

**SUPERVISION MANUAL (PASSPORTING GUIDANCE)
INSTRUMENT 2003**

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) of the Financial Services and Markets Act 2000 (Guidance).

Commencement

- B. This instrument comes into force on 1 July 2003.

Amendments to the Supervision manual

- C. The Supervision manual is amended by inserting, as SUP App 3, the provisions in Annex A to this instrument.

Amendments to the Glossary

- D. The Glossary is amended in accordance with Annex B to this instrument.

Citation

- E. This instrument may be cited as the Supervision Manual (Passporting Guidance) Instrument 2003.

By order of the Board
15 May 2003

Annex A

Amendments to SUP

Appendix 3

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Guidance on passporting issues

3.1 Application

3.1.1 G This appendix applies to all *firms* when passporting.

3.2 Purpose

3.2.1 G The purpose of this appendix is to give *guidance*:

- (1) to *UK firms* on some of the issues that are involved in addressing the questions “What is a *branch*?” and “Where is a service provided?” (see *SUP App 3.5* (The right of establishment) and *SUP App 3.6* (Freedom to provide services));
- (2) to all *firms* on the relationship between *regulated activities* and activities passported under the *Single Market Directives* (see *SUP App 3.9* (Mapping of the Investment Services Directive and Banking Consolidation Directive to the Regulated Activities Order)).

This *guidance* refers to comments made by the European Commission. These comments do not themselves have the force of legislation (see *SUP App 3.3.5G* (Interpretative communications)).

3.3 Background

The Treaty establishing the European Community

3.3.1 G The European Community Treaty (the ‘*Treaty*’), as amended by later Treaties, established in EC law the rights of freedom of establishment and freedom to provide services in the European Community.

3.3.2 G The *Treaty* provides the framework for the provision of banking, insurance and investment business, while the *Single Market Directives* clarify the rights and freedoms within that framework.

EC and EEA

3.3.3 G The agreement on the *European Economic Area*, signed at Oporto on 2 May 1992, extends EC legislation to any *EEA State* that is not part of the European Community. Any references to an EC Member State in this appendix should, therefore, be read as referring to an *EEA State*.

Interpretative communications

3.3.4 G In 1997, the European Commission published an interpretative communication (Freedom to provide services and the interests of the general good in the Second Banking Directive (97/C 209/04)) (the text of this directive and the First Banking Directive is now consolidated in the *Banking*

Consolidation Directive). The European Commission's objective in publishing this communication was to explain and clarify the Community rules. The European Commission deemed it desirable "...to restate in a Communication the principles laid down by the Court of Justice and to set out its position regarding the application of these Principles to the specific problems raised by the Second Banking Directive".

- 3.3.5 G In 2000, the European Commission published a further interpretative communication (Freedom to provide services and the general good in the insurance sector (2000/C43/03)). This allowed the European Commission to publicise its own interpretation of the rules on the freedom to provide services.
- 3.3.6 G The European Commission has not produced a communication on the *Investment Services Directive*. It is arguable, however, that the principles in the communication on the Second Banking Directive can be applied to *investment services*. This is because article 11 of the *Investment Services Directive* (containing provisions relating to conduct of business rules) also applies to the *investment services* of *firms* operating under the *Banking Consolidation Directive*.
- 3.3.7 G In giving its views, communications made by the European Commission have the status of guidance and are not binding on the national courts of *EEA States*. This is because it is the European Court of Justice that has ultimate responsibility for interpreting the *Treaty* and secondary legislation. Accordingly, the communications "...do not prejudge the interpretation that the Court of Justice of the European Communities, which is responsible in the final instance for interpreting the *Treaty* and secondary legislation, might place on the matter at issue." (European Commission interpretative communication: Freedom to provide services and the general good in the insurance sector (C(99) 5046). However, the Courts may take account of European Commission communications when interpreting the *Treaty* and secondary legislation.
- 3.3.8 G *Firms* should also note that European Commission communications do not necessarily represent the views taken by all *EEA States*.

E-commerce

- 3.3.9 G The *E-Commerce Directive* covers services provided at a distance by means of electronic equipment for the processing (including digital compression) and storage of data. The services would normally be provided in return for remuneration and must be provided at the individual request of a recipient (see recital 17 of the *E-Commerce Directive*). The Directive implements the *country of origin* approach to regulation. This approach makes *firms* subject to the conduct of business requirements of the *EEA State* from which the service is provided. This is subject to certain derogations (see *SUP App 3.3.11G*).
- 3.3.10 G The *E-Commerce Directive* does not affect the responsibilities of *Home*

States under the *Single Market Directives*. This includes the obligation of a *Home State regulator* to notify the *Host State regulator* of a *firm's* intention to establish a *branch* in, or provide *cross border services* into, the other *EEA State*.

3.3.11 G There are, however, general derogations from the internal market provisions under article 3(3) of the *E-Commerce Directive*. The derogations include consumer contracts, the permissibility of unsolicited e-mail and certain insurance services (both life and non-life). Where these derogations apply, the *EEA States* in which the recipients of the service are based may continue to be able to impose their own requirements.

3.3.12 G Further details concerning the impact of the *E-Commerce Directive* on *UK firms* are available in *ECO*.

3.4 Introduction

3.4.1 G The *Treaty* lays down central principles governing the legal framework for freedom of establishment and the free movement of services in the European Community. There are, however, a number of areas where the legal position is not clear. This includes, for example, identifying whether a service is provided through an establishment, where the issues involved are complex. Therefore, this Appendix is intended to provide *guidance* but cannot be regarded as comprehensive. Ultimately, the construction of the *Treaty* and relevant Directive provisions is a matter for the European Court of Justice.

3.4.2 G *SUP 13.5* (Notices of intention) sets out the notification requirements for a *firm* seeking to establish a *branch* or provide *cross border services*. As *firms* will note, the decision whether a passport notification needs to be made will be a matter of interpretation. The onus is on *firms* to comply with the requirements of the *Act* and, where relevant, the laws of other *EEA States*. So, in cases of doubt, *firms* should obtain their own legal advice on the specific issues involved.

3.4.3 G Blanket notification is the practice of the *Home State regulator* notifying all *Host State regulators* in respect of all activities regardless of any genuine intention to carry on the activity. This practice is discouraged by the *FSA*. However, a *firm* may be carrying on activities in the *United Kingdom* or elsewhere in a way that necessarily gives rise to a real possibility of the provision of services in other *EEA States*. In such cases, the *firm* should consider with its advisers whether it should notify the relevant authorities and include that possibility in its business plan.

3.5 The right of establishment

3.5.1 G Article 43 (formerly 52) of the *Treaty* grants nationals of an *EEA State* the right to establish themselves in another *EEA State* and, if they are already established in one *EEA State*, to set up agencies, branches or subsidiaries in any other *EEA State*.

Permanent nature of presence in a Host State

- 3.5.2 G The right of establishment assumes a non-temporary presence in the *Host State*.
- 3.5.3 G The European Commission has issued statements about the treatment of a *credit institution* or *insurance undertaking* that maintains a permanent presence in the *EEA State* in which it provides services. It has stated that such an institution or undertaking comes, in principle, under the *Treaty* provisions on the right of establishment. The European Court of Justice has ruled that: "A national of a Member State who pursues a professional activity on a stable and continuous basis in another Member State where he holds himself out from an established professional base to, amongst others, nationals of that State, comes under the provisions of the...right of establishment, and not those...relating to services" (Case C-55/94 Gebhard [1995] ECR I-4165). The European Commission has also indicated that a banking activity exercised within a territory in a durable, frequent or continuous manner by a *credit institution* exercising the freedom to provide services, may fall under the right of establishment.
- 3.5.4 G On the basis of previous cases, the European Commission's view is that:
- (1) a *credit institution* or *insurance undertaking* may be working within the territory of an *EEA State* in order to carry out a limited number of tasks in connection with existing customers. Such a *credit institution* or *insurance undertaking* could have the infrastructure necessary to perform these tasks without being deemed to be 'established' within the meaning laid down in Community law;
 - (2) if, however, the *credit institution* or *insurance undertaking* went beyond the limited number of tasks referred to in (1), it could fall within the scope of the right of establishment. This may arise if, for example, it were to approach nationals of the *Host State* offering banking services in the same way as a *branch* would do.

Definition of 'branch'

- 3.5.5 G The *Single Market Directives* state the following about the meaning of "branch":
- (1) Article 1 of the *Banking Consolidation Directive* provides that a *branch* is "... a place of business which forms a legally dependent part of a credit institution and which carries out directly all or some of the transactions inherent in the business of credit institutions...".
 - (2) Article 1 of the *Investment Services Directive* provides that a branch is "...a place of business which is a part of an investment firm, which has no legal personality and which provides investment services for which the investment firm has been authorised...".

- (3) Article 1 of the *Consolidated Life Directive* and Article 3 of the *Second Non-Life Directive* provide that "...any permanent presence of an undertaking in the territory of a Member State shall be treated in the same way as an agency or branch, even if that presence does not take the form of a branch or agency, but consists merely of an office managed by the undertaking's own staff or by a person who is independent but has permanent authority to act for the undertaking as an agency would."

3.5.6 G The *Single Market Directives* state that all a *firm's* places of business in any particular *EEA State* are treated as a single branch. So, once a *firm* has satisfied the conditions for establishing a branch in another *EEA State* as referred to in *SUP* 13.5.1G (Specified contents: notice of intention to establish a branch), there is no requirement to follow these procedures in respect of the establishment of further places of business in that same *EEA State*. It should be noted that different principles may apply in respect of the overseas territories of some *EEA States*. *Firms* should also note that changes to a *firm's* places of business are likely to result in changes to the *firm's* requisite details (see *SUP* 13.6 (Changes to branches)). With regard to the position in Gibraltar, *firms* should be aware of the requirements of the Financial Services and Markets (Gibraltar) Order 2001 (2001/3084).

Use of an intermediary or independent person: branches

3.5.7 G The European Court of Justice has held that, if a *firm* has access to an independent *person* or intermediary established in the territory of an *EEA State*, it may fall within the rules on the right of establishment. This applies if the *firm* maintains the access so as to carry on activities in that *EEA State* on a stable and continuous basis. The European Court of Justice has ruled that:

- (1) "...an insurance undertaking of another Member State which maintains a permanent presence in the Member State in question comes within the scope of the Treaty on the right of establishment, even if that presence does not take the form of a branch or agency, but consists merely of an office managed by the undertaking's own staff or by a person who is independent but authorised to act on a permanent basis for the undertaking, as will be the case with an agency." (Case 205/84 *Commission v Germany* [1986] ECR 3755).

- (2) "One of the essential characteristics of the concepts of branch or agency is the fact of being subject to the direction and control of the parent body." (the *De Bloos* case (Case 14/76 [1976] ECR 1459)).

3.5.8 G The European Court of Justice has held that "The concept of branch, agency or other establishment implies a place of business which has the appearance of permanency, such as the extension of a parent body, has a management and is materially equipped to negotiate business with third parties, so that the latter, although knowing that there will, if necessary, be a legal link with the parent body, the head office of which is abroad, do not have to deal directly with

such parent body but may transact business at the place of business constituting the extension.” (the Somafer case (Case 33/78 [1978] ECR 2183)).

- 3.5.9 G The European Commission considers that, for the use of an intermediary or independent *person* to result in a *firm* possibly falling within the scope of the right of establishment, three criteria must be met. These criteria are as follows:
- (1) the intermediary or independent *person* must have received a permanent mandate or brief which must:
 - (a) be long-term and continuous and not be limited in time or be a one-off instruction; and
 - (b) relate to the activities that are part of the *insurance undertaking*'s or *credit institution*'s objectives;
 - (2) the intermediary or independent *person* must be subject to the direction (in the case of insurance) or management (in the case of banking) and control of the *credit institution* or *insurance undertaking* he represents. The European Commission believes that "an exclusive brief received by an independent intermediary from a single insurer is an indication that the intermediary is subject to the direction and control of that insurer". To ascertain if this condition is met, a check should be made, in particular, to:
 - (a) see whether the intermediary or independent *person* is free to organise his or her own work and to decide what proportion of time to devote to the *credit institution* or *insurance undertaking*; and
 - (b) consider whether the *intermediary* or independent *person* can represent competitors or is bound by an exclusive agreement;
 - (3) the *intermediary* or independent *person* must be able to commit the *credit institution* or *insurance undertaking*. To satisfy this condition the following will apply:
 - (a) the acts or decisions of the intermediary or independent *person* must be able to commit the *insurance undertaking* or *credit institution* in transactions with third parties, as determined in the case law of the European Court;
 - (b) the intention on the part of the *insurance undertaking* or *credit institution* to be directly committed may also be shown by the intermediary or independent *person*'s brief;
 - (c) the intermediary or independent *person* can make a complete offer on behalf of a *credit institution* or *insurance undertaking*

even if only the *credit institution* or *insurance undertaking* can sign the contract. This condition is not met if the *credit institution* or *insurance undertaking* can reject the proposal or refuse to sign the contract.

3.5.10 G The European Commission has stated in its communications that, if the use of an intermediary or independent *person* results in a *credit institution* or *insurance undertaking* falling within the scope of the right of establishment, the *person* would not constitute a *branch* because it is independent and not part of the *firm's* business (see SUP App 3.5.5G (Definition of branch)). However, in such cases, a passporting notification would be required.

3.5.11 G If an *insurance undertaking* provides services within the territory of another *EEA State* under the freedom to provide services, the European Commission has indicated that it can use the services of independent *persons* in that *EEA State* without falling within the scope of the right of establishment. It has also indicated that this can be either upstream or downstream of the transaction without establishing a *branch*. Examples include:

- (1) local experts who assess the risks to be covered but who do not conclude *contracts of insurance* and whose activity is limited to forwarding insurance proposals;
- (2) local medical services;
- (3) a permanent structure for collecting premiums or receiving notices of claims;
- (4) canvassers who do not conclude *contracts of insurance* and whose activity is limited to forwarding insurance proposals.

Where local experts conclude claims settlements, they may be regarded as performing activities falling within the scope of establishment.

3.5.12 G In the case of *credit institutions*, the European Commission has also indicated that marketing services through an intermediary that is itself a *credit institution* should not require prior notification as the intermediary will be supervised in its activities by its *Home State*.

Automatic telling machines as a branch

3.5.13 G Automatic telling machines (ATMs) capable of performing the banking or insurance activities listed in the *Single Market Directives* may form the only presence of a *credit institution* or *insurance undertaking* in a Member State. The European Commission considers that, where this is the case, they are unlikely to be covered by the right of establishment. The *FSA* considers that ATMs can only be considered to be an establishment if the three criteria referred to in SUP App 3.5.9G (Use of an intermediary or independent person) are satisfied to the extent that they apply to a *credit institution* or an *insurance undertaking*.

3.6 Freedom to provide services

3.6.1 G Article 49 (Services) (formerly article 59) of the *Treaty* grants to EC nationals established in one *EEA State* the freedom to provide *cross border services* to the nationals of other *EEA States*.

How services may be provided

3.6.2 G Under the *Treaty*, the freedom to provide services within the EC may be exercised in three broad ways:

- (1) where the provider of a service moves temporarily to another *EEA State* in order to provide the service;
- (2) where the service is provided without either the provider or the recipient moving (in this situation the provision, and receipt, of the service may take place by post, telephone or fax, through computer terminals or by other means of remote control);
- (3) where the recipient of a service moves temporarily to another *EEA State* in order to receive (or, perhaps, commission the receipt of) the service within that State.

3.6.3 G Under the *Single Market Directives*, however, *EEA rights* for the provision of services are concerned only with services provided in one of the ways referred to in *SUP App 3.6.2G* (1) and (2) (How services may be provided).

Notification

3.6.4 G The *Single Market Directives* require *credit institutions*, *insurance undertakings* and *investment firms* to make a notification to the *Home State* before providing *cross border services* into the *Host State's* territory for the first time under the freedom to provide services.

Place of supply

3.6.5 G In the opinion of the European Commission (and in the wording of the *Single Market Directives*) "only activities carried on within the territory of another Member State should be the subject of prior notification" (Commission interpretative communication: Freedom to provide services and the interests of the general good in the Second Banking Directive (97/C 209/04)). In determining, for the purposes of notification, whether a service is to be provided 'within' another *EEA State*, it is necessary to determine the place of supply of the service.

3.6.6 G An *insurance undertaking* that effects *contracts of insurance* covering risks or commitments situated in another *EEA State* should comply with the notification procedures for the provision of services within that *EEA State*.

The location of risks and commitments is found by reference to the rules set out in paragraph 6 of schedule 12 to the *Act*, which derive from article 1 of the *Consolidated Life Directive* and article 2 of the *Second Non-Life Directive*. It may be appropriate for insurers to take legal advice as to how these rules are interpreted and applied in other *EEA States*. The need to passport may arise because of only one of the risks covered by an insurance policy. This includes, for example, where a policy covers a number of property risks and one of those properties is in another *Member State*.

- 3.6.7 G In respect of banking services, the European Commission believes that "...to determine where the activity was carried on, the place of provision of what may be termed the 'characteristic performance' of the service i.e. the essential supply for which payment is due, must be determined" (Commission interpretative communication: Freedom to provide services and the interests of the general good in the Second Banking Directive (97/C 209/04)). In the *FSA's* view, this requires consideration of where the service is carried out in practice.
- 3.6.8 G The *FSA* is of the opinion that *UK firms* that are *credit institutions* and *ISD investment firms* should apply the 'characteristic performance' test (as referred to in *AUTH* 3.6.7G) when considering whether prior notification is required for services business. *Firms* should note that other *EEA States* may take a different view. Some *EEA States* may apply a solicitation test. This is a test as to whether it is the consumer or the provider that initiates the business relationship.
- 3.6.9 G In the case of a *UK firm* conducting portfolio management, for example, this would mean looking at where the investment decisions and management are actually carried on in order to determine where the service is undertaken. Similarly, a *UK stockbroker* that receives orders by telephone from a customer in France for execution on a *UK exchange* may be deemed to be dealing or receiving and transmitting orders within the territory of the *United Kingdom*. In such a case, whether the *firm* solicited the overseas investor would be irrelevant.
- 3.6.10 G Where, however, a *credit institution* or *ISD investment firm*:
- (1) intends to send a member of staff or a temporarily authorised intermediary to the territory of another *EEA State* on a temporary basis to provide financial services; or
 - (2) provides advice, of the type that requires notification under either the *Investment Services Directive* or the *Banking Coordination Directive*, to customers in another *EEA State*;
- the *firm* should make a prior notification under the freedom to provide services.

Temporary activities

3.6.11 G The key distinction in relation to temporary activities is whether a *firm* should make its notification under the freedom of establishment in a *Host State*, or whether it should notify under the freedom to provide services into a *Host State*. It would be inappropriate to discuss such a complex issue in *guidance* of this nature. It is recommended that, where a *firm* is unclear on the distinction, it should seek appropriate advice. In either case, where a *firm* is carrying on activities in another *Member State* under a *Single Market Directive*, it should make a notification.

3.6.12 G The European Commission has made the following statements on the subject of temporary activities:

- (1) "...the fact of temporarily visiting the territory of a Member State to carry on an activity preceding (e.g. survey of property prior to granting a loan) or following (incidental activities) the essential activity does not, in the Commission's view, constitute a situation that is liable in itself to be the subject of prior notification. The same is true of any visits which a credit institution may pay to a customer if such visits do not involve the provision of the characteristic performance of the service that is the subject of the contractual relationship.";
- (2) "...temporarily visiting the territory of a Member State to conclude contracts, prior to the exercise of a banking activity should not be regarded as exercising the activity itself.";
- (3) "...if the service is supplied to a beneficiary who has gone in person for the purpose of receiving that service, to the Member State where the institution is established, prior notification should not take place."

3.6.13 G If, however, the *credit institution* sends a member of staff or a temporarily authorised intermediary to the territory of another *EEA State* to provide the 'characteristic performance' of banking services to its non-resident customers, the European Commission believes that prior notification is necessary.

Non-resident customers of banks

3.6.14 G The European Commission is of the opinion that "a bank may have non-resident customers without necessarily pursuing the activities concerned within the territory of the Member State where the customers have their domicile" (Commission interpretative communication: Freedom to provide services and the interests of the general good in the Second Banking Directive (97/C 209/04)).

Monitoring procedures

3.6.15 G The *FSA* considers that, in order to comply with *Principle 3: Management and control* (see *PRIN 2.1.1R*), a *firm* should have appropriate procedures to monitor the nature of the services provided to its customers. Where a *UK firm* has non-resident customers but has not notified the *EEA*

State in which the customers are resident that it wishes to exercise its freedom to provide services, the *FSA* would expect the *firm's* systems to include appropriate controls. Such controls would include procedures to prevent the supply of services covered by the *Single Market Directives* in the *EEA State* in which the customers are resident if a notification has not been made and it is proposed to provide services otherwise than by remote communication. In respect of *insurance business*, the *insurer's* records should identify the location of the risk at the time the policy is taken out or last renewed. That will, in most cases, remain the location of the risk thereafter, even if, for example, the *policyholder* changes his habitual residence after that time.

Remote communication

3.6.16 G In respect of banking services, the European Commission stated in its interpretative communication: Freedom to provide services and the interests of the general good in the Second Banking Directive (97/C 209/04) that:

"The provision of distance banking services, for example via the Internet, should not, in the European Commission's view, require prior notification, since the supplier cannot be deemed to be pursuing its activities in the customer's territory". This is because, as stated in *SUP App 3.5.7G* (Use of an intermediary or independent person), the European Commission believes that banking services are deemed to be provided where the 'characteristic performance' of the service is carried out, that is, where the service is carried out in practice. The European Commission notes, however, that "as long as the Court has not ruled on this issue, any credit institution is at liberty to choose, for reasons of legal certainty, to make use of the notification procedures provided for in the Second Banking Directive even if, according to the criteria proposed above, notification may not be necessary".

3.6.17 G In respect of *insurance business*, the European Commission, in its interpretative communication: Freedom to provide services and the general good in the insurance sector (2000/C 43/03), stated that:

- (1) "The use of remote means of communication (telephone, fax the press etc) and in particular electronic commerce (e.g. via the Internet) to conclude insurance policies covering a risk (or commitment) situated in a Member State other than the Member State of establishment of an insurer should be regarded as insurance business carried on under the freedom to provide services with no movement on the part of the contracting parties.";
- (2) "...the place where the technological means used for providing the service are located (e.g. where the Internet server is installed)" may not be relevant in determining the Member State of establishment of the *insurance undertaking* concluding a policy by remote means which will be its head office or branch; and
- (3) "...an insurance undertaking operating from one EC State which is prepared to conclude via the Internet contracts of insurance covering risks or commitments situated in other EC States will probably be

required to comply with the notification procedures for the provision of services."

- 3.6.18 G However, the European Commission has also stated in its interpretative communication: Freedom to provide services and the general good in the insurance sector (2000/C 43/03) that:
- (1) "...the use of electronic commerce methods for the sole purposes of advertising, providing commercial information or enhancing awareness of the insurance undertaking cannot be regarded as an insurance activity;" and
 - (2) "... it is out of the question to make such advertising and information activities subject to the notification procedures laid down by the Third Directives (Article 34 and following) which was designed for actual insurance activities carried on under the freedom to provide services."
- 3.6.19 G The *FSA*, therefore, believes that a notification is required only where there is an intention to provide the services themselves within the territory of the other *EEA State*.
- 3.6.20 G However, the *E-Commerce Directive* (see *SUP App 3.3.10G* (E-commerce)), which came into force in January 2002, has an effect on this matter. This Directive provides that, subject to certain limited derogations, the *country of origin* regulates e-commerce services.

Automatic telling machines : provision of services

- 3.6.21 G If a fixed automatic telling machine , capable of performing banking or insurance activities, is the only presence of a *credit institution* or *insurance undertaking* in an *EEA State*, the European Commission believes that "...it may be possible to treat it as a provision of services in the territory of that Member State." This right exists, according to the European Commission, regardless of the presence of a *person* or *company* in the *EEA State* responsible for equipping it or dealing with technical problems.

Use of an intermediary or independent person: freedom to provide services

- 3.6.22 G The European Commission's view is that, if a bank uses an intermediary to provide temporary or occasional banking services within the territory of an *EEA State*, it must first give notification under the freedom to provide services.
- 3.6.23 G Where the duties of an intermediary consist only of seeking customers for a *credit institution*, however, the European Commission believes that the *credit institution* cannot be considered to be necessarily intending to carry on its activities in the territory of the *EEA State*. So, notification may not be required. However, *UK firms* should note that some *EEA States* do not take this view. Therefore, *UK credit institutions* should confirm the position with

the relevant *Host State regulator* before engaging an intermediary in that *EEA State* to seek customers.

- 3.6.24 G In respect of *insurance undertakings*, examples of the use of independent *persons* which, in the European Commission's view, may fall under the freedom to provide services, include situations where:
- (1) the independent *person* works for an *insurance undertaking* which has not given him an exclusive brief (even if another *insurance undertaking* has given the independent *person* an exclusive brief in respect of certain other *classes* of insurance); or
 - (2) the independent *person* negotiates contacts with customers if those contracts can be rejected by the *insurance undertaking*.

Membership of regulated markets

- 3.6.25 G The *FSA* is of the opinion that where a *UK firm* becomes a member of a *regulated market* that has its registered office or, if it has no registered office, its head office, in another *EEA State*, the same principles as in the 'characteristic performance' test should apply. Under this test, the fact that a *UK firm* has a screen displaying the exchange's prices in its *UK office* does not mean that it is dealing within the territory of the *Home State* of the *regulated market*.
- 3.6.26 G *Firms* are reminded of their rights, under article 15(1) of the *Investment Services Directive*, to become members of, or have access to, the *regulated markets* in other *Member States*.
- 3.6.27 G *Firms* should note that, in circumstances where the *FSA* takes the view that a notification would not be required, other *EEA States* may take a different view.

Financial promotion

- 3.6.28G In relation to the need for a *credit institution* to notify where its advertising is available to *persons* in a particular *Member State*, the European Commission, in its interpretative communication (Freedom to provide services and the interests of the general good in the Second Banking Directive (97/C 209/04)), stated that:
- (1) "the prior existence of advertising or an offer cannot be linked with the need to comply with the notification procedure"; However the existence of an advertisement may indicate that there is an intention to provide services which would trigger the need for notification;
 - (2) "canvassing customers from a distance does not necessarily mean that an institution plans to provide services within the territory of another *Member State*."

- 3.6.29 G The European Commission's rationale for the views referred to in *SUP App* 3.6.28G (1) and (2) is that "...for the sake of simplicity and in keeping with the Second Directive, all forms of advertising, targeted or otherwise, and all offers of service made at a distance by any means whatsoever (e.g. post, fax, electronic mail) should be exempt from the requirements of prior notification. Only if a credit institution plans to carry on its activities within the territory of the customer's country under the freedom to provide services... will it be obliged to notify" (Commission interpretative communication: Freedom to provide services and the general good in the insurance sector' (2000/C 43/03).
- 3.6.30 G In relation to *insurance undertakings*, the European Commission has expressed the view that "... in accordance with the Third Directives, all forms of advertising by whatever means (mail, fax, electronic mail etc) should not be subject to the notification procedures referred to in Article 34 et seq. of the Third Directives. It is only if the insurance undertaking plans to carry on insurance activities under the freedom to provide services and only if it offers insurance products to potential clients established in another Member State that it must comply with the notification procedure." (Commission interpretative communication: Freedom to provide services and the general good in the insurance sector (2000/C 43/03).
- 3.6.31 G The European Commission has not expressed a view about the circumstances where notification may be needed where *investment firms* advertise in other Member States. In the *FSA's* opinion, the European Commission's views on the need for *credit institutions* and *insurance undertakings* to notify their intention to provide services in another *Member State* can be applied, in general terms, to *investment firms*. However, given the broad range of activities covered by the *Investment Services Directive*, due account may need to be taken of the particular circumstances in which the *investment firm's* advertisements are made available to *persons* in the *United Kingdom*. In this respect, it is notable that there is no concept under the *Regulated Activities Order* of offering to carry on a *regulated activity* being a *regulated activity* in its own right. This is a change to the earlier position under the Financial Services Act 1986. This change seems consistent with the fact that overseas *investment firms* may be able to make their advertisements available to *persons* in the *United Kingdom* without needing to notify under the *Investment Services Directive*.

3.7 Simultaneous exercise of the freedom to provide services and the right of establishment

- 3.7.1 G The European Commission believes that a *credit institution*, an *investment firm* or an *insurance undertaking* can simultaneously carry on business in the same *EEA State* under the freedom to provide services and under the right of establishment. This is so, even where the same activity is involved. Separate notifications should be made for each. The *credit institution*, *investment firm* or *insurance undertaking* should be able to link the activity concerned to either the right of establishment or to the freedom to provide services.

3.8 Avoidance

- 3.8.1 G The European Commission has stated that "it should be ensured that an institution is not able artificially to connect its activities to the arrangements governing freedom to provide services as a way of side-stepping the legal and tax framework which would apply in the same activity were considered to be carried on by a branch or by any other form of establishment" (Commission interpretative communication: Freedom to provide services and the interests of the general good in the Second Banking Directive' (97/C 209/04)).
- 3.8.2 G The European Court has also acknowledged that, in certain circumstances, an *EEA State* "is entitled to take steps to prevent a service provider...from exercising the freedom to provide services...". The circumstances are where "a service provider whose activity is entirely or mainly directed towards its territory, but who has become established in another Member State in order to circumvent the rules of professional conduct that would apply to him if he were established in the territory of the State where he entirely or mainly pursues his activities..." (Commission interpretative communication: Freedom to provide services and the interests of the general good in the Second Banking Directive (97/C 209/04)).

3.9 Mapping of the Investment Services Directive and Banking Consolidation Directive to the Regulated Activities Order

- 3.9.1 G The following Tables 1 and 2 provide an outline of the *regulated activities* and *specified investments* that may be of relevance to *firms* considering undertaking *passported activities* under the *Banking Consolidation Directive* or the *Investment Services Directive*. The tables may be of assistance to *UK firms* that are thinking of offering financial services in another *EEA State* and to *EEA firms* that may offer those services in the *United Kingdom*.
- 3.9.2 G The tables provide a general indication of the *investments* and activities specified in the *Regulated Activities Order* that may correspond to categories provided for in either the *Banking Consolidation Directive* or the *Investment Services Directive*. The *guidance* does not cover the *UCITS Directive*. The tables do not provide definitive *guidance* as to whether a *firm* is carrying on an activity that is capable of being passported, nor do the tables take account of exceptions that remove the effect of articles. Whether a *firm* is carrying on a *passported activity* will depend on the particular circumstances of the *firm*. If a *firm's* activities give rise to potential passporting issues, it should obtain specialist advice on the relevant issues.
- 3.9.3 G In considering the issues raised in the tables, *firms* should note that:
- (1) article 64 of the *Regulated Activities Order* (Agreeing to carry on specific kinds of activity) applies in respect of agreeing to undertake the specified activity; and

- (2) article 89 of the *Regulated Activities Order* (Rights to or interests in investments) applies in respect of rights to and interests in the types of *investments* to which the category applies.

Table 1: BCD activities		Part II RAO Activities	Part III RAO Investments
1.	Acceptance of deposits and other repayable funds from the public	Article 5	Article 74
2.	Lending	Article 61, 64	Article 88
3.	Financial leasing		
4.	Money transmission services		
5.	Issuing and administering means of payment (eg credit cards, travellers' cheques and bankers' drafts)		
6.	Guarantees and commitments		
7.	Trading for own account or for account of customers in: (a) money market instruments (b) foreign exchange (c) financial futures and options (d) exchange and interest rate instruments (e) transferable securities	Article 14, 21, 25 (see Note 1), 64 Article 14, 21, 25, 64 Article 14, 21, 25, 64 Article 14, 21, 25, 64 Article 14, 21, 25, 64	Article 77, 78, 80, 83-85, 89 Article 83-85, 89 Article 83-85, 89 Article 83-85, 89 Article 76-81, 89
8.	Participation in share issues and the provision of services relating to such issues	Article 14, 21, 25, 53, 64	Article 76-81, 89
9.	Advice to undertakings on capital structure, industrial strategy and related questions and advice and services relating to mergers and the purchase of undertakings	Article 14, 21, 25, 53, 64	Article 76-80, 83-85, 89
10.	Money broking	Article 25, 64	Article 77, 78, 89
11.	Portfolio management and advice	Article 14, 21, 25, 37, 53, 64	Article 76-81, 83-85, 89

12.	Safekeeping and administration of securities	Article 40, 45, 64	Article 76-81, 83-85, 89
13.	Credit reference services		
14.	Safe custody services	Article 64	Article 76-81, 83-85, 89

Note 1. The *BCD* activity of trading for account of customers does not extend to the *regulated activity* of making arrangements with a view to transactions in investments under article 25(2) of the *Regulated Activities Order* unless the arrangements bring about or would bring about particular transactions.

Table 2: ISD activities		Part II RAO Activities	Part III RAO Investments
	1. Core services		
1.	(a) Reception and transmission, on behalf of investors, of orders in relation to one or more of the relevant instruments	Article 25 (see Note 1), 64	Article 76-81, 83-85, 89
	(b) Execution of such orders other than for own account	Article 21, 64	Article 76-81, 83-85, 89
2.	Dealing in any of the relevant instruments for own account	Article 14, 64	Article 76-81, 83-85, 89
3.	Managing portfolios of investments in accordance with mandates given by investors on a discretionary, client-by-client basis where such portfolios include one or more of the relevant instruments	Article 14, 21, 25, 37, 53, 64	Article 76-81, 83-85, 89
4.	Underwriting in respect of issues of any of the relevant instruments and/or the placing of such issues	Article 14, 21, 25, 64	Article 76-81, 83-85, 89
	2. Non-core services		
1.	Safekeeping and administration services	Article 40, 45, 64	Article 76-81, 89
2.	Safe custody services		
3.	Granting credits or loans to an investor to allow him to carry out a transaction in one or more of the relevant instruments where the firm granting the credit or loan is involved		

4.	Advice to undertakings on capital structure, industrial matters and advice and services relating to mergers and the purchase of undertakings	Article 14, 21, 25, 53, 64	Article 76-80, 83-85, 89
5.	Services related to underwriting	Article 25, 53, 64	Article 76-81, 83-85, 89
6.	Investment advice concerning one or more of the relevant instruments	Article 53, 64	Article 76-81, 83-85, 89
7.	Foreign exchange services where these are connected with the provision of investment services	Article 14, 21, 25, 53, 64	Article 83-85, 89

Note 1. The *ISD* activity of receiving and transmitting orders does not extend to the *regulated activity of making arrangements with a view to transactions in investments* under article 25(2) of the *Regulated Activities Order* unless the arrangements bring about or would bring about particular transactions. This is the case, whether or not the bringing about arises or would arise as a result of the *person* who makes the arrangements receiving and transmitting orders in relation to particular transactions or in any other way.

3.10 Mapping of Insurance Directives to the Regulated Activities Order

Introduction

3.10.1 G The *guidance* in *AUTH* 3.10 and Table 3 describes in broad outline the relationship between:

- (1) the insurance-related *regulated activities* specified in the *Regulated Activities Order*; and
- (2) the activities within the scope of the *Insurance Directives*.

3.10.2 G This is a guide only and should not be used as a substitute for legal advice in individual cases.

Table 3: Insurance Directive activities		Part II RAO Activities	Part III RAO Investments
3. Non-life Insurance Directive activities			
1.	Taking up and carrying on direct non-life insurance business	Article 10	Article 75
2.	Classes 1 to 18 of direct non-life insurance business in Point A of the Annex to the First Directive		Corresponding paragraphs 1 to 18 of Schedule 1, Part I

	2. Consolidated Life Directive activities		
1.	Taking up and carrying on direct life insurance business	Article 10	Article 75
2.	Classes I to IX of direct life insurance business in the Annex 1 to the Consolidated Life Directive		Corresponding paragraphs I to IX of Schedule 1, Part II
	It will normally be the case that the activities of taking up and carrying on direct non-life or life insurance business will also embrace the activity of accepting deposits	Article 5	Article 74

Meaning of contract of insurance

3.10.3 G The meaning of *contract of insurance* is set out in article 3(1) of the *Regulated*

Activities Order (Interpretation). It does not include benefit-in-kind funeral plans, which are specified in article 60 of the *Regulated Activities Order* (plans covered by insurance or trust arrangements). Such funeral plans (to the extent that they are insurance) are also excluded from the *Insurance Directives*. It covers some contracts which might not otherwise be viewed as insurance in the *United Kingdom* (for example, contracts of guarantee). These contracts are also governed by the *Insurance Directives*. For the purpose of the *Regulated Activities Order*, a *contract of insurance* includes a contract of reinsurance as well as a contract of direct insurance.

The Insurance Directives

3.10.4 G Article 1 of the *First Non-Life Directive* and article 2 of the *Consolidated Life Directive* provides that the Directives "concern the taking up and pursuit of the self-employed activity of direct insurance". By contrast, article 10 of the *Regulated Activities Order* (Effecting and carrying out contracts of insurance) also covers reinsurance.

3.10.5 G Articles 2, 3 and 4 of the *First Non-Life Directive* and *article 3 of the Consolidated Life Directive* set out certain exclusions by reference to:

- (1) types of insurance;
- (2) types of insurer;
- (3) particular conditions under which insurance activities are carried out;
- (4) annual income; and

(5) particular identified institutions.

- 3.10.6 G Some of the exclusions referred to in *SUP* App 3.11.2G mirror exclusions in the *Regulated Activities Order*. So, the exclusion for breakdown insurance in article 2(3) of the *First Non-Life Directive* is matched by a slightly narrower exclusion in article 12 of the *Regulated Activities Order* (Breakdown insurance). The separate treatment of benefit-in-kind funeral plans under the *Regulated Activities Order* (see *SUP* App 3.10.4G) is matched by their exclusion on a slightly wider basis in article 3(5) of the *Consolidated Life Directive*. Other requirements from these Directives are also excluded from regulation by the *Exemption Order*.
- 3.10.7 G Most of the exclusions under the Directives, however, are not excluded from being *regulated activities*. For example, article 3 of the *Consolidated Life Directive* and article 3 of the *Non-Life Directive* exclude certain mutual associations whose annual contribution income falls below a defined threshold. In the *United Kingdom*, these include certain smaller *friendly societies* commonly referred to as "*non-directive friendly societies*". The activities of such societies are regulated under the *Act*, on a "lighter basis" than the activities of other insurers.

Territorial scope of the Regulated Activities Order and the Directives

- 3.10.8 G Under the *Act* and the *Regulated Activities Order*, the activities of *effecting and carrying out contracts of insurance* are treated as being carried on in the *United Kingdom* on the basis of legal tests under which the location of the risk is only one factor. If the risk is located in the *United Kingdom*, then (other relevant factors being taken into account) the activity will, in the vast majority of cases, also be viewed as carried on in the *United Kingdom*. There are exceptions, however, and overseas insurers may insure risks in the *United Kingdom* without carrying on business here and so without requiring to be regulated (although the *financial promotion* regime may apply). By contrast, under the Directives, the responsibility, as between *EEA States*, for regulating the conduct of passported insurance services is determined by reference to the location of the risk or commitment, as defined in article 1 of the *Consolidated Life Directive* and article 2 of the *Second Non-Life Directive*.
- 3.10.9G So, the effect of *SUP* App 3.12.1G is that an *insurer* may be carrying on *insurance business* in the *United Kingdom* which is to be treated as a *regulated activity* under article 10 to the *Regulated Activities Order* (Effecting and carrying out contracts of insurance) in circumstances where the risks covered are treated as located in another *EEA State*. In that event, the *insurer* is required by Schedule 3 to the *Act* to passport into the State concerned and may be subject to conduct of business requirements in that State (see *SUP* 13.10 (Applicable provisions)).
- 3.10.10G An *insurer* authorised in another *EEA State* who is insuring *UK* risks and so passports on a services basis under the *Insurance Directives* into the *United Kingdom* (see *SUP* App 3.12.1 G), may not be carrying on a *regulated activity*

in the *United Kingdom*. But, if it passports into the *United Kingdom*, it will qualify for *authorisation* under paragraph 12 of Schedule 3 to the *Act* (Firms qualifying for authorisation). Where this is the case, the *insurer* will be subject to conduct of business requirements in the *United Kingdom* (see *AUTH 5.6* (Which rules will an incoming EEA firm be subject to?)).

Activities carried on by incoming EEA firms in connection with insurance business.

3.10.11G Although the *Insurance Directives* are concerned with the *regulated activities* of *effecting and carrying out contracts of insurance*, an *incoming EEA firm* passported under the *Consolidated Life Directive* will be entitled to carry on certain other *regulated activities* without the need for *top-up permission*. This is where the *regulated activities* are carried on for the purposes of or in connection with the *incoming EEA Firm's insurance business*. These *regulated activities* may include:

- (1) *dealing in investments as principal;*
- (2) *dealing in investments as agent;*
- (3) *arranging (bringing about) deals in investments;*
- (4) *making arrangements with a view to transactions in investments;*
- (5) *managing investments;*
- (6) *safeguarding and administering investments;*
- (7) *advising on investments;*
- (8) *agreeing to carry on a regulated activity* of the above kind.

Financial promotion

3.10.12G The *financial promotion* regime under section 21 of the *Act* (Restrictions on financial promotion) may also apply to *EEA insurance undertakings* regardless of whether they carry on a *regulated activity* in the *United Kingdom* or passport into the *United Kingdom*.

Position of EEA reinsurers

3.10.13G The *Insurance Directives* do not apply to reinsurance. But, the *Insurance Directives* do not prevent *insurance undertakings* authorised under those Directives from carrying out reinsurance as well as direct insurance business. Article 13(2) of the *First Non-Life Directive* and article 10(2) of the *Consolidated Life Directive* state that financial supervision of *insurance undertakings* "shall include verification, with respect to the insurance undertaking's entire business, of its state of solvency, of the establishment of technical provisions and of the assets covering them". On that basis, an

insurance undertaking authorised in another *EEA State* which carries on a mixed direct insurance and reinsurance business, and is, therefore, subject to the requirements of the Directives, will generally be treated as being subject to 'equivalent protection'. This is for the purpose of paragraph 3 of Schedule 4 to the *Act* (Exercise of treaty rights). The *insurance undertaking* will, therefore, generally be able to qualify for *permission* as a *Treaty firm* for its reinsurance business if it follows the procedure provided for by Schedule 4 (see *AUTH* 5.3.4G to *AUTH* 5.3.13G (Treaty Firms) and also *AUTH* 3.21 (Treaty firms applying for *Part IV Permission*)). This will be in addition to the *insurance undertaking* being an *EEA firm* under Schedule 3 of the *Act* for its direct insurance business.

Annex B

Amendments to the Glossary

Insert the following new definition in the appropriate alphabetical position:

<i>Consolidated Life Directive</i>	the Council Directive of 5 November 2002 on the taking-up and pursuit of the business of life assurance (No 2002/83/EC), which consolidates the provisions of the <i>First</i> , <i>Second</i> and <i>Third Life Directives</i> .
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