ESA Guidelines and Recommendations

9. Our supervisory expectation in respect of Guidelines and Recommendations remains the same. Persons requiring authorisation or recognition to continue to provide services in the UK post-exit day will become subject to these expectations.

10. In particular:

- i. we expect firms and market participants to continue to apply the Guidelines to the extent that they remain relevant, as they did before exit-day, interpreting them in light of the UK's withdrawal from the EU and the associated legislative changes that are being made to ensure the regulatory framework operates appropriately
- ii. we shall continue to apply such Guidelines and Recommendations in respect of our own functions in the same manner as before, interpreting them in light of the UK's withdrawal from the EU and the associated legislative changes.

Other EU non-legislative material

11. We will continue to have regard to other EU non-legislative material where and if they are relevant, taking account of Brexit and ongoing domestic legislation. Firms, market participants and stakeholders should also continue to do so.

Are there any exceptions to our expectations to non-legislative EU material?

12. Where we have previously informed the relevant ESA that we will not comply with part of, or all of, a pre-exit Guideline we will continue this approach. For example, we have notified that we would not comply with parts of the Guidelines in the cases listed below. In those circumstances, we explained our reasons for why it would not be appropriate to comply with all or part of the guidelines and the legal consequences of the refusal to comply. For example:
- i. ESMA's short-selling guidelines: We notified ESMA that we would comply with all the Guidelines with the exception of the provisions concerning the requirement to be a member of a trading venue (i.e. that a market maker be a member of a venue on which the instrument trades that it wishes to make markets in) and the scope of the products eligible for the exemption (i.e. that the market making exemption should not be limited to equities, sovereign debt and equity/sovereign debt derivatives).³ We expect stakeholders to continue applying the Guidelines, with the exception of those provisions.
 - ii. EBA's sound remuneration policies: We notified the EBA that we would comply with all aspects of these Guidelines, except for the requirement that the limit on awarding variable remuneration to 100% of fixed remuneration, or 200% with shareholder approval ('the bonus cap'), must be applied in any case to all firms subject to the Capital Requirements Directive.⁴
 - iii. EBA's internet payment security guidelines: We notified the EBA that, while fully supportive of the objectives behind the Guidelines, we did not have the power, without legislative change, to make binding rules requiring all payment service providers (credit institutions, payment institutions, and e-money institutions) to comply with the Guidelines. Implementation of the Guidelines would require some providers to make significant changes to their systems and controls, and significant additional changes would likely be necessary following implementation of the Payment Services Directive II. We noted that we indicated to participants that compliance with the Secure Pay Recommendations would be needed, in line with PSD2 transposition requirements.⁵
 - iv. The acquisition Directive Guidelines: We notified the ESAs that we would comply with the Guidelines except for provisions relating to the identification of acquirers of indirect holdings. We noted firms should continue to use the existing methodology as laid out in Part II. We will continue to comply with the Guidelines in this way and expect firms to do so as well.
13. We have also made changes to the application of EBA Guidelines relating to the applicable notional discount rate for variable remuneration, compared to the position prior to exit-day. Pre-exit, SYSC 19A/19D required firms applying the discount rate to apply the approach prescribed in the Guidelines. This creates deficiencies as the formula is dependent on figures published by Eurostat which may cease to be produced for the UK following EU withdrawal. Therefore, post-exit we expect firms to make every effort to comply with the Guidelines.

³ Please see our website after exit day

⁴ Please see our website after exit day

⁵ Please see our website after exit day

14. Post-exit day the FCA may determine that firms, financial institutions or market participants are no longer expected to 'make every effort to comply' with a particular pre-exit Guideline, for example, due to changes made to the relevant legislation. In those circumstances, this guidance will be updated accordingly.
15. Finally, we maintain our approach to the ESMA MIFID Q&A 'Appropriateness/Complex Financial Instruments'. The ESMA Q&A states that shares in non-UCITS collective investment undertakings explicitly excluded under point (i) of Article 25(4) of the MIFID II cannot be deemed non-complex financial instruments for the purposes of the appropriateness test. We stated in our MIFID 17/14 Policy Statement⁶ that *'in our view, investment trusts and non-UCITS retail schemes (NURS) are neither automatically non-complex nor automatically complex, but must be assessed against the criteria set out in the MiFID II delegated regulation'*. We also said that *'when firms apply these criteria, they should adopt a cautious approach if there is any doubt as to whether a financial instrument is non-complex. This remains our view of how this part of MiFID II should be interpreted, and how firms should apply these rules.'*

Post-exit non-legislative EU material

16. The FCA may consider materials produced by the ESAs post-exit, including where pre-exit material is updated. Where we consider it appropriate to do so, we will set out our expectations as to how it should be treated.

How to interpret non-legislative EU material

17. As a result of the UK's withdrawal from the EU, EU non-binding materials may include references which no longer have their intended effect (for example, references to legislation that may have been amended during the withdrawal process and may therefore no longer be correct). In these situations, we expect firms and other market participants to sensibly and purposively interpret EU non-binding material, taking into account the UK's withdrawal from the EU, the provisions of the Act and amendments made to relevant legislation in the withdrawal process, including the FCA Handbook.
18. Examples of where non-legislative EU material needs to be interpreted in line of the UK's withdrawal from the EU include:
 - a. References to passporting across the EU. References to passporting or associated processes have been deleted from UK legislation and are no longer relevant. References in non-legislative EU material to passporting and associated processes that have been deleted from legislation can be ignored.
 - b. References to reporting to the ESAs are redundant, as there are no longer requirements in UK legislation to report to the ESAs. References in non-legislative EU material to ESA reporting and associated processes can be interpreted in light of the amendments made to the relevant legislation.
 - c. References to any roles or responsibilities currently carried out by EU authorities. Those have, to the extent that they remain relevant, been reallocated to the most appropriate UK authority. Firms should interpret references to EU functions with reference to the new UK authority taking on that function. This may be the case, for example, for equivalence assessments and recognition of third-country jurisdictions for market access.

⁶ <https://www.fca.org.uk/publication/policy/ps17-14.pdf>