



regulatory focus

Issue 81

A synopsis of the Financial Conduct Authority's (FCA) latest news and publications issued in January 2015.

Welcome to Kinetic Partners' latest issue of *regulatory focus*, our regulatory newsletter for the financial services community.

AIFMD Annex IV Transparency Reporting:

The deadline for Annex IV reporting via GABRIEL was 30 January 2015. Following several issues relating to Annex IV reporting, the FCA published an [important message](#) on 29 January explaining that no actions will be taken against firms who have come up against difficulties either because they have not received the relevant Product Reference Numbers ("PRNs") or where system issues with GABRIEL prevented them from submitting or uploading their reports.

However, it should be noted that the FCA stated in its message that Annex IV reporting should be submitted as soon as the issues are resolved. Therefore, adopting a pro-active approach is highly recommended in order to avoid any late submission fees.

MiFID II Update:

On 19 December 2014, the European Securities and Markets Authority ("ESMA") published its [final technical advice](#) and launched a [consultation on its draft regulatory technical and implementing standards](#) (RTS/ITS) regarding the implementation of the Markets in Financial Instruments Directive (MiFID II) and Regulation (MiFIR). Firms who wish to respond to the Consultation Paper must use the ESMA "form to reply" and submit their responses by 2 March 2015.

MiFID II/MiFIR introduces changes to the functioning of secondary markets, including transparency requirements for a broad range of asset classes, the obligation to trade derivatives on trading venues, requirements for algorithmic and high-frequency-trading and new supervisory tools for commodity derivatives. The new regulatory framework aims to ensure that secondary markets are fair, transparent, safe and that investors' interests are safeguarded when being sold investment products.

The European Commission will be responsible for turning the technical advice from ESMA into delegated acts. During the drafting process it will be liaising with Member States through the European Securities Committee, and once the drafts have been finalised they will be sent to the Council and European Parliament for formal approval. The FCA advised that it does not expect this to happen before the middle of 2015.

Domestically, the FCA is working on three main workstreams:

- The FCA implementation of MiFID II by identifying the major changes which will need to be made;
- Making the necessary changes to the FCA Handbook. The FCA advised that a discussion paper will be issued during the first quarter of 2015 which will seek views on issues relating to conduct of business. However, a formal consultation on Handbook changes will not take place until the end of 2015;
- The FCA is working closely with the Treasury to agree the legislative changes required to implement MiFID II. The Treasury will consult on the changes during the first quarter of 2015.

Regulatory highlights this month include:

- PS 15/2 Recovery and Resolution Directive including feedback on CPI4/15 and final rules
- Tribunal upholds fines and prohibitions for partners of Arch Financial Products
- Two former senior executives of Martin Brokers fined and banned for compliance failings related to LIBOR

Regulatory Update

We also provide regulatory updates on key developments as and when these arise. For further information, including recent updates, please visit [here](#).

- [ECON and LIBE vote in favour of the proposed Fourth Money Laundering Directive and Wire Transfer Regulation](#)
- [FAQs on how to implement the SFC's new guidance on assessing Corporate Professional Investors](#)
- [SEC announces examination priorities for 2015](#)

OUR RECENT AWARDS

ONE STAR 'VERY GOOD'
ACCREDITATION
2015
Best Companies UK

BEST OVERALL
ADVISORY FIRM IN THE US
2014
HFWeek

BEST ASIAN ADVISORY FIRM
FOR REGULATION
AND COMPLIANCE
2014
HFWeek

BEST EUROPEAN ADVISORY
FIRM FOR REGULATION
AND COMPLIANCE
2014
HFWeek

BEST ADVISORY FIRM
REGULATION AND COMPLIANCE
2014
HFWeek

BEST SEC REGISTRATION
TEAM - HONG KONG
2014
Acquisition International

UCITS FUND ADVISOR OF
THE YEAR - IRELAND
2014
Acquisition International

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The FCA is set to obtain new competition powers on 1 April 2015. These new powers will see the Regulator better equipped to deal with anti-competitive behaviour in relation to the provision of financial services.

RRD applies to IFPRU 730k investment firms but proportionality will be applied for those firms in scope but which pose a lesser threat to financial stability.

Policy Documents

CPI 15/1 FCA Competition Concurrency Guidance and Handbook amendments

15 January

The FCA is set to obtain new competition powers on 1 April 2015. These new powers will see the Regulator better equipped to deal with anti-competitive behaviour in relation to the provision of financial services, through the Competition Act 1998 and the Treaty on the Functioning of the European Union (TFEU). It will also provide additional powers under the Enterprise Act 2002 to carry out market studies, and to make market investigation references to the Competition and Markets Authority ("CMA") relating to financial services.

Thus, in respect of financial services, CMA and the FCA will, for the first time, have concurrent powers. These new powers are in addition to the current powers that enable the FCA to pursue their competition objective. The significance of these changes is potentially great and the FCA is aware that stakeholders may wish to have their say prior to rules being formulated. A period of consultation is currently underway, with the Regulator seeking views on three core areas:

- Draft guidance on their powers under the Competition Act 1998
- Draft guidance on market studies and making market investigation references
- A draft legislative instrument to introduce minor amendments to the FCA handbook

The Regulator will be accepting feedback via their [online response system](#) until 13 March 2015, upon which they will reflect on the feedback received and issue guidance.

For full details of the competition concurrency guidance and handbook amendments, see the FCA [consultation paper](#) or visit the 'promoting effective competition' [webpage](#).

PS 15/2 Recovery and Resolution Directive ("RRD") including feedback on CPI 14/15 and final rules

16 January

RRD is designed to prevent or mitigate the effects of large banks failing. RRD applies to IFPRU 730k investment firms but proportionality will be applied for those firms in scope but which pose a lesser threat to financial stability. Simplified obligations will be applied for all but the largest IFPRU 730k firms.

The FCA has issued Policy Statement 15/2 which reports on the main issues arising from CPI 14/15 published in August 2014. It has also set out final rules to transpose the RRD into the UK regulatory regime for investment firms (IFPRU 730k firms) and certain group entities (when a group contains a 730k investment firm or credit institution) that are regulated prudentially and that fall within the scope of the RRD.

The majority of the rules came into force on 19 January 2015. The rules on the contractual recognition of bail-in will come into force on 1 January 2016. The reporting of recovery plans will be phased in from the end of June 2015, with the largest firms reporting first.

PS can be found [here](#).

CP 15/2 Financial Services Compensation Scheme - Management Expenses Levy Limit 2015/16 (CP 15/1)

19 January

On 19 January 2015, the FCA and the PRA released a joint consultation paper on the management expenses levy limit ("MELL") for the Financial Services Compensation Scheme ("FSCS"). The MELL, which the FCA and PRA are required to jointly set under the Financial Services and Markets Act 2000 ("FSMA"), provides the FSCS with the necessary financial resources to carry out its function efficiently and economically, and more specifically, meet its responsibilities to consumers. In the consultation paper, the regulators recommend that the levy be set at £74.4 million, which would consist of a minimum levy of £69.1 million and a contingency reserve of £5.3 million. The management expenses portion of the proposed MELL for 2015/16 represents a 7.4% reduction compared to the 2014/2015 levy. Both regulators believe a MELL of £74.4 million is adequate to allow the organisation to meet its obligations.

The FCA and PRA have invited comments on the consultation paper. The final rules will take effect on 1 April 2015 with invoices being sent to authorised firms from July 2015. The consultation paper will be of particular interest to those firms which are not FSCS exempt for the purposes of fees.

Consultation Paper can be found [here](#).

Enforcement Matters

FCA fines Reckitt Benckiser £539,800 for listing rules failures

20 January

The Reckitt Benckiser Group has been fined over half a million pounds in relation to breaches of the listing, disclosure and transparency rules. The fine also relates to breaches of the Model Code as it was found that two of the senior executives failed to notify the market of share dealings as soon as possible, and also failed to make notifications including all the required information. The FCA clarified that there is no suggestion that any of the senior management intentionally breached the Model Code or traded on inside information.

It was found that failures in internal systems, controls and training over a seven year period, as well as internal record-keeping, left the firm unable to monitor its share dealings effectively. It was found that key risks had not been identified or mitigated in the firm's share dealing policy. Also the firm relied heavily on informal processes and the knowledge of individuals in place of clear processes or structured training. It was stressed that lack of appropriate systems and late notifications undermine the FCA's objectives of market integrity.

Press Release can be found [here](#).

Final Notice can be found [here](#).

Tribunal upholds fines and prohibitions for partners of Arch Financial Products

20 January

The Upper Tribunal ("Tribunal") has upheld the FCA's decision (December 2012) to issue a public censure against Arch Financial Product LLP ("AFP") and to prohibit Robin Farrell and Robert Addison from performing any role in regulated financial services. The Tribunal supported the FCA's initial findings that AFP, Robin Farrell (CEO of AFP) and Robert Addison had acted recklessly and failed to fairly manage conflicts of interests in relation to four specific transactions. The Tribunal also upheld initial findings concerning insufficient controls over the access and use of material non-public information and that non-public information relating to publicly listed Guernsey cells was available to those making decisions on behalf of the funds. The Tribunal found further instances where control about the access to and segregation of non-public information was deficient.

In relation to breaches of FCA Statements of Principle stemming from misconduct during the period under review Mr Farrell and Mr Addison received fines totalling £850,000. The Firm would have been fined £9million if it was not for the firm's financial position. The case highlights the importance of firms having robust business models in place in order to maintain integrity and to ensure that clients' interests are put before those of a firm and its employees.

To note, in its initial findings the FCA raised concerns about the liquidity risks posed to the funds as a result of the investment strategy being pursued. These findings were not upheld by the Tribunal.

The Press Release can be found [here](#).

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The case highlights the importance of firms having robust business models in place in order to maintain integrity and to ensure that clients' interests are put before those of a firm and its employees.

The systems and controls were non-existent and there was a culture at the firm where profits were prioritised to the detriment of regulatory compliance.

Two former senior executives of Martin Brokers fined and banned for compliance failings related to LIBOR

22 January

The FCA published a Press release on 22 January 2015 indicating that it has fined and banned two former senior executives of interdealer broker Martin Brokers (UK) Limited for compliance and cultural failings at the firm. This follows previous enforcement action taken in 2014, where the firm was fined £630,000 for misconduct relating to the London Interbank Offered Rate (LIBOR).

David Caplin (former chief executive) was fined £210,000 and Jeremy Kraft (former compliance officer) was fined £105,000. Both are also banned from performing significant influence functions at financial services firms.

It was found that the CEO's and Compliance Officer's failings led to a lack of compliance oversight of the front office, a culture at the firm that permitted LIBOR manipulation to take place and enabled the misconduct to continue undetected over a prolonged period of several years. The FCA discovered as part of its investigation that brokers were induced to assist in LIBOR manipulation in exchange for corrupt brokerage payments and there were no systems within the firm to detect "washed trades". Consequently, the integrity of the financial markets was compromised.

Speaking out, Georgina Philippou, the acting director of enforcement and market oversight at the FCA explained that Mr Kraft, as Compliance Officer, and Mr Caplin, as CEO, were responsible for setting the right culture at the firm and ensuring that the firm's risk management systems and controls were adequate to oversee its broking activities. In fact, the systems and controls were non-existent and there was a culture at the firm where profits were prioritised to the detriment of regulatory compliance, which was seen as unimportant rather than as an integral part of the running of the company. Both individuals ignored the obvious risks that brokers would give or accept inducements, including what the FCA described as "lavish entertainment". The FCA was also critical of the fact that neither Mr Caplin nor Mr Kraft paid proper attention to recommendations made by an external compliance consultancy which identified serious compliance deficiencies.

The FCA made clear that this case should serve as a strong warning to senior management of regulated firms; in the event that a firm's misconduct can be attributed to cultural failings, holders of significant influence functions must be in a position to answer for that misconduct.

Full Press Release can be found [here](#).

Other Developments

The retrospective application of rules: feedback on the call for examples

22 January

In August 2014 the FCA asked firms to provide examples of retrospective application of regulatory rules, defined as when the regulator had applied a more demanding standard or interpretation of the rules after the event. This call for examples was designed to help the FCA understand the issues, identify any problems and address its regulatory approach if necessary.

In its report, the FCA summarised the analysis of the responses received and stated that despite receiving 36 responses, none of these reflected retrospection in the specific terms outlined. However, it was highlighted that firms used this opportunity to raise questions and concerns about the nature of the FCA's regulation, leading the regulator to realise that there were a number of examples where firms felt that the FCA had intervened too late. The FCA concluded that it has found the feedback from firms to be valuable and also reiterated its desire to be a forward-looking regulator.

The main questions/responses concerned the following topics:

- The treatment of Traded Life Policy Investments (TLPIs) - the FCA branded these products as "toxic" for the retail market causing a fall in their value;
- Financial Ombudsman Service (FOS) and the Ombudsman's decisions - essentially around the threat of interplay of regulatory activity in which rules laid by one body can be reinterpreted by another;
- Persistent issues where the regulator was aware of certain market practices and later on decided to review past business and declared that mis-selling occurred. The suggestions concerned: pensions, endowments, PPI, Arch Cru, Interest rate hedging products (IRHP), capital at risk products, legacy business review and S166 reviews.
- The issue of a new interpretation based on a new methodology - the consequences of using a new technique to judge past actions or in the event that the regulator would change its view on the value of a disclosure, where once the disclosure was viewed as sufficient but is now seen as insufficient due to a greater awareness of consumer inertia.

The FCA's report can be found [here](#).

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