



ITALY PROVIDES FOR POST-BREXIT TEMPORARY REGIME

The Italian Council of Ministers has approved a new law decree creating an 18-month temporary regime for UK firms engaging in regulated business in Italy and Italian firms engaging in regulated business in the UK. The temporary regime will become effective, if there is a no-deal Brexit, on the day the UK leaves the EU (for convenience, the ‘exit date’). The new regime aims to mitigate the main ‘cliff-edge’ impacts and disruption that could have ensued under Italian law following the sudden loss of the EU passport rights in a no-deal Brexit.

Italy’s Brexit law decree, published in the Official Gazette last night, provides an 18-month breathing space from the exit date in a no-deal Brexit to UK firms that lose their ‘passport rights’ to do regulated business in Italy based on their UK licence. This temporary regime will apply across most regulated sectors, but with a few exceptions discussed below.

Firms qualifying for the temporary regime may, for 18 months, ‘continue to carry out the regulated services or activities’ in which they engaged before Brexit in much the same way as they used to before the exit date. There are, however, certain differences in the scope and modalities of the temporary regime based on the type of entity concerned, the type of regulated business, the way of doing business in Italy (via a local branch or cross-border) and the type of targeted clients.

Whenever the 18-month temporary regime is not available, a shorter ‘grace period’ (six months from the exit date) will be allowed to run- off the existing business, during which no new contracts with clients may be entered into.

1. UK Regulated Entities

1.1 Temporary regime

The multifaceted temporary regime under the Brexit law decree is best described using the following table, which summarises the scope, requirements and limits of the temporary regime for each category of UK- regulated entities. We discuss the treatment of Italian regulated entities below.

Temporary regime for UK-regulated entities doing business in Italy as of the exit date

	Step required to benefit from temporary regime	Activity permitted during temporary regime	
		Entities operating via branch	Entities operating cross-border
Banks providing banking/ financial services (including deposit takings and lending)	Notice to Bank of Italy at least three business days prior to exit date	Can 'continue to carry out the banking and financial services' that they used to carry out before exit date	Can 'continue to carry out the banking and financial services' that they used to carry out before exit date, <i>provided that</i> , with respect to deposit taking, they will only be permitted to 'service those relationships initiated prior to the exit date', 'without entering into any new contracts' ¹
Banks/investment firms providing investment services²	Notice to Bank of Italy (banks) or Consob (investment firms) at least three business days prior to exit date	Can 'continue to carry out the investment services' that they used to carry out before exit date	Can 'continue to carry out the investment services' that they used to carry out before exit date, but only with respect to MiFID-eligible counterparties, per se professional clients and – solely to manage life-cycle events of OTC non-cleared derivatives ³ – regions, independent provinces and public entities ⁴

¹ We take this to mean that also new deposits may be made by clients, as long as they are made in the context of already existing client relationships.

² Other than managing multilateral trading facilities (MTFs) or organised trading venues (OTFs), to which the regime described in the row relating to trading venues will apply.

³ And subject to limits set forth under Article 62 of the law decree No. 112 / 2008, outlining the currently applicable framework on derivatives for public entities.

⁴ This regime is meant to apply, in the 18-month period after exit date, 'until a decision is taken by the EU Commission under Article 47(1)' of MiFIR (Regulation (EU) No 600/2014). This is the decision by which the EU Commission would confirm, in relation to a third country (this would be the UK), that the legal and supervisory arrangements of that third country ensure that firms authorised in that third country comply with legally binding prudential and business conduct requirements equivalent to those in the EU. Third-country firms established in a country whose legal and supervisory framework has been recognised as equivalent to that in the EU ones would be able to provide investment services to eligible counterparties and per se professional clients in Member States of the EU without the establishment of local branches. Although the language in the law decree is not entirely clear on this point, we would presume that if such an equivalence decision is handed down by the EU Commission, the MiFIR regime described above in this footnote will take over, and apply in lieu of the temporary regime under the law decree (and so would potentially allow UK banks and investment firms providing investment services into Italy to continue to provide such services in such a way even beyond the end of the 18-month temporary period).

	Step required to benefit from temporary regime	Activity permitted during temporary regime	
		Entities operating via branch	Entities operating cross-border
E-money institutions	Notice to Bank of Italy at least three business days prior to exit date	Can continue to operate in Italy in the same ways as before exit date	Must cease to do business in Italy (no later than the end of the six-month grace period after exit date)
Payment institutions, asset managers, investment funds Banks / investment firms providing investment services cross-border to retail and opted up professional clients⁵	N/A	Must cease to do business in Italy (no later than the end of the six-month grace period after exit date, during which only existing contracts may be serviced, but without entering into new contracts)	
Trading venues	Submission, by the exit date, of an application to Bank of Italy (banks) or Consob (investment firms and markets) for authorisation, as the case may be, to manage multilateral trading facilities (MTFs) or organised trading venues (OTFs) to which access is intended to be granted to clients established in Italy, or for recognition in Italy of a non-EU market (in the case of markets)	Can continue to carry out activities in Italy, 'thus being able to continue to grant access to the trading venue to clients established in Italy that are members of the trading venue as of the exit date'	
Insurance undertakings	None	Can continue to carry out activities in Italy limited to the servicing of existing contracts and existing coverage, without entering into any new contracts or renewing existing ones	

⁵ The regime outlined in this row will also apply to banks and investment firms which would have been in a position to benefit from the 18-month temporary regime, notwithstanding that they failed to notify Bank of Italy / Consob in time of their intention to benefit from the temporary regime.

1.2 Steps required to benefit from the 18-month temporary regime

As mentioned in the table above, in order to benefit from the 18-month temporary regime, depending on the type of entity, prior notice to the relevant Italian regulator (Bank of Italy, or Consob) or filing the application to be authorised as a third country firm (or market) may be required

In particular, banks providing banking / financial services, banks or investment firms providing investment services and e-money institutions operating via a branch, must deliver the prior notice. This is expected to be a very simple notice⁶, informing the relevant regulator of the regulated entity's intention to benefit from the temporary regime. It will have to be drawn up in the form of the templates which will be published by Bank of Italy and Consob (these are not yet available as of the time of publication of this client briefing); and will have to be delivered to the addresses that will be specified by Bank of Italy and Consob.

As far as trading venues are concerned, as we have also noted in the table, in order to benefit from the temporary regime, UK banks or investment firms managing MTFs or OTFs, and managers of UK markets, in each case where clients established in Italy have access, must, by the exit date, submit their application to Bank of Italy (banks) or Consob (investment firms and markets) for authorisation, as the case may be, to manage MTFs or OTFs to which access is intended to be granted to clients established in Italy; or for recognition in Italy of a non- EU market (in the case of markets).

This is a full application, as opposed to a simple notice. It requires some substantive information, and documentation, to be provided, which will not be an easy exercise in the potentially short time available before exit date; however, the entities concerned may consider filing a preliminary application before the exit date, to then follow up with additional information, as needed, after the exit date.

1.3 Steps during the temporary regime

UK banks, investment firms and e-money institutions (e-money institutions operating via a branch must, if they intend to continue to carry out services in Italy after the end of the transitional period, submit their application to obtain an Italian licence (as a third country firm) or establish an Italian-regulated entity. (Yet another alternative – albeit not mentioned in the law decree – is obviously to transfer the business to a licensed regulated entity established in another EU Member State, which could then 'passport' into Italy.)

Under the law decree, such an application must be submitted within six months of the start of the 18-month temporary period.

In terms of UK insurance undertakings, those benefiting from the 18- month temporary regime are required to submit to IVASS (the Italian insurance regulator), within 90 days of the enactment of the law decree (and so potentially far into the 18-month temporary period), 'a plan setting forth the appropriate measures that will enable the relevant insurance undertakings properly to service the contracts outstanding as of the exit date, including as to the payment of claims or benefits'.

⁶ However, UK banks and investment firms authorised to participate in Italian government bond auctions are exempt from the requirement to deliver the notice, except if they wish to engage in deposit taking after the exit date (in which case they will also have to deliver the notice to benefit from the temporary regime).

The purpose of this 'plan' is not entirely clear. Based on its contents required under the law decree (which are meant to include the appropriate measures for servicing contracts), it would seem to be a plan to ensure that, notwithstanding Brexit and all that goes with it (e.g. potential deviation of the UK framework from that of the EU or potential lack of coordination between the respective regulators), the UK insurance undertaking will be able to perform contracts throughout the temporary period. There is no suggestion that it would be necessary to terminate during the temporary period or by the end of it.

However, the law decree further stipulates that, where the UK insurance undertaking cannot 'fully implement the plan by the end of the transitional period', it should seek an extension from IVASS – at least 90 days prior to the end of the transitional period – explaining the need for an extension on the basis of 'the structure, the terms and the multi-year tenor of contracts'. IVASS would assess the application for an extension, and consult with the UK regulator. All these provisions suggest that the 'plan' must be one as part of which contracts are expected to be terminated – rather than purely an assortment of measures to ensure the due performance of contracts during the temporary period – as otherwise the extension which may be granted to the temporary regime beyond the 18 months would make very little sense, if at all⁷. Also, the fact that no 'grace period' for the run-off of the Italian business is envisaged in the law decree for insurance undertakings (on the 'grace period' see below) points in that direction⁸.

As from exit date, clients may withdraw from contracts of insurance with residual duration over one year at no cost and any automatic renewal clauses will cease to be effective.

1.4 Where the temporary regime does not apply, or where no steps are taken for after the end of the temporary regime. The six-month 'grace period' for run-off

UK-regulated entities that cannot benefit from the temporary regime⁹, or that could have benefited but failed to timely take the steps (notice or application) needed to take advantage of it¹⁰, or that have benefited from the temporary regime but failed to submit their application to obtain an Italian licence or to establish an Italian-regulated entity within six months of the start of the temporary period, must cease their Italian operations within six months of the exit date (in the case of those who did not benefit from the temporary regime) or of the date within which a licence ought to have been sought (in the case of those who failed to timely apply for a licence, for the period after the end of the transitional period).

⁷ If the only purpose of the plan was to set up measures ensuring performance of contracts, it is hardly plausible to anticipate that such a plan may not have been implemented (and so such measures may not yet have been taken) by the end of the transitional period. The purpose of the plan, therefore, must be also to cause the termination of outstanding contracts.

⁸ The period during which the Italian portfolio is expected to be run off must be the transitional period itself.

⁹ These include payment institutions, asset managers, investment funds, banks / investment firms providing investment services cross-border to retail, opted-up professional clients and e-money institutions operating cross-border. Please refer to the table above in the text.

¹⁰ These are UK banks and investment firms, as well as e- money institutions (e-money institutions operating via a branch), which have to deliver a prior notice; in the case of UK trading venues (including where managed by banks or investment firms) an application for authorisation has to be submitted. Please refer to the table above in the text.

While running off their Italian business (within maximum six months as we have noted), such UK entities must seek to terminate their relationships with clients, and comply with the applicable termination notice periods; until termination, they must limit their activities to the servicing of the then existing client relationships without entering into any new contracts or renewing existing contracts.

By way of exception to this rule, banks and investment firms with OTC non-cleared derivatives in place with Italian clients can manage life cycle events of such contracts, including where this results in new contracts¹¹.

Finally – for the avoidance of doubt – the law decree clarifies that, during the run-off phase, the payment terms of financing arrangements, both relating to interest and relating to principal, remain unchanged.

Relevant entities must inform clients and the regulator, within 15 days of the enactment of the law decree, of the actions they intend to take with a view to ensuring the orderly run-off of the Italian business.

1.5 Scope of the temporary regime

A question may arise as to whether UK-regulated entities should, in the transitional period, only service existing contracts, or may also originate new relationships and engage with new clients.

Whenever reference is made, in the law decree, to the continuance of services existing before the exit date¹², it should be possible not only to service existing relationships, but also, potentially, to acquire new clients. This is supported by the fact that, where it is intended that the post-Brexit activities should be limited to servicing the existing contracts, the law decree states that exactly, adding that no new contracts may be entered into¹³.

Note that, regarding trading venues, these can continue to grant access to clients established in Italy during the transitional period and if they benefit from the transitional period. However, no new clients can be on-boarded.

Where contracts have, under the law decree, to be terminated – such as in the six-month run-off period – we understand that the ‘contracts’ referred to are those which are capable of being terminated unilaterally by notice to the client, i.e. typically the

¹¹ This possibility is granted (a) with respect to OTC contracts as of exit date, and for the six months thereafter, in the case of banks / investment firms that failed to timely deliver the prior notice to benefit from the transitional period; (b) with respect to OTC contracts as of the date within which the application ought to have been submitted, and for the six months thereafter, in the case of banks / investment firms that failed to timely submit the application for the licence needed for the period after the end of the transitional period

¹² This is the case of banks providing banking / financial services (including deposit taking and lending) which can ‘continue to carry out the banking and financial services’ that they used to carry out before exit date; of banks / investment firms providing investment services, which can ‘continue to carry out the investment services’ that they used to carry out before exit date; and of e-money institutions, which can continue to operate in Italy in the same ways as before exit date to the extent they act from an Italian branch.

¹³ This is the case, e.g., of payment institutions, asset managers, investment funds, and banks / investment firms providing investment services cross-border to retail and opted-up professional clients during the six-month run-off period; or of insurance undertakings during the 18-month transitional period.

terms of business for the provision of banking or investment services. There will be outstanding contracts, however, entered into with clients under the general terms of business and which, by their terms, must be performed and cannot be contractually terminated by one side alone; for example, derivatives.

It would appear – although this is admittedly a matter of interpretation, as the point is not explicitly addressed in the law decree – that contracts entered into under the general terms of business or master agreements (such as derivatives) do not have to be terminated and can continue to be performed after the exit date regardless of the transitional regime (whether or not this is available). It should be possible to argue, based on general principles of Italian law, that those contracts should not be affected by the loss of the licence to provide services (a licence which was duly held by the UK entity at the point of entering into the contract) and may accordingly continue to be performed until their final maturity.

Consistent with this interpretation is the rule laid down, for the six- month run-off period, in relation to OTC non- cleared derivatives. In the context of these, any rights relating to life cycle events may be exercised in the run-off period, even where new contracts may arise as a result (e.g. following the exercise of options). Clearly, since such ‘new contracts’ (resulting from life cycle events) may happen to arise, potentially, even as late as near the end of the six-month run-off period, it must be possible to continue to perform those ‘new contracts’ even beyond the end of the run-off period¹⁴. So, arguably, the continuance of binding contracts (other than terms of business) must not be dependent on any express permission to keep those contracts in place, whether under the transitional regime or under the 6-month run-off period.

It should also be possible to pursue this same line of argument with respect to contracts of insurance. As we have already seen above, the ‘plan’ to be submitted by UK insurance undertakings likely requires them to seek to terminate outstanding contracts; however, the possibility is envisaged in the law decree that the relevant UK insurance undertaking may not succeed in implementing the plan by the end of the transitional period. In that case – which may be due to the ‘multi-year’ tenor of contracts – an extension may be sought by the UK insurance undertaking from IVASS. This may lead – in our understanding – to keeping policies in place until they are due to expire, if it is not possible for the insurer to terminate earlier.

¹⁴ Why, otherwise, permit new contracts to arise, as a result of life cycle events, to then immediately, upon the end of the six-month run-off period, impose that they be terminated? This would be hardly plausible.

1.6 Applicable rules under the temporary regime

UK banks, investment firms and e-money institutions benefiting from the temporary regime shall be subject, during the temporary period, to the same rules that applied to them before the exit date (and so the EU framework); however, the Italian regulators may exercise over them the powers in the matter of crisis management and insolvency that are available with respect to non-EU firms.

UK banks providing banking/financial services, payment institutions and e-money institutions with branches in Italy, as well as banks/investment firms providing investment services into Italy out of an Italian branch, will have to continue to participate in the out-of-court dispute resolution scheme foreseen under Italian law; whereas those same entities, if operating cross-border into Italy, may also adhere to a non-Italian out-of-court dispute resolution scheme as long as it is part of the Fin-Net network endorsed by the EU Commission.

UK banks with a branch in Italy will be considered automatically a member to the Italian deposit insurance scheme; those taking deposits in Italy on a cross-border basis may continue to be members only to the UK deposit insurance scheme in so far as this makes a statement confirming that Italian depositors will be covered. The same applies to banks and investment firms, as far as investor protection schemes are concerned¹⁵.

2. Italian Regulated Entities

Italian-regulated entities can continue to carry out their activities in the UK in the transitional period subject to prior notice to the competent Italian regulator¹⁶, at least three business days ahead of the exit date, and in compliance with applicable provisions of UK law. Within six months after the exit date, Italian-regulated entities will have to apply to the Italian authorities for authorisation to continue to carry out their activities in the UK after the end of the transitional period (as long as the UK requirements are also complied with).

Italian managers of trading venues (MTFs, OTFs or markets) willing to continue to grant access to clients established in the UK after exit date must file the relevant application with the competent Italian authorities for authorisation to operate in the UK (again, also the UK requirements will have to be observed).

¹⁵ UK banks and investment firms with a branch in Italy will be considered automatically a member to the Italian investor protection scheme; those providing investment services in Italy on a cross-border basis may continue to be members only to the UK investor protection scheme in so far as this makes a statement confirming that Italian investors will be covered.

¹⁶ Except for Italian insurance undertakings, which do not have to submit any prior notice.

3. Tax Provisions

During the transitional period, Italian tax provisions based on EU membership, including those deriving from the implementation of EU tax Directives, will continue to apply to the United Kingdom. The same will apply, as far as compatible, for VAT and excise duties provisions deriving from EU Directives and Regulations.

This means that qualifying UK entities would in principle continue to benefit from:

- withholding tax exemption provided under domestic law on interest payments under medium/long-term loans granted to Italian enterprises;
- 0.25% substitute tax regime on medium/long- term loans granted to Italian enterprises (in lieu of stamp taxes ordinarily applicable);
- withholding tax exemption regimes granted by EU Directives on dividend, interest and royalty payments made by Italian entities;
- reduced 1.2% withholding tax (in lieu of the 26% ordinary rate) on profits distributions by Italian
- entities, in case the conditions for the application of full exemption regime under the Parent Subsidiary Directive are not met;
- tax neutrality, for corporate income tax purposes, of cross-border M&A transactions.
- Terms and procedures for the implementation of the transitional tax provisions introduced by the law decree will be set out by one or more Decrees to be issued by the Italian Ministry of Economy and Finance.

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