



Amendment of Rules Applicable to French Branches of Non-European Banks

A bank that has its registered office outside the European Economic Area (“EEA”) may consider establishing a presence in France in order to provide banking services to French counterparties. The bank may either set up a full-fledged subsidiary or a branch office, i.e., a more simple structure that is not a separate legal entity of the bank and is exempt from a number of requirements applicable to a subsidiary. Branches of banks based outside the EEA may conduct the same business as French banks except for the activities that the banks are not authorized to conduct under the legislation of their home jurisdiction.

The rules applicable to French branches of banks based outside the EEA were revised by Order no. 2015-558 dated May 21, 2015. The Order mostly clarifies preexisting rules but also introduces additional requirements, as a result of Article 47(1) of Directive 2013/36/EU of June 26, 2013 (CRD IV), whereby Member States should not hold branches of non-EEA banks to standards that would be more favorable than that applicable to those having their head office in the EEA.

Importantly, these new provisions will not only affect future branches to be set up in France but also currently existing branches that are already authorized to operate in France.

This *Commentary* provides an overview of the main provisions arising under the Order in terms of requirements applicable to authorization, regulatory capital, governance, and compensation.

Authorization of Branches of Non-EEA banks

Since November 2014, the European Central Bank (“ECB”) has been mandated to authorize all new credit institutions based in the Eurozone. The ECB took over from the national regulators as part of the Eurozone-wide single supervisory mechanism. By way of exception, the French national banking regulator (*Autorité de contrôle prudentiel et de résolution*, “ACPR”) will retain its power to authorize branches of banks based outside the EEA.

It is logical that the ACPR (as opposed to the ECB) should retain its power to authorize French branches of non-EEA banks, given that the French branch of a non-EEA bank is not entitled to “passport” recognition, i.e., the French branch is not allowed to conduct its activities in another European jurisdiction on the basis of its authorization in France. At least for the time being, such “passport” recognition is available to EEA credit institutions only.

The French branch will be granted an authorization on the condition that non-EEA banks expressly commit to carrying out supervisory duties over the French branch that are equivalent to the supervisory duties over a French credit institution and its executives that French law requires from the board of directors and the general shareholders meeting. Non-EEA banks that have already set up existing branches will have until November 22, 2016 to make this commitment to the ACPR.

This commitment will require running a careful comparison between French rules, on the one hand, and the supervisory duties that the non-EEA bank exercises over its French branch, on the other hand. By way of example, French rules would include the annual review of the branch's system of governance and policies in relation to taking, managing, and monitoring risk. This commitment may involve strengthening the non-EEA banks' supervision of the local branches if French standards are not met.

Regulatory Capital

EEA credit institutions have to conform to a number of ratios relating to capital adequacy, solvency, liquidity, leverage, and high risk. Under the former rules, branches were allowed a certain degree of flexibility and could be exempted from a number of requirements provided that (i) French institutions receive equivalent treatment from the regulators of the home jurisdiction, (ii) the non-EEA bank is required to comply with rules as least as strict as the French rules, and (iii) the non-EEA bank confirms that it supervises the operation of the French branch and that the French branch has sufficient funds to meet its commitments.

Broadly, the new provisions replicate the required conditions to rely on exemptions from the application of certain ratios but add new conditions. These conditions are now that (i) the legislation and supervision of the home jurisdiction must be deemed equivalent to the French regulations, (ii) the bank commits to supervising its French branch in compliance with its home legislation, (iii) the French branch has sufficient funds to meet its commitments and its short-term liquidity needs,

(iv) the bank agrees to inform the ACPR if the conditions set out above are no longer fulfilled, (v) the regulator of the home jurisdiction agrees to such exemptions, and (vi) French institutions receive equivalent treatment from the regulators of the home jurisdiction.

In practice, complying with these conditions will require coordination between the regulator of the bank's home jurisdiction and the ACPR, which has jurisdiction over the local branch, to confirm that both regulations are equivalent and ensure reciprocity of treatment, and that the home regulator shares the view of the ACPR, notably on proposed exemptions from the application of regulatory capital.

Governance

New requirements are introduced in the area of governance. Such requirements vary depending on whether or not the branch is of significant size. Metrics for determining whether a branch is of significant size will be clarified by way of secondary legislation to be released at a later date.

At least two senior managers to be notified to the ACPR, which will assess their fitness and propriety, are responsible for the business operation of the branch. These senior managers may not combine their role as senior manager with the position of chair of the bank's board of directors (or equivalent).

The branch's senior managers are required to provide the bank's board of directors with information necessary to review the system of governance and to take remedial action if needed, as well as policies in relation to taking, managing, and monitoring risk.

Branches that are of significant size have to comply with additional requirements, i.e., they must set up a risk committee and a compensation committee (or a procedure achieving the same purpose). Members of these committees must be independent from senior managers; such independence is to be ensured by their compensation and nomination. Members of the risk committee and the compensation committee are bound by French banking secrecy rules (with some statutory exemptions).

Compensation

Finally, senior managers of the branch are required to provide the bank's board of directors with information necessary for the bank to issue and review the branch's compensation policy. Such review is to be conducted at least annually.

The compensation committee (to be set up by branches of significant size) reviews the compensation policy annually, in particular with respect to asset managers and material risk takers.

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