

MEMORANDUM

To Fiona Taylor ISDA

From Allen & Overy, Italy
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Subject **CONSOB Warnings in connection with Brexit**

This Memorandum provides summary information in connection with certain communications which have been issued by Consob (Italy's securities regulator) in order to address, *inter alia*, the ability of UK banks and investment firms (UK Institutions) to provide investment services, including in respect of OTC derivatives entered into with Italian counterparties, in light of Brexit.

The Consob updated its website following the reaching of the withdrawal agreement, in order to take note of the fact that previous legislation for a "no-deal" scenario¹ was no longer applicable and therefore cancel the relevant communications Consob had issued in order to allow UK intermediaries and trading venues to continue to operate in Italy under a specific transitory regime. The communications of Consob in relation to Brexit preparedness have been issued in the form of "Warnings" addressed to market participants.

The only communication Consob did not cancel from its "no-deal" series of Warnings is Warning no. 4 of 12 March 2019 (**Warning 4/2019**), which requires in general terms that UK Institutions offering investment services in Italy (whether through branches or cross border) proceed with urgency, if they have not already done so, to provide customers with appropriate information on the consequences of the changes to operating conditions following Brexit. The information provided by UK firms should be calibrated to the type of

¹ Italian law decree no. 22/2019.

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customer (retail vs professional) and discuss the impact of Brexit on the trading relationship and the measures taken to ensure the orderly termination of activities.

The fact that Warning 4/2019 is still considered to be in effect for Consob may not require any specific action on the part of UK Institutions if they have already been in touch with customers to provide information surrounding Brexit. Nevertheless, Warning 4/2019 could, in our view, be interpreted as requiring UK Institutions to update information to customers as to the transition period (currently scheduled to expire on 31 December 2020) based on the Withdrawal Agreement which entered into force on 1 February 2020², in particular as the end of the transition period approaches.

On 26 March 2020, Consob issued three Warnings (numbers 3, 4 and 5 of 26 March 2020), which are based on the arrangements set forth in the Withdrawal Agreement.

Warning no.3 of 26 March 2020 (**Warning 3/2020**) deals with the situation of UK Institutions (as opposed to trading venues) and takes note of the fact that, at the end of the transition period, UK entities will become "third country" entities for the purposes of MiFID II/MiFIR.

The Consob points out the potential for an equivalence decision to be reached at the EU level, but states that, even in the absence of an equivalence decision, each Member State is entitled to allow non-EU firms to operate in its territory, either through a branch or on a cross border basis. In that regard, Warning 3/2020 draws attention to the provisions Article 28(6) of Italy's Consolidated Law on Finance (the **CLF**) which address authorisation for third country entities and notes that the establishment of a branch is required for the provision of services to retail and elective professional clients. Although not yet evidenced in the official role kept by Consob, we note that Consob has conditionally³ authorised a UK investment firm to carry out investment services in Italy vis-à-vis eligible counterparties and per se professional clients on a cross-border basis. We understand that CONSOB granted the authorisation on the basis of a Memorandum of Understanding (the **MoU**) entered into between the Bank of Italy and CONSOB and the UK supervisory authority. Although the content of the MoU is not publicly available, we believe that the MoU is considered by Consob to satisfy the requirement for a sufficient cooperation agreement with the third country (i.e. UK) regulator, as required under the Italian third-country licensing regime.

Apart from Brexit-related authorisations, we would note that, at present, no intermediaries constituted outside of the European Union have been authorised by Consob to provide investment services in Italy either through a branch or on a cross-border basis. In particular, this is the case because Consob does not consider any of the cooperation agreements it has entered into with non-EU supervisors as eligible for the purposes of the Italian Financial Act.

If, on the other hand, an equivalence decision is forthcoming at the EU level, Consob notes that UK Institutions will have to request a specific authorisation from Consob if operating with retail and elective professional clients.

Warning 3/2020 invites UK Institutions to promptly notify Consob of their interest in continuing to operate in Italy or their intention to cease operations once the transition period will have ended.

With specific reference to the OTC derivative contracts in place with Italian counterparties, Warning 3/2019 notes that – in the absence of an equivalence decision and/or authorisation of a UK Institution as a "third country entity" - contracts outstanding at the end of the transition period (i.e. those that have not been transferred to an EU27 entity) may lead to UK Institutions facing charges for lack of licensing, which may in turn have repercussions on the contracts themselves. The Consob cites in particular a potential "early termination" for OTC derivatives in this case. However, we would not exclude further repercussions for

² Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community (2019/C 384I/01).

³ The conditionality relating to actual departure of the UK from the EU, the terms of any agreement governing the future relationship of the UK and the EU and also the potential for any equivalence decision to be in place at such time.

contracts in these circumstances, including difficulties in the UK entity enforcing obligations under the contract.

Finally, Warning 3/2020 states that UK Institutions should provide Italian clients with up-to-date information on *"the consequences of the changed operating conditions resulting from Brexit, also with reference to the specific implications for the OTC contracts in place."* To the extent that a UK Institution would be transferring trading relationships to an EU 27 entity, then it is clear to us that information in connection with that process should be communicated to Italian customers. It is not clear to us what sort of information should be communicated if the UK Institution finds itself in the position noted in the preceding paragraph, but as noted above, we believe that this would be a situation leading to serious problems of enforceability for OTC derivatives contracts in any case.

Warnings 4 and 5 of 26 March 2020 are specific to trading venues as opposed to relating to UK Institutions.