

GERMANY PREPARES FOR "NO DEAL BREXIT"

To prevent market disruption and negative implications for the financial markets in case of a "no deal Brexit", the German Ministry of Finance has published a draft law to preserve market access for UK firms offering banking business, financial services or insurance services in Germany under the European passport regime.

Amendments to the German Banking Act

BaFin may continue to apply the provisions for passported branches and cross-border services for a transitional period

Aiming for a swift and effective response to prevent market disruption, the draft law empowers the Federal Financial Supervisory Authority ("**BaFin**") to treat UK banks and investment firms currently providing banking and investment services under the European passport regime as if they continued to hold an EU passport post-Brexit. This transitional regime may be applied for a period of up to 21 months after the Brexit date, corresponding to the timeframe currently discussed between the UK and the EU to allow for an orderly transition. It is subject to the absence of a withdrawal agreement. According to the reasoning, BaFin's powers are subject to any regulation at European level taking precedence.

While the transitional period ensures contract continuity for existing financial transactions post-Brexit, transactions entered into after 29 March 2019 are only in scope if these transactions are closely connected to transactions that existed at the time of Brexit. The draft law does not define "close connection" and does not specifically address services provided on a continuing basis. However, based on the reasoning of the draft law, hedging of pre-Brexit transactions or certain life-cycle events would be in scope.

The draft law grants wide discretionary powers to BaFin when implementing the transitional regime. Hence, the draft law does not provide for a general automatic continuation of the use of the EU passport. However, in light of the purpose of the draft law to avoid any harm to the functioning or stability of financial markets, it seems likely that BaFin will issue a general decree (*Allgemeinverfügung*) applying the transitional period to passported UK institutions, as this would allow prompt and effective action in case of a "no deal Brexit". However, it remains to be seen whether BaFin will require the relevant institutions to notify BaFin of their intention to rely on the transitional

Summary

- BaFin may apply transitional period for providing certain banking/investment services in Germany
- Grandfathering regarding German covered bonds (*Pfandbriefe*) and building associations saving schemes
- Limits to dismissal protection for material risk takers

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measures in order to keep control over such institutions and the related transaction volumes.

According to the reasoning, the proposed law is without prejudice to the existing ability of BaFin to grant individual UK entities permission to provide banking or financial services on a cross-border basis beyond the Brexit date, for example as an interim measure until a regular licence as applicable to any third country institution operating in Germany is granted or to provide for an orderly unwinding of business operations in Germany.

Modifications of dismissal protection to facilitate the relocation of senior executives

In addition, the German Banking Act will be amended to limit dismissal protection for material risk takers as defined in the current Regulation on the Supervisory Requirements for Institutions' Remuneration Systems (*Institutsvergütungsverordnung*), treating them equivalent to senior executives (*leitende Angestellte*) entitled to self-employment or dismissal of employees. The adjustment applies only to material risk takers of major institutions that receive a fixed annual remuneration of currently at least €234,000 or approximately €208,000 (with respect to former Eastern Germany). For all other employees in the financial sector, the dismissal protection does not change.

Amendments to the Insurance Supervision Act

Possibility to grant a transitional arrangement to avoid any harm to policyholders and beneficiaries of insurance contracts

The proposed amendment to the Insurance Supervision Act (*Versicherungsaufsichtsgesetz*) will give BaFin the possibility to grant a transitional arrangement (including by way of general decree (*Allgemeinverfügung*)) for a period of 21 months after the Brexit date to protect insured persons and beneficiaries. The intention is to enable insurance companies based in the UK to transfer or terminate existing contracts within a reasonable timeframe to an insurance company within the EEA or to meet the necessary prudential requirements for an orderly run-off of such contracts.

Eligibility of UK based assets and guarantees

German real estate covered bonds (*Pfandbriefe*)

The German Ministry of Finance further proposes to grandfather claims secured by UK based real estate or claims against or guaranteed by the UK or UK based debtors or guarantors. Where such claims have been included in the coverage for existing German covered bonds (*Pfandbriefe*) prior to 30 March 2019, these assets continue to be eligible coverage post-Brexit.

Building associations saving schemes (*Bausparverträge*)

Similarly, UK real estate will remain eligible security for loans granted by German building societies (*Bausparkassen*) if in place prior to the Brexit date. In addition, the draft law provides that German building societies may continue to hold accounts with, or debt issued by, UK credit institutions established or acquired before 30 March 2019 until their maturity for the purposes of German building societies' saving schemes.

Next steps

Further to the comments by relevant associations and government entities, the consolidated draft will be introduced to the German parliament in due course.

Background information

The draft law can be downloaded under the following link:

- **German version (Amendments to German Banking Act and Insurance Supervision Act)**

https://www.bundesfinanzministerium.de/Content/DE/Gesetzestexte/Gesetze/Gesetzesvorhaben/Abteilungen/Abteilung_VII/19_Legislaturperiode/2018-11-20-Brexit/0-Gesetz.html

- **German version (Amendments to *inter alia* German Covered Bond Act (Pfandbriefgesetz))**

https://www.bundesfinanzministerium.de/Content/DE/Gesetzestexte/Gesetze/Gesetzesvorhaben/Abteilungen/Abteilung_IV/19_Legislaturperiode/Gesetze_V_erordnungen/Brexit-StBG/0-Gesetz.html

- **English version (Amendments to German Banking Act and Insurance Supervision Act)**

<https://www.bundesfinanzministerium.de/Content/EN/Gesetze/Laws/2018-Brexit-Gesetz-engl.html>

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