

## Financial Services: Settlement Finality (Third Country Provisions)

### Withdrawal of the United Kingdom from the European Union (Consequential Provisions) Act 2019

#### Most relevant to

- Irish, UK and other investors trading Irish equities, bonds and units in exchange-traded funds.



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Part 7 of the Act addresses a very specific (but fundamental) element of Irish financial services infrastructure.

The Irish Stock Exchange currently uses a UK central settlements depository, CREST, to settle trades in Irish bonds, equities and fund units. In a no-deal scenario, the ability of Irish market counterparties to access CREST or other designated system and to benefit from the relevant EU rules and benefits under the Settlement Finality Directive would be compromised.

To address this issue the EU Commission has proposed a transition period of two years to allow market counterparties to transition to an EU based central security depository.

#### What does the Act say?

Part 7 is proposed to support the EU proposal by conferring power on the Minister for Finance to designate third country systems (such as CREST) under Irish law as a relevant arrangement or designated system under the Settlement Finality Directive.

Under the terms of the Act, an operator of any UK settlement system which falls within the definition of "relevant arrangement" must notify the Central Bank of Ireland (CBI) and the Minister no later than three months from the date on which the operator becomes aware that the section applies. Upon receipt of any notification by the Minister, he or she will notify the European Securities and Markets Authority of the receipt of the notification and the name of the operator of the relevant arrangement.

Once the notification has been received, the Minister may (in his or her discretion) issue a notice designating the system as a relevant arrangement where the CBI has

notified the Minister that it is satisfied that:

- the rules would (if the arrangement were an EU system) comply with the regulations implementing the Settlement Finality Directive; and
- the UK laws applicable to matters which the Settlement Finality Directive relates are equivalent to the relevant Irish laws.

The Minister also has the power to issue a withdrawal notice cancelling the designation of a relevant system where the CBI notifies the Minister that it is no longer satisfied that the conditions above apply.

This designation process (whereby UK settlement systems may be designated as a relevant arrangement under the Settlement Finality Directive) will only apply for a transition period of nine months from the date on which part 7 is brought into force by statutory order. This is the same period as outlined in the draft General Scheme and the Bill. The designation will also cease to apply if the Minister issues a withdrawal notice, or if there ceases to be an Irish participant in the relevant UK settlement system.

#### Our thoughts

As with the terms of the Bill, the proposal outlined in the Act is very welcome in clarifying the basis for the transitional period, many questions remain for Irish counterparties as to how trades in Irish equities, bonds and fund units will be settled once the transition period has expired. The establishment of a new European central depository scheme is currently under consideration by Euroclear; however, it is currently unclear as to whether the new system will replicate all of the current features of the CREST system used by Irish

participants. In particular, it remains to be seen whether the new central depository system will allow counterparties trade Irish equities in the same manner as on the current CREST system.

It is also unclear how market participants will transition to a new system following expiry of the transition period. Primary legislation would be the most efficient manner to allow participants access the new system and to take all necessary steps to transition their current arrangements (such as updating share registers and other administrative changes). However, in the absence of primary legislation, market participants might need to consider individual schemes of arrangement in relation to instruments which are traded and settled on the Irish Stock Exchange.

Part 7 is the only part of the Act dealing with general financial services (apart from insurance which is covered in Part 8). In contrast to Part 8, no proposals

have been included to date in Part 7 or elsewhere in the Act to allow market participants in receipt of services or products issued by UK or Gibraltar to continue to rely on such services or products received to date. While customers relying on insurance products may be in a different position to many customers receiving other financial services, it remains to be seen if any further transitional or other arrangements will be proposed for financial service providers currently writing business into Ireland (in particular business involving the provision of products that will continue post-Brexit).