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THE NEW EU/UK DEAL

THE IMPACT ON UK BANKS AND THE BREXIT DEBATE

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"The new deal reached between UK Prime Minister David Cameron and the European Union represents significant progress for UK interests in banking services," says Clifford Chance Partner Jonathan Lewis.

"The provisions give a balanced framework to preserve UK interests in banking services and preserve a level playing field for all EU financial institutions whilst permitting euro area Member States to pursue their own long term goals of deeper fiscal and economic union," he said. It provides both euro area Member States and non-euro area Member States a pathway for the future.

The deal, which was signed in February, is legally binding and should in future be used as an aid to interpretation of the EU Treaties and legislation. However, the new arrangements will cease to exist if the British public votes to leave the EU in the referendum in June. "If the UK votes 'out' it could mean that the UK and its financial institutions will not benefit from the safeguards of the February settlement but will still have to abide by EU laws and regulatory requirements in order to maintain access to the single market. The UK could potentially become a rule-taker and less of a rule-maker comparable with EEA countries such as Norway and no longer have a guaranteed place at the negotiation table," Lewis said.

The new deal offers the UK important safeguards whilst permitting the euro area to pursue its project of deeper fiscal and economic integration as mapped out in the Five Presidents' Strategic Paper "Completing Europe's Economic and Monetary Union". The protections of UK interests under the new deal are more robust than the existing status quo which is limited to the double voting mechanism at the EBA, certain anti-discrimination provisions in the regulation creating the single resolution mechanism and the fall-back of taking legal action at the ECJ which has to date offered limited success for the UK (with the exception of the location of clearing house case).

Since the global financial crisis the EU has focused on making financial institutions safer, the tightening-up of capital requirements, steps to facilitate the resolution of institutions including those which are "too big to fail" and a move away from state sponsored "bail outs." Since the euro areas sovereign debt crisis, the Euro area Member States pushed through a series of concerted measures, driven by unprecedented political cohesion which, while defusing the debt crisis and preserving the euro, dramatically transformed the dynamic and institutional framework of the EU. These changes were, in the main, driven by the euro area and decided by the Member States of the euro area, often acting on an inter-governmental basis and have created new euro area institutions and, with a view to breaking the negative feedback or "death loop" between weak banks and weak sovereigns, created a banking union for the euro area.

"It provides both euro area Member States and non-euro area Member States a pathway for the future."

Jonathan L. Lewis, Partner, Paris

The UK had a number of concerns regarding the increased integration of the euro area. With the growing influence and importance of the ECB, the Eurogroup and new euro area or banking union institutions, there was a perceived loss of influence for the UK. There was a feeling that decisions directly affecting the euro area or banking union were being made by institutions or intergovernmental arrangements which related solely to the euro area but which had a wider impact on the EU and the single market in meetings where the UK was simply "not in the room." There were also concerns that by the euro area acting en bloc, decisions could be taken in relation to banking union or by qualified majority voting which would undermine the single market and the level-playing field to the detriment of non-euro area financial institutions.

There was also a perceived threat that rules or decisions could be set in a discriminatory fashion to the detriment of non-euro area institutions. The threats were not just perceived but manifested themselves in concrete action, such as the decision of the ECB that central derivatives clearing houses should be required to have access to Eurosystem liquidity in order to be eligible to clear euro-denominated derivative contracts.

In the financial services area the new deal includes the following:

- An explicit recognition of there being different paths to integration.
- The participation of non-euro area Member States in measures to deepen economic and monetary union will be voluntary (i.e. the UK will not be obliged to adopt these measures). On the other hand, non-euro area Member States shall not create obstacles but facilitate the further deepening of integration by the euro area Member States.
- EU institutions and Member States shall facilitate co-existence between euro area and non-euro area Member States to ensure the equality of Member States under the EU Treaties as well as the level-playing field and the integrity of the single internal market.
- There is an express prohibition against discrimination between legal or natural persons based on the official currency or legal tender of their Member State.
- Legal acts, including inter-governmental agreements shall respect the internal market and not construct trade barriers to or discriminations in trade.
- Banking union laws shall only apply to credit institutions located in euro area Member States (or non euro area Member States which have concluded a close cooperation agreement).
- The single rule book shall apply to all credit and other financial institutions to ensure a level-playing field within the single internal market. However, there is recognition that specific provisions may be needed for euro area institutions only.
- Non-euro area Member States shall have no budgetary responsibility for emergency measures designed to safeguard the financial stability of the euro area but shall have sole authority and budgetary responsibility for measures to preserve their own financial stability and the stability of institutions established in such Member State.

"The package represented by the new deal is an improvement on the status quo."

- With a view to preserving the role of all Member States in Council deliberations, there is a requirement that euro area Ministers respect the powers of the Council. Similarly, there is a requirement that informal discussions between Member States respect the powers of Council and the right of non-euro area Member States to participate in deliberations even on matters where they do not have a vote.

The deal also includes the non-euro area "Yellow Card" mechanism. If a Member State which is not part of the Banking Union indicates its reasoned opposition to a legislative act which appears to contravene the principles on economic governance, it can require the Council to discuss the issue. The Council is required to do all in its powers to reach a satisfactory solution to the concerns of the non-euro area Member State including a potential referral of the issue to the European Council to resolve.

Whilst the "Yellow Card" procedure is a political rather than a judicial mechanism in an EU context the behavioural expectation of achieving a solution through mutually agreed consensus when vital national interests are at stake should not be underestimated. However, it is not a veto.

The "acid test" of the efficacy of the new deal will be whether in practice the European Court of Justice uses the principles of this new aid to the interpretation of the EU Treaties to come to conclusions which reflect the principles of non-discrimination and maintenance of the level playing field set out in the settlement.

Other provisions which may have impact financial services include the "Red Card" mechanism to require the Council to discontinue discussions of draft legislative acts if 55% of national parliaments pass reasoned resolutions objecting to a measure because it does not respect the subsidiarity mechanism.

Lewis says: "This represents a genuine attempt to create a balanced solution to permit deeper integration amongst the euro area Member States whilst providing safeguards to protect UK and non-euro area Member States' interests." He added that the new deal aims to protect the integrity of the internal market and level-playing field and to preserve real participation of the UK in Council level discussions. The safeguards are clearly a significant advance on the limited protections which currently exist prior to the Decisions of 18 and 19 February 2016 coming into force.

"If the sole criterion for a decision on the referendum were to be the financial services industry, the integrity of the single market, access to the single market for financial services and the maintenance of a level playing field for all European financial institutions, it would be necessary to weigh the tangible benefits of the new deal, which is an improvement on the status quo against the potential outcome on these issues under the terms of any Article 50 withdrawal agreement to be negotiated following an "Out" vote".

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