Newsletter from our FRANKFURT OFFICE (Tokyo - Frankfurt): *Atsumi Sakai Janssen Rechtsanwaltsgesellschaft mbH*

Atsumi & Sakai is a multi-award-winning, independent Tokyo law firm with offices in London and Frankfurt.
Expanding from its highly-regarded finance practice, the firm now acts for a wide range of international and domestic companies, banks, financial institutions and other businesses.
The firm operates as a foreign law joint venture, combining a comprehensive Japanese-law and German-law practice consisting of a team of highly experienced Japanese, German and other foreign lawyers.
The Frankfurt office advises its clients in Japanese, English or German both in German and European law.

‘Brexit’ Implications for Financial Institutions (1)
- Why Frankfurt can be an alternative -

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Brexit Vote

Following the referendum of 23 June 2016 whereby 51.9 per cent of the electorate voted for an exit of the United Kingdom from the European Union, it is now envisaged that the United Kingdom will leave the European Union (EU), which in turn means, it will most likely leave the European Economic Area (EEA), as well. This has created significant uncertainty for the UK, the EU, and global economies.

With formally declaring the exit according to Article 50 Treaty on European Union (TEU) on 29 March 2017 vis-à-vis the EU, British prime minster Theresa May triggered the two-year process of leaving the EU.

Brexit talks now have started as scheduled on 19 June 2017, the goal of which is the negotiation of a withdrawal agreement. If no such agreement can be reached by the end of March, 2019, the EU treaties will automatically cease to apply to the UK (so called ‘Hard Brexit’). In order to avoid Hard Brexit, a withdrawal agreement would have to be agreed upon beforehand, or at the latest, by March 29, 2019. Afraid to lose the ability to conduct business in the EEA, many banks and other Financial Institutions (jointly “Financial Institutions”) based in the UK have already taken steps to relocate parts of their business to other EEA countries. Though the outcome of the negotiations is at this point still unclear, it is fair to say that the impact of Brexit on the financial sector will be substantial and that it is not advisable to simply wait out the process. The stakes are clearly too high.

This newsletter will deal with the EU financial passports and reaction of the market to Brexit, whereas a second newsletter will address the matter of setting up a subsidiary in Germany and a third newsletter the labor law aspects.

No more passporting rights

One of the main aspects regarding the UK’s decision to leave the EU is the fear of losing so-called European passporting rights ("EU passports"), introduced in 1995. The EU passport is a term referring jointly to a variety of different passports, which enable Financial Institutions inside the EEA to trade their products and do business within the whole of the EEA by having just one EEA-licensed subsidiary. There is no single EU passport set out in any one directive. Whenever an EU directive or regulation which deals with a regulated activity, provides for member states to allow businesses from other member states to enter their market, this is termed passporting. A summary of some of the relevant directives can be found at:
http://www.bankofengland.co.uk/pra/Pages/authorisations/passporting/default.aspx.

‘Brexit’ will lead to a situation in which Financial Institutions currently established in the UK will be treated as third country Financial Institutions, thereby losing the privileges available under the current system, unless stipulations in the withdrawal agreement provide to the contrary, which appears to be unlikely.

Loss of passporting rights will affect all Financial Institutions (in particular, investment-banking, asset management, wealth management, payments, and cash management activities). For asset management activities, the Alternative Investment Fund Managers Directive (AIFMD)[1] could probably be extended to the UK as a third-party country operating under “equivalent” regulation[2], with a number of limitations and subject to approval from the European Securities and Markets Authority (ESMA). To distribute Undertakings for Collective Investment in Transferable Securities (UCITS) funds in the EEA, however, the UCITS Directive[3] requires the domiciliation of funds and their management companies in the EEA, meaning that UK asset managers would need to establish a gateway hub in the EEA if they do not already have one.

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Likewise, investment management businesses in the UK would also require an EU gateway hub in order to provide products and services in the EU under the Markets in Financial Instruments Directive (MiFID)[4], unless their products target only professional clients, which is possible under "granting of equivalence" . A very good summary of the differences between passporting and equivalence under the various directives can be found in the table on p. 3 of the following document:
http://www.europarl.europa.eu/RegData/etudes/BRIE/2016/587369/IPOL_BRI(2016)587369_EN.pdf

As such, Financial Institutions face the option of either giving up their EU business, or establishing a fully authorized and licensed branch or subsidiary in one of the other EU member states. Depending on the outcome of negotiations between the UK and the EU, these subsidiaries may need to be "substantial" (beyond merely a light footprint) and both independently and robustly capitalized in order to be compliant.

A solution in which the UK leaves the EU, but at the same time upholds only the beneficial rules without supporting the EU budget and allowing for the free movement of persons is not very likely. For instance, the often-discussed Norway model, where Norway is a member of the EEA, but not the EU (just like Iceland and Liechtenstein), still includes the free movement of persons, which according to Theresa May would not be acceptable for the UK.
(sources: e.g.
https://www.fnlondon.com/articles/norway-model-offers-britain-a-solution-on-brexit-20170616;
https://www.theguardian.com/politics/2016/dec/01/can-the-uk-adopt-the-norway-model-as-its-brexit-solution)

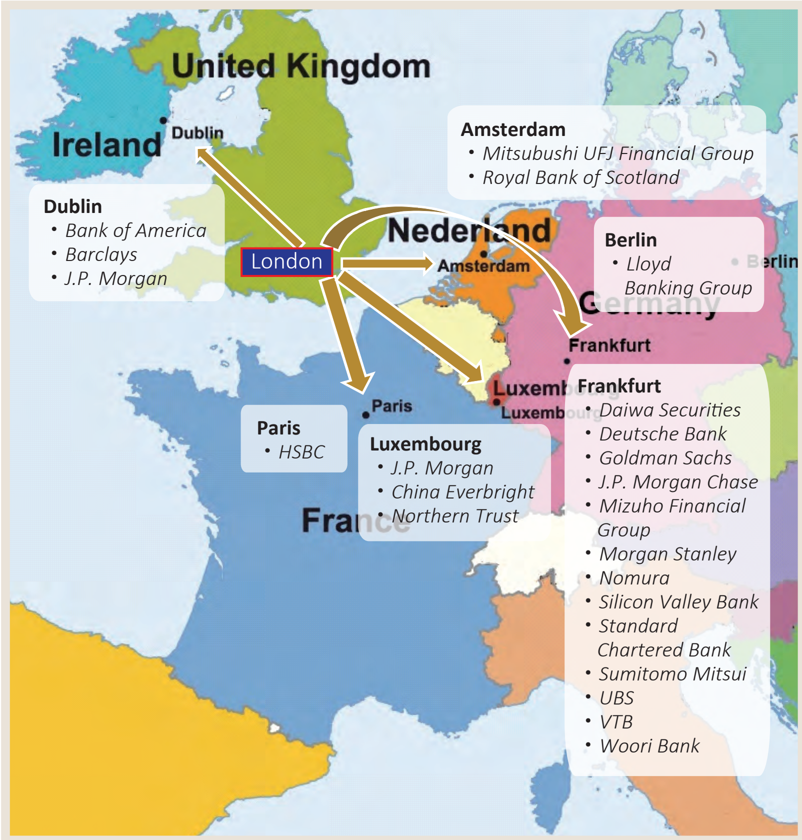
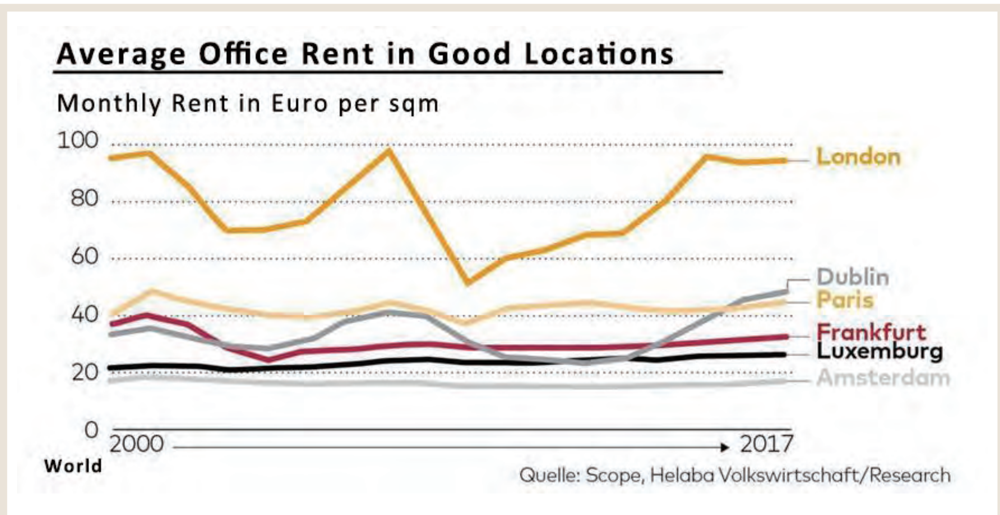


Image retrieved from the website of European Commission:
https://ec.europa.eu/avservices/photo/photoByMediaGroup.cfm?sitelang=en&mgid=38

Reactions of the market

Frankfurt is the greatest winner in the battle for 'Brexit' relocations of Financial Institutions. So far, a number of Financial Institutions have decided to relocate a substantial part of their operations to Frankfurt and – in some cases to establish their future EU headquarters in the city - to ensure access to the single market even after a 'Brexit' .

Amongst the Financial Institutions that have already indicated that they will extend their presence in Frankfurt considerably are Sumitomo Mitsui Banking Corporation, Nomura Holdings Inc., Daiwa Securities Group Inc., Standard Chartered Plc, Citigroup Inc., Goldman Sachs Group Inc. and Morgan Stanley.



Frankfurt is not only Germany' s financial center, but already one of Europe' s and the world' s financial centers. Among other banks and Financial Institutions it is the location of the European Central Bank (ECB), the European Insurance and Occupational Pensions Authority (EIOPA), the German Bundesbank as well as the German Federal Financial Supervisory Authority (BaFin). Especially the close proximity of the ECB, being the central bank for the EURO, is an advantage for Financial Institutions. The ECB defines and implements the monetary policy of the eurozone[5]. A constant and immediate contact with the regulatory authority itself allows for information exchange, lobbying opportunities and the discussion of questions and future policies both on a formal and informal level.

It is reported that Wolfgang Schäuble, Germany' s finance minister, encouraged all Financial Institutions to favour Frankfurt as their new home after Brexit and touted the stable German economy as a key plus side of making the move. Also, Volker Bouffier, the Minister-President of the state of Hessen, lauds the city as "the most important financial hub in continental Europe and a key centre of financial market stability" .

The city has many advantages in comparison with other options like Paris, Dublin or Amsterdam. From a more practical point of view, Frankfurt' s airport is a major air traffic hub, located just 20minutes from the city center and offering several daily direct flights to Japan. The BBC reports that there are approximately one million square metres of office space in Frankfurt available for immediate occupancy, and an extra 250,000 square metres will be available within the next few years. It has also been reported that there is a plan for 20 new skyscrapers in Frankfurt[6]. Also, there is an advantage from a language perspective, in which everyday communication can easily be conducted in English in Frankfurt. Germany also offers the option for tax returns and regulatory submissions to be carried out in English.

Furthermore, the state of Hessen currently is exploring ways to loosen labor law requirements for highly paid employees that are not categorized as executives (will be described in a later newsletter). Lastly, Frankfurt is a cultural center of the region. It boasts with numerous museums, theatres, restaurants, and cafés, as well as a famous opera house and several festivals throughout the year.

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[1] DIRECTIVE 2011/61/EU. This Directive lays down the rules for the authorisation, ongoing operation and transparency of the managers of alternative investment funds (AIFMs) which manage and/or market alternative investment funds (AIFs) in the Union (Art. 1).
[2] "Equivalence" is a critical concept for financial services offered inside the EU, but originating from third countries. If the regulations in those third countries are substantially close to those in the EU, the financial institutions regulated in such country can perform certain financial services in the EU under certain regulations which are less strict than other foreign financial institutions.
[3] DIRECTIVE 2009/65/EC ('UCITS Directive') is the directive on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities. It facilitates that such collective investment schemes are possible in the EU in case they are authorized in at least one member state.
[4] DIRECTIVE 2004/39/EC. MiFID harmonizes regulation for investment services in the EEA, with the aim on increasing competition and consumer protection. Due to several amendments over the years it has been recast with DIRECTIVE 2014/65/EU (MiFID II), extending the scope of products and activities, enhancing investor protection and extending transparency.
[5] Art. 3 ECB Statute
[6] *http://www.bbc.com/news/business-41026575*


Frankfurt


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Topics

Japanese attorney (Bengoshi) Daisuke Tsuzuki commenced work at the Frankfurt office on September 1, 2017 after completing his LL.M. at the University of Southern California (USC) Gould School of Law.

Author(s) / Contacts

[Author / Local Contact]
Atsumi Sakai Janssen Rechtsanwaltsgesellschaft mbH,
a German legal professional corporation

Frank Becker

Admitted in the Federal Republic of Germany*

> View Profile

E-mail:
frank.becker@asj-law.jp

[Author / Contact in Japan]
Atsumi & Sakai
Tokyo Head Office

Takafumi Uematsu

Admitted Japan (2004)
and California (2010)

> View Profile

E-mail:
takafumi.uematsu@aplaw.jp

[Author]
Atsumi Sakai Janssen Rechtsanwaltsgesellschaft mbH,
a German legal professional corporation

Pascal Soepper

Admitted in the Federal Republic of Germany*

> View Profile

E-mail:
pascal.soepper@asj-law.jp

* Not Registered as a Foreign Lawyer and not practicing law in Japan

Profiles

Frank Becker

Before opening the Frankfurt office, Frank Becker was one of the founding partners of the Munich office of a major US law firm and an associate in a Magic Circle firm. He leads the Frankfurt office and has extensive experience in M&A transactions and joint ventures. He studied law in Japan for a year and advises Japanese clients in connection with German law related matters, with a focus on transactional, corporate and compliance matters.

Takafumi Uematsu

Takafumi Uematsu previously worked as a secondee at the Frankfurt office of Norton Rose, and since then has been involved in EU-related matters, such as EU financial regulations, antitrust, and data protection matters.
He has experience in cross-border matters between Japan and the EU.
He has extensive experience in securitizations and M&A transactions.
He manages the Tokyo-based German desk.

Pascal Soepper

After serving as Assistant Professor at Niigata University for a term of 3 years, Pascal Soepper joined Atsumi Sakai Janssen in 2016 and recently relocated to Frankfurt. He works in the field of general contract and corporate law, as well as IT Law and FinTech, with a particular emphasis on crowdfunding.

Location (Frankfurt Office)

Atsumi Sakai Janssen Rechtsanwaltsgesellschaft mbH
Taunusanlage 21, 60325 Frankfurt am Main, Germany

Contact

Europe Practice Team (Atsumi & Sakai)
E-mail: info_frankfurt@aplaw.jp