

## 7. Specific thematic article: FMI-PSP Inspection observations in the context of Brexit

Jozeften Uyterhoeven, Hilal Sefsaf, Reinout Temmerman

### Introduction

In 2017, the NBB developed a dedicated policy aimed at setting out its expectations in relation to UK payment and electronic money institutions (PIs and ELMIs) seeking to migrate their activities in the European Economic Area (EEA) to a Belgian payment or e-money institution applicant in order to avoid the consequences of Brexit.

The framework was described in an English-language Application Guide for Payment Institutions and E-money institutions<sup>1</sup> and provided a detailed overview of requirements to which these applicants should adhere. These were FCA-regulated going-concern firms under a European legislative framework, i.e. the revised Payment Services Directive<sup>2</sup> (PSD2), at that time also fully applicable in the UK. Hence, certain requirements could be fulfilled more quickly by these institutions given their existing experience with analogous regulation in the UK.

Since 2017 the NBB has so far licensed six PIs and one ELMI under this framework.

Since then, and following the FMI-PSP inspection's team launch in January 2020, several thematic inspections at PIs and ELMIs were conducted, notably on the safeguarding requirements<sup>3</sup>. These mainly consisted in verifying the correct interpretation and application of the technical and operational safeguarding requirements, but also ensuring that the related governance and control framework are in place to support this implementation. Certain PIs and ELMIs that developed their business within the EEA from Belgium, which were granted a licence in Belgium following Brexit, were included in the inspection planning for 2020 and 2021. The NBB is therefore able to provide the sector with an overview of the most important observations made during the inspections performed so far at these institutions.

1 Available at [https://www.nbb.be/doc/cp/eng/2018/application\\_guide\\_payment\\_institutions.pdf](https://www.nbb.be/doc/cp/eng/2018/application_guide_payment_institutions.pdf)

2 Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC.

3 Articles 41, 42 and 194 of the Law of 11 March 2018 on the status and supervision of payment institutions and electronic money institutions, access to the activity of payment service provider, and to the activity of issuing electronic money, and access to payment systems ("the Law of 11 March 2018").

## Safeguarding of funds

Institutions formerly based in the UK are familiar with the safeguarding requirements as they stem from the PSD2. Therefore, the operational implementation, typically outsourced to the Treasury department of the parent company (see below), generally conforms to the regulatory expectations. Several specific elements of the safeguarding calculations and processes could gain even more in maturity, such as “*payments on hold*”<sup>1</sup>, foreign exchange (FX) risk, credit risk and “*management of banking holidays*”.

Moreover, due to the high level of outsourcing of this matter, institutions should further reinforce their control and monitoring framework via the 2<sup>nd</sup> line of defence, to verify the adequate implementation of the applicable safeguarding requirements.

## Outsourcing context and associated control framework

The locally allocated resources and locally embedded control framework must continue to develop in order to match the materiality of the EU subsidiaries of UK PIs and ELMIs licensed in Belgium. Indeed, while these institutions are quite significant in terms of the number of clients transferred from the UK to the Belgian entity, thus making them important players in the Belgian and EU payments landscape, a large part of the operations, and notably the Treasury and IT departments, typically stays within the parent company located in the UK, and performs services for the Belgian entity by means of intra-group outsourcing arrangements. The local subsidiary must therefore ensure sufficient available and locally dedicated resources at all times to maintain close monitoring of these outsourced activities. Indeed, the Belgian entity must remain responsible for these outsourcing arrangements, as stated in the applicable NBB Circular Letter<sup>2</sup>, and exercise proper oversight and control over the outsourced activities. In that perspective, intra-group Service Level Agreements, intended to legally define the level of services expected from the provider of the outsourcing to the institution, must be sufficiently precise and robust to allow for appropriate monitoring and reporting to the institution’s management.

## Management bodies and central administration concept

As they develop, the local management bodies of the Belgian subsidiary entities are recommended to continuously assess and ascertain that they are properly set up and sufficiently substantial to act with full autonomy – albeit in a group context – in fulfilling all their legal duties in accordance with the Law of 11 of March 2018 and the relevant NBB Circular Letters<sup>3</sup>.

In that perspective, the effective management whose role is to manage the daily business of the institution, and the legal administrative body (LAB) overseeing the effective management’s decisions, must duly record in their minutes the topics discussed, the content of the discussion and the decisions taken, so as to be able to provide in all instances sufficient evidence that they properly execute their respective legal duties. This provides evidence that the decision-making power is located in Belgium, avoiding the risk that the central administration of the

1 Payments pending or temporarily blocked due to screening for anti-money laundering (AML) purposes.

2 Circular Letter NBB\_2019\_09 on the guidelines issued by the European Banking Authority (EBA) dated 25 February 2019 on outsourcing (EBA/GL/2019/02).

3 Articles 34, 35 and 36 of the Law of 11 March 2018, Circular NBB\_2012\_14 on the Compliance function, Circular NBB\_2015\_21 on internal control and the internal audit function.

institution is not considered to be located in Belgium, and proving that it complies with the relevant regulatory requirements<sup>1</sup>.

### **Three lines of defence model**

Belgian subsidiaries of UK PIs and ELMIs should also ensure that their three lines of defence model is commensurate with the size and materiality of the subsidiary at all stages of its development. In that regard, the 2<sup>nd</sup> and 3<sup>rd</sup> lines of defence must ensure at all times and in all circumstances (i) proper experience and knowledge of the Belgian regulatory landscape, (ii) sufficiently developed local risk and audit functions including appropriate staffing, and (iii) (complete) mandatory compliance and audit documentation. Management bodies must actively follow up on control function reports and recommendations.

<sup>1</sup> Articles 23 and 177 of the Law of 11 March 2018.

