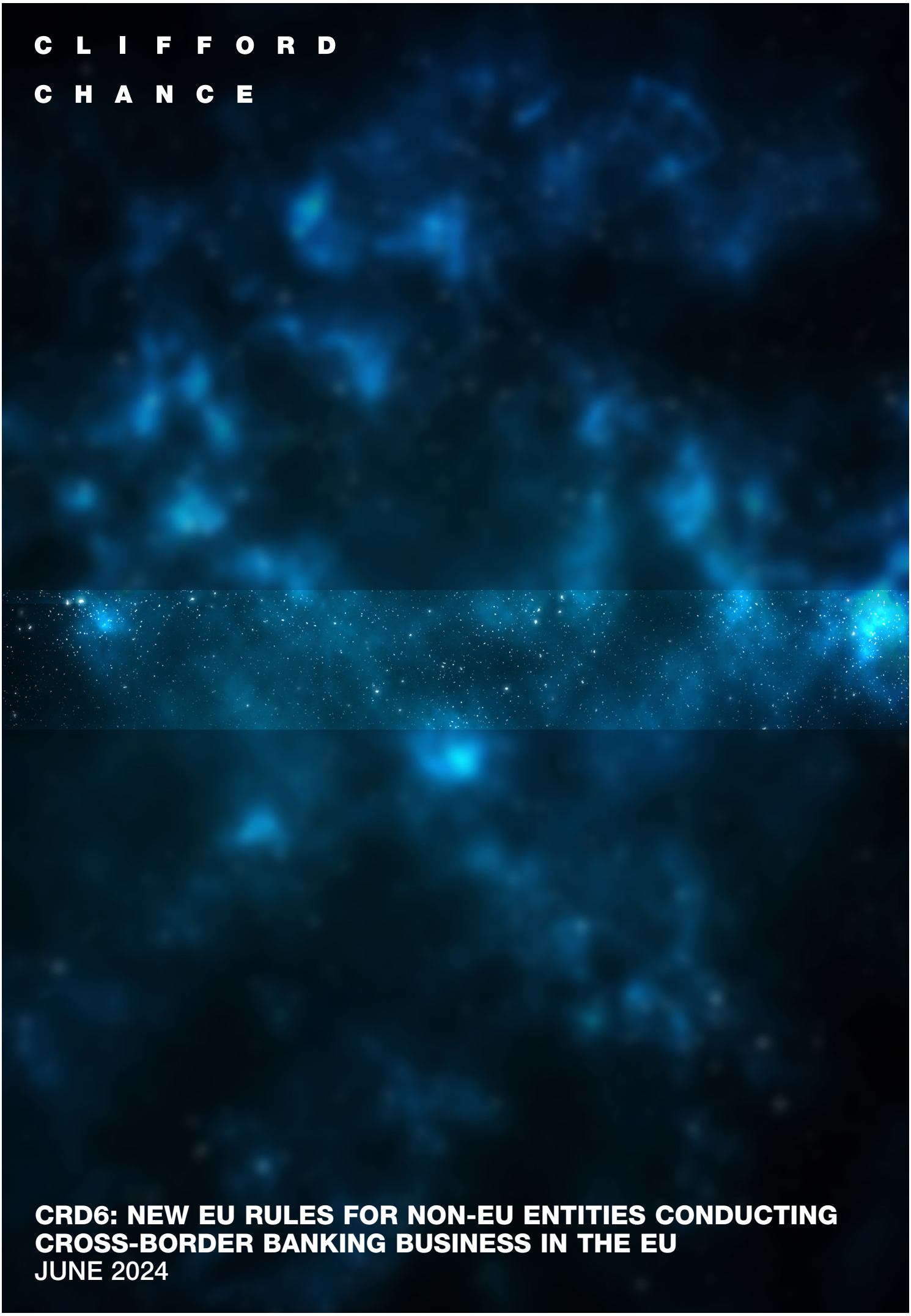


# CRD6: NEW EU RULES FOR NON-EU ENTITIES CONDUCTING CROSS-BORDER BANKING BUSINESS IN THE EU

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# CRD6: NEW EU RULES FOR NON-EU ENTITIES CONDUCTING CROSS-BORDER BANKING BUSINESS IN THE EU

The new EU Capital Requirements Directive (CRD6) will require non-EU entities intending to provide 'core banking services' in an EU Member State to establish an authorised local branch in that Member State unless one of the limited exemptions applies. A new Article 21c of the Capital Requirements Directive (CRD) will restrict the cross-border provision of loans or credit and guarantees or commitments by non-EU banks and the taking of deposits or other borrowing in the EU by any non-EU entity. Member States will be required to apply the new rules from January 2027.

CRD6 also includes amendments to the CRD that will harmonise the rules that Member States must apply when authorising and supervising EU branches of non-EU banks (see our briefing, CRD6: *New EU rules for EU branches of non-EU banks*, available on our website). CRD6 is being adopted in parallel with a new EU regulation (CRR3) which amends the Capital Requirements Regulation (CRR) to implement the final elements of the Basel 3 framework for the prudential regulation of banks.

## When will the new rules for cross-border banking business take effect?

CRD6 has now been published in the Official Journal and will enter into force on 9 July 2024.

Member States will be required to transpose the new requirements for cross-border business into their national legislation by 10 January 2026 (18 months after entry into force) and to apply the new requirements to cross-border business from 11 January 2027 (30 months and one day after entry into force). Non-EU entities conducting cross-border business in a Member State covered by the new rules will have to cease conducting that business or obtain authorisation for a local branch by the date of application of the new rules unless one of the exemptions applies.

### Key issues

- New restrictions will apply to the provision of cross-border 'core banking services' by non-EU entities
- The new restrictions will apply to the following activities in a Member State:
  - Non-EU banks providing loans or credit or guarantees or commitments
  - Any non-EU entity taking deposits or otherwise borrowing money
- There are exemptions for:
  - business conducted on the basis of reverse solicitation
  - business with EU banks
  - business with other members of the same group of companies
  - accommodating ancillary activities, the purpose of which is to provide services under MiFID
  - rights under contracts entered into at least six months before the new rules apply
- Authorised EU branches of non-EU banks will be prohibited from conducting cross-border business into other Member States except for:
  - some intragroup funding transactions;
  - transactions entered into on a reverse solicitation basis
- EU supervisors will be able to require EU branches and bank subsidiaries to provide information on cross-border business into the EU by non-EU group entities
- Member States to apply new rules from January 2027

**CRD6 – key dates for cross-border business of non-EU entities**

| | Timing |
|---|---|
| CRD6 enters into force … | 9 July 2024 |
| EBA to review scope of exemption for financial sector entities by … | 10 July 2025 |
| Member States to adopt national implementing measures for CRD6 by … | 10 January 2026 |
| Member States to protect legacy contracts entered into before … | 11 July 2026 |
| Member States to apply new rules for cross-border business from … | 11 January 2027 |

## What is the current EU framework for cross-border banking business into the EU?

Currently, Member States are largely free to set their own rules as to when third-country (non-EU) entities are permitted to carry on cross-border banking business with local clients or counterparties without establishing a branch. Many Member States only allow a non-EU entity to engage in such business where the business results from the 'own exclusive initiative' of the local client or counterparty (reverse solicitation). However, other Member States allow non-EU entities to obtain a licence, waiver or registration, or provide exemptions, permitting some categories of cross-border business. In some cases, Member States effectively allow non-EU entities to conduct cross-border business with local clients or counterparties because the type of business (such as commercial lending) is not a regulated activity in that Member State.

The Markets in Financial Instruments Directive (MiFID) created a regime restricting the provision of cross-border investment services to retail clients, but Member States can choose whether to apply that regime. The Markets in Financial Instruments Regulation (MiFIR) also created a regime allowing the provision of cross-border investment services to wholesale clients in the EU, but that regime is only available to investment firms authorised in 'equivalent' non-EU countries and the Commission has not yet assessed any non-EU country as being 'equivalent' for those purposes.

As a result, non-EU entities seeking to conduct cross-border business with EU clients and counterparties must deal with a 'patchwork' of different national rules, rather than a harmonised EU regime.

## What cross-border business will be subject to the new rules?

The new harmonised rules will apply to non-EU entities providing the following 'core banking services' in a Member State:

| Restrictions apply to | Providing the following core banking services |
|---|---|
| **Non-EU banks** | • Lending including, inter alia: consumer credit, credit agreements relating to immovable property, factoring, with or without recourse, financing of commercial transactions (including forfaiting).<br>• Guarantees and commitments. |
| **Any non-EU entity** | • Taking deposits and other repayable funds. |
| Source: New Articles 21c and 47(1) CRD added by CRD6 and points 1, 2 and 6 Annex I CRD. | |

A non-EU bank or non-EU entity commencing or continuing the relevant restricted core banking services referred to above in a Member State will be required to establish a branch in that Member State and apply for authorisation of the branch under the new regime established by CRD6 unless one of the limited exemptions applies. Alternatively, it may decide to conduct that business through an EU subsidiary which benefits from the ability to passport into other Member States.

For these purposes, a non-EU entity will be treated as a non-EU bank if, were it established in the EU, it would be classified as a credit institution under CRR or (even if does not take deposits) it would meet the criteria in the extended definition of 'credit institution' in CRR designed to cover large investment firms (as amended by CRR3).

CRD6 does not specify when a non-EU bank or other non-EU entity will be regarded as conducting activities "in" a Member State for these purposes and Member States may transpose or apply the requirement in different ways.

## What are the exemptions?

CRD6 provides five exemptions from the new restrictions.

- ***Reverse solicitation***. The restrictions will not apply where a non-EU entity provides core banking services to EU retail or professional clients or eligible counterparties that approach the non-EU entity at their 'own exclusive initiative'. The Directive provides that non-EU entities cannot rely on the exemption where they or a related entity (or another person acting on their behalf) have solicited the counterparty or where they market (otherwise than through an EU branch) categories of products, activities or services other than those originally solicited by the client or counterparty. However, it allows non-EU entities to market services, activities or products necessary for, or closely related to the provision of the service, product or activity originally solicited by the client or counterparty at its own exclusive initiative.
- ***Interbank business***. The restrictions will not apply to business with EU banks, including large investment firms covered by the extended definition of credit institution. The European Banking Authority (EBA) will be tasked with delivering a report by 10 July 2025 (12 months after CRD6 enters into force) on whether this exemption should be expanded to cover business with other financial sector entities. But even if the EBA meets this deadline and the Commission submits a legislative proposal for amendments extending the exemption, the EU legislators may not adopt the amendments in time for them to come into force at the same time as the new rules begin to apply.
- ***Intragroup business***. The new restrictions will not apply to activities conducted by a non-EU entity with a member of its own group of companies.
- ***MiFID ancillary business***. The new restrictions will not apply to 'core' investment services or activities covered by MiFID, including any accommodating ancillary services, such as related deposit taking or the granting of credit or loans, the purpose of which is to provide services under MiFID. A recital indicates that this exemption should take into account compliance with EU anti-money laundering and counter-terrorist financing rules.
- ***Legacy contracts***. CRD6 states that, "in order to preserve clients' acquired rights under existing contracts", the new restrictions are to be "without prejudice to existing contracts" but only if they are entered into by 11 July 2026 (six months before the application of the new restrictions). The Directive does not address the extent to

which it is possible to rely on framework agreements covering core banking services entered into before the relevant date or the impact of amendments, renewals or extensions of existing contracts.

## What are the changes for cross-border business by EU branches of non-EU banks?

The new framework for the authorisation of EU branches of non-EU banks (so-called third-country branches or TCBs) will require Member States to prohibit TCBs authorised by them offering or conducting the activities for which they have received authorisation in other Member States on a cross-border basis (even if the activity is not regulated in that other Member State, eg, because that Member State does not regulate commercial lending or any deposits or other repayable funds are not regarded as taken 'from the public').

The Directive allows Member States to provide exemptions for TCBs concluding intragroup funding transactions with other TCBs of the same non-EU bank (or a non-EU parent undertaking of that bank) and for transactions entered into on a reverse solicitation basis. However, it does not provide exemptions for other interbank or intragroup business, MiFID ancillary business or legacy contracts.

## How will EU supervisors monitor compliance with the new restrictions?

CRD6 will require each Member State to ensure that their supervisors have the power to require local branches of non-EU banks and EU banks authorised by them to provide information required to monitor the services provided to clients or counterparties in that Member State where those services are provided by non-EU entities that are part of the same group based on reverse solicitation by the EU client or counterparty. Each Member State must also ensure that a branch of a non-EU bank authorised in that Member State is subject to a requirement to report the services provided by the bank to EU clients based on reverse solicitation of services in accordance with the exemption referred to above.

## What changes were made to the Commission's original legislative proposal?

The Commission's October 2021 legislative proposal for CRD6 included proposed rules which would, if they had been adopted in their original form, have required Member States to prohibit any non-EU entity conducting cross-border business with EU clients and counterparties otherwise than on a reverse solicitation basis. The restriction would have applied to all business that is covered by the passport regime for EU banks, including deposit-taking, consumer and commercial lending, leasing, payments business, custody business, foreign exchange business and MiFID business.

The proposals were controversial because they had not been the subject of previous public consultation or impact assessment, they would have required Member States to terminate existing national regimes that allow local entities to access cross-border services provided by non-EU entities and they would have discriminated against non-EU entities by prohibiting non-EU entities conducting business activities (such as commercial lending) which local entities can conduct without a licence (in a way that might have been inconsistent with the EU's trade commitments to afford national treatment to non-EU providers of financial services).

The European Parliament took the position that the scope of the restrictions should be more limited and that there should be some additional exemptions. The Council of the EU took the position that the proposed restrictions on cross-border business should be deleted in their entirety and that the EBA should be tasked to report on how best to regulate cross-border business to inform a subsequent legislative initiative.

The eventual outcome represents a compromise between the position of the Parliament and the Council. While the final text retains restrictions on cross-border business, it further narrows the types of business subject to the restrictions, limits some of the restrictions so that they only apply to non-EU banks and broadens the exemptions available to non-EU entities.

## What will be the impact of the proposals?

Much will depend on how Member States transpose and apply the requirements of CRD6. However, it seems likely that the main impacts will be in the following areas:

- ***Cross-border lending or credit business and guarantee or commitment activities of non-EU banks***. Currently, non-EU banks can make cross-border loans or otherwise grant credit to borrowers (other than consumers) in some Member States because they can rely on national regimes specifically allowing cross-border business or because the activity of commercial lending is not a regulated activity in the Member State in question. Non-EU banks will need to re-evaluate their lending and credit activities in these Member States to determine whether they can bring themselves within one of the exemptions. Similar issues may arise where non-EU banks purchase loans or other receivables or provide guarantees or commitments, such as letters of credit or other trade finance facilities, in those Member States. In addition, non-EU entities engaging in cross-border lending or credit business or guarantee or commitment activities in the EU will need to determine whether they would be classified as a credit institution or entity meeting the amended criteria in CRR3 subject to the new regime if they were established in the EU (which may not always be straightforward). On the other hand, non-EU banks may find that the exemptions provided under CRD6 provide new opportunities for cross-border lending or credit or guarantee or commitment business in some Member States which currently have more restrictive regimes.
- ***Cross-border borrowing by non-EU entities***. Currently, non-EU banks or other entities can in some cases take deposits from or otherwise borrow or raise debt finance from EU creditors (including by the issue of debt securities) because they can rely on national regimes specifically allowing cross-border business, because their activity is not regarded as meeting threshold tests of continuity or regularity to be regarded as a deposit-taking business, because their activities are not regarded as taking deposits or other repayable funds ‘from the public’ or because they otherwise fall within national exemptions. Non-EU banks and other non-EU entities taking deposits or otherwise raising debt finance from EU creditors (other than EU banks and group companies) will need to consider how they are affected by the new restrictions on taking deposits or other repayable funds in the EU.
- ***EU entities holding bank accounts with non-EU banks***. Non-EU banks will need to re-evaluate the extent to which they can continue to provide banking services to EU customers in the light of the new regime under CRD6. However, even where a non-EU bank can rely on exemptions under CRD6 to provide basic account services involving deposit-taking or overdraft or other credit services, other restrictions may apply under national law to related services, such as restrictions on providing payment services or foreign exchange conversions.

- ***Custody services***. Non-EU entities providing custody services to EU clients may be regarded as taking deposits or other repayable funds or providing credit as part of the services. It may be unclear whether some providers of these services will be able to rely on the exemption for MiFID ancillary services.
- ***Increased regulatory scrutiny***. Non-EU entities may be subject to increased scrutiny of how they comply with the restrictions on cross-border business, in particular given the new reporting requirements that will apply to their EU bank affiliates and TCBs.

Although CRD6 will provide a limited degree of harmonisation, it will not completely end the 'patchwork' of differing national laws and regulations governing non-EU entities conducting cross-border business with EU clients and counterparties. Even where Member States fully implement the requirements of CRD6, non-EU entities may have to comply with additional requirements when conducting cross-border business in the EU.

## What should non-EU entities do now?

Although the new rules are not expected to apply until January 2027, non-EU entities that conduct cross-border business with clients or counterparties in the EU should evaluate the extent to which they are likely to be affected by national implementation of the new rules or other changes made by Member States to existing rules when implementing the new requirements and monitor the way in which Member States are implementing the new requirements. Non-EU entities that may need to cease conducting new cross-border business in Member States should consider the extent to which they may be able to rely on the provisions governing legacy contracts to run-off existing arrangements (and the need for early communication with EU clients on the impact of the changes on them).

Non-EU banks that consider that they will need to establish a new branch in the EU in advance of the date of application of the new rules may wish to seek authorisation for those branches under the existing national rules before the new rules for TCBs begin to apply so that they can take advantage of the permitted transitional arrangements if the Member State elects to apply those arrangements. Alternatively, they may decide to conduct the business through EU subsidiaries which benefit from the ability to passport into other Member States.

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