DUFF & PHELPS

Protect, Restore and Maximize Value

Regulatory Focus

Issue 131

In this edition of Regulatory Focus, the experts in Duff & Phelps' UK Compliance and Regulatory Consulting team, provide a detailed synopsis of the latest news and publications issued by the Financial Conduct Authority (FCA) during November and December 2019.

INSIDE

Amendments to the Money Laundering Regulations

On 10 January 2020 changes to the Money Laundering Regulations came into force to transpose the EU 5th Money Laundering Directive. We have highlighted some of the significant changes that may be of relevance to our clients:

Firms must update their beneficial ownership records of corporate clients

There is now an explicit customer due diligence ("CDD") requirement for firms to take reasonable measures to understand the ownership and control structure of their corporate customers. The reference to "reasonable measures" suggests that a risk-based approach can be taken in each case. In addition, there is a new requirement for firms to check the beneficial ownership register on Companies House before establishing a business relationship and to report discrepancies between their CDD information and the information held on the Companies House Register.

New requirement to identify CEOs and chief executives

There is now an explicit CDD requirement to take reasonable measures to verify the identity of the senior managing official when the beneficial owner of a body corporate cannot be identified. This enhances the existing requirement for firms to take reasonable measures to verify the names of the board of directors and senior managing officials.

Additional requirement to establish source of wealth and source of funds

In addition to the existing requirement to establish the source of wealth and source of funds for politically exposed persons, there is a new requirement to do so for business relationships with persons established in high-risk third countries or in relation to relevant transactions where either of the parties is established in a high-risk third country. Being "established in" is defined as being incorporated in or having its principal place of business in that country or for financial institutions having its principal regulatory authority in that country.

New high-risk factors for enhanced due diligence

Firms have new high-risk factors to consider when assessing the need for enhanced due diligence, where:

- there are relevant transactions between parties based in high-risk third countries,
- the customer is the beneficiary of a life insurance policy,
- the customer is a third-country national seeking residence rights or citizenship in exchange for transfers of capital, purchase of a property, governments bonds or investment in corporate entities, and
- transactions related to oil, arms, precious metals, tobacco products, cultural artefacts, ivory or other items related to protected species, or archaeological, historical, cultural and religious significance, or of rare scientific value.

To see our full article summarising key changes introduced by Money Laundering Regulations 2019, please click here.

FCA extends the Senior Managers and Certification Regime to 47,000 firms

9th December

The FCA extended the Senior Managers & Certification Regime ("SM&CR") to approximately 47,000 firms on 9th December 2019. The extension of the SM&CR, which had already applied to the banking and insurance sectors, is a key step in ensuring that individuals take accountability for their own actions, behaviour and competence.

The aim of the regime is to encourage greater individual accountability and sets a new standard of personal conduct in financial services by:

- ensuring senior managers are accountable for conduct in their areas of responsibility;
- ensuring a minimum standard of behaviour for everybody working in the sector through the FCA's five individual Conduct Rules; and
- enhancing professionalism in the industry by requiring firms to certify that their staff are fit and proper.

Jonathan Davidson, Executive Director of Supervision – Retail and Authorisations, has stated that "the SM&CR is an important way to ensure that individuals take personal responsibility and it is a catalyst for driving cultural transformation". Moreover, Mr. Davidson has expressed that firms shouldn't just look to tick boxes to comply with the regime on 9th December 2019, but also continue to ensure that employees are "stepping up and taking accountability every day from here on".

By 9 December 2020, solo-regulated firms will need to ensure that:

- all relevant staff are trained on the Conduct Rules and how they apply to their roles (Senior Managers and Certified staff should have been trained by 9 December 2019);
- all staff in certified roles are fit and proper to perform that role and are issued with a certificate; and
- data is submitted to the FCA for the directory of key people working in financial services.

More information on how firms should prepare for the above can be found here.

D&P has helped many firms implement SM&CR and also helps firms to comply on an ongoing basis by providing ongoing support, advisory services and training. We also undertake health checks for firms to assess compliance with the new regime, highlighting any gaps and weaknesses and assist with remediation work where required. Please contact us if you would like to discuss further.

MiFID II: The European Securities and Market Authority (ESMA) consults on position limits in commodity derivatives

5th November

ESMA has launched a consultation paper, part of a review it is obliged to perform under MiFID II, on position limits and position management in commodity derivatives.

Following a call for evidence, which was published in May, this consultation analyses a number of different factors including the impact of position limits on market abuse, orderly pricing, settlement and less liquid commodity derivative contracts.

The consultation seeks views on proposed changes to the legal framework around the scope of commodity derivatives, introducing a limited position limit exemption for financial counterparties and enhancing the convergence of position management regimes by trading venues. Views are also sought on the recent amendments to the quantitative thresholds that have triggered the publication of weekly position reports by trading venues.

ESMA intends to complete these workstreams by the end of March 2020.

To see the full consultation paper, please click here.

ESMA updates its Q&A's on the securitisation regulation

15th November

ESMA has updated its Questions and Answers on the Securitisation Regulation (" Securitisation Q&As").

The majority of Q&As in this document provide clarification on the different aspects of the templates contained in the draft technical standards on disclosure, which were recently published by the European Commission. The Q&As provide guidance on how specific fields in the templates should be completed and contains clarifications relating to STS notifications and securitisation repositories. There are new Q&As addressing the handling of corrections, as well as clarifications on transitional provisions that apply to the completion of disclosure templates, use of templates for less common underlying exposures, delegation of reporting to third parties, reporting of static data, and detailed clarifications on certain definitions and the use of specific fields on templates.

The fourth version of the Securitisation Q&As includes a summary table to provide an easy overview of the list of Q&As. The overview table clearly sign-posts new and modified Q&As.

The document was created to promote common, uniform and consistent supervisory approaches and practices in the day-to-day application of the Securitisation Regulation and to ensure regulated entities comply with their obligations.

Please see the updated Securities Regulation Q&As here

Conduct risk during LIBOR transition: questions and answers

19th November

LIBOR, used as the interest rate benchmark to value different financial products, will end after 2021. In light of their expectation that firms should be ready to switch to alternative rates in advance of this date, the FCA has answered a number of key questions about conduct risk put to it by industry bodies. The following key areas are covered:

- Governance and accountability
- Replacing LIBOR with alternative rates in existing contracts / products
- Offering new products with risk-free rates (RFRs) or alternative rates
- Communicating with customers about LIBOR and alternative rates / products
- Firms investing on customers' behalf and LIBOR transition

The FCA has outlined that, in addition to continuing to treat customers fairly, it expects firms to have made appropriate plans and to take any required steps during the move away from LIBOR. It has urged firms across all sectors to assess and manage the impact of LIBOR transition on their business, focusing particularly on "prudential, operational and conduct risks".

To read the questions and answers in full, please click here.

FCA to ban promotion of speculative mini-bonds to retail consumers

26th November

The FCA has announced that it will ban the mass marketing of speculative mini-bonds to retail customers. Ahead of the upcoming Individual Savings Account (ISA) season the FCA introduced this restriction without consultation by using its product intervention powers. The restriction came into force on the 1st of January 2020 and will last for 12 months. During this period, the FCA will consult on making the ban permanent.

The term mini-bond refers to a variety of investments; however, the ban will apply to more complex and opaque arrangements, where the funds raised are used to lend to a third party, invest in other companies or purchase or develop properties. Exemptions to the ban include:

- companies which raise funds for their own activities (other than the ones above);
- listed mini-bonds; and
- mini-bonds used to fund a single UK property investment.

The FCA has limited powers over unauthorised issuers of speculative mini-bonds; however, if an authorised firm approves or communicates a financial promotion, or directly advises on or sells these products, the FCA can take action.

The FCA has given examples of the work it has undertaken to tackle the risks for investors from mini-bonds, including:

1. Investigating more than 80 cases of regulated activities potentially being carried out without FCA authorisation.
2. Assessing over 200 cases of financial promotions that appeared not to have complied with the FCA rules.
3. Seeking to persuade the internet service providers, particularly Google, to take more action, for instance to take down websites promptly where they are likely to involve a breach of law or regulations.
4. Contact with the Department of Culture, Media and Sport to urge inclusion of financial harm in the proposed legislation on online harms.
5. Developing tools for data analysis, for instance introducing web scraping to assist in the identification of mini-bond promotions.

As a result of the ban, promotion of unlisted speculative mini-bonds to investors will only be permitted for investors that are known to be sophisticated or high net worth. Any marketing material which is distributed must also include a specific risk warning and disclose any costs or payments to third parties that are deducted from the money raised from investors.

The read the full article click here.

ESMA updates Q&As on MiFID II and MiFIR investor protection and intermediaries

4th December

ESMA updated its Q&As on the implementation of investor protection topics under the Market in Financial Instruments Directive and Regulation (MiFID II/ MiFIR). The updated Q&As provide new answers on the following topics:

- Costs and charges disclosures:
  - Ex-post information in case of portfolio management; and
  - Relationship Article 50(9) and Article 60 of the Delegated Regulation in case of portfolio management
- Product intervention:
  - The application of national product intervention measures in case of services provided on a cross-border basis

To read the full article click here.

ESMA updates AIFMD questions and answers

4th December

ESMA updated its Q&As regarding the application of the Alternative Investment Fund Managers Directive (AIFMD). It has added a new Q&A in relation to how AIFMs should report results of liquidity stress testing for closed-ended unleveraged AIFs that they manage.

It clarifies that although such AIFs are exempt from the requirement to conduct liquidity stress tests, when reporting to the applicable National Competent Authority, AIFMs should specify in the mandatory field of the report that it is 'not applicable'. However, if the AIFM has conducted liquidity stress tests on a closed-ended unleveraged AIF, the results should be reported in the same field.

To read the updated Q&A in full, please click here.

Building operational resilience: impact tolerances for important business services

5th December

The Bank of England, Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) have published a shared policy summary and coordinated consultation papers (CPs) on new requirements to strengthen operational resilience in the financial services sector.

All three supervisory authorities have a shared priority of ensuring they assist in enhancing operational resilience within firms and across Financial Market Infrastructures (FMIs). They will also build upon the concepts that were set out in the operational resilience Discussion Paper (DP18/4).

The policy stated that firms and FMIs were expected to take ownership of their operational resilience with the impact of the public's interest being assessed when prioritizing plans and investment choices. If firms are to identify any disruptions, they are expected to clearly communicate to clients any alternative means of accessing their services.

Under the proposals, firms and FMIs would be expected to:

- identify their important business services that, if disrupted, could cause harm to consumers or market integrity, threaten the viability of firms or cause instability in the financial system
- set impact tolerances for each important business service, which would quantify the maximum tolerable level of disruption they would tolerate
- identify and document the people, processes, technology, facilities and information that support their important business services
- take actions to be able to remain within their impact tolerances through a range of severe but plausible disruption scenarios

Andrew Bailey, FCA Chief Executive, said: 'It is in the public interest that a resilient financial system is able to supply the most important services with minimal interruption even during severe operational events. The proposed new requirements are aimed at achieving this outcome. He added, 'Disruptive events can have a high impact on consumers and businesses, so firms and FMIs need to know where the risks to their service delivery lie and make sure that they are prepared for any service disruption by testing their planned response'.

Read full article here.

ESMA publishes 2nd Annual Report on EMIR penalties and supervisory measures

9th December

ESMA has published its second annual report on supervisory measures carried out and penalties imposed by national competent authorities (NCAs) under the European Market Infrastructure Regulation (EMIR). The report, which covers the period January 2018 to December 2018, can be found here.

As well as considering the supervisory measures and enforcement actions carried out by NCAs, the report also looks at the interaction between NCAs and market participants when monitoring compliance with the following EMIR requirements:

- the clearing obligation for certain OTC derivatives (Art. 4 EMIR);
- the reporting obligation of derivative transactions to trade repositories (Art. 9 EMIR);
- requirements for non-financial counterparties (Art. 10 EMIR); and
- risk mitigation techniques for non-cleared OTC derivatives (Art. 11 EMIR).

The report contains some interesting commentary on the types of process and channels used by different NCAs to communicate with market participants e.g. the use of feedback processes, webpages, public guidelines and working groups. In terms of supervisory measures, the report found some supervisory areas to be highly harmonised, such as NCAs' sources of information used to check compliance with EMIR requirements (for example publicly available financial statements, as well as information received from trade repositories and directly from firms), as well as NCAs' supervisory and enforcement tools. Commonly used supervisory tools include the inspection of documents, information from third parties, on-site investigations and interviews. The report also found that supervisory practices have evolved in relation to compliance with EMIR requirements, with there being a greater effort towards making better use of information available for supervisory purposes.

However, the report has also identified areas of supervision which may benefit from coordinated approaches between NCAs, including:

- the supervision of NFCs in relation to the clearing obligation;
- how to identify excessive reliance on the exception applied to hedging positions; and
- the supervision of counterparties below the clearing threshold and of third country entities trading in OTC derivatives with significant impact in the EU.

In terms of enforcement, the number of NCAs conducting investigations during 2018 into the following issues were as follows:

- 18 regarding reporting requirements;
- 8 into risk-mitigation techniques;
- 6 into the clearing obligation; and
- 4 into non-financial counterparties.

Further to the above, approximately 10% of NCAs issued recommendations or sent warning letters to market participants, however, no new sanctions or penalties were imposed on supervised entities during 2018. On average, the NCAs of five countries sent recommendation or warning letters to individual market participants, and four countries sent general recommendations to all market participants. These related to various topics, including; clearing obligations; instances of high numbers of rejected reports; lack of reporting; timing and content of portfolio reconciliation and valuation.

The report, which ESMA expects to be a useful tool to understand the supervisory and enforcement efforts of NCAs, has been sent to the European Parliament, the Council and the Commission.

ESMA calls for strengthened supervision on suspicious transaction reporting

12th December

ESMA published a peer review report discussing how national competent authorities (NCAs) handle suspicious transactions and order reports (STOR) under the Market Abuse Regulation (MAR).

ESMA issued a self-assessment questionnaire to 31 NCAs and made on-site visits to NCAs in Germany, Greece, Ireland, Italy, Romania and Sweden, where they met various investment stakeholders and European industry bodies representing trading venues, investment firms and asset managers. They also received input from their Securities & Markets Stakeholder Group.

The Report details a significant increase in STORs and finds that national supervisors could do more to ensure financial participants help combat market abuse.

Persons professionally arranging or executing transactions, investment firms and trading venues should report STORs to their NCAs, who will analyse suspicious behaviours and investigate insider dealing or market manipulation.

In 2015, NCAs received 4,634 suspicious transaction reports in 2015 under the market abusive directive. This increased to 10,653 in 2017 and 11,130 in 2018 following increased reporting requirements under MAR. In addition, in 2018, NCAs received 1,560 notifications of alleged market abuse, including consumer complaints and whistle-blower reports.

This report assessed all 31 NCAs in six areas for the effectiveness of STOR supervision and found all NCAs are performing well in the analysis of suspected market abuse reported in STORs.

However, there are areas for improvement in NCAs' supervision and enforcement of the STOR requirements, ESMA recommends NCAs should:

- ensure all financial parties, including asset managers, are complying with the STOR requirements.
- enhance their focus on suspected non-reporting/poor-reporting of STORs and enforce and sanction non-compliance.

NCAs from Belgium, France, Italy, the Netherlands, Portugal and the United Kingdom were considered fully compliant in at least four of the six assessment areas.

Eleven NCA's were assessed as partially-compliant, or non-compliant, in their supervision of the STOR requirements by financial parties. Thirteen were assessed as partially compliant, or non-compliant, in their response to poor-quality or suspected non-reporting of STORs and associated enforcement actions.

ESMA gave bespoke improvements for each NCA that was not fully compliant and will follow-up with NCAs on the different individual findings as noted in the peer review report.

The full report is available here.

FCA and Bank of England statement on joint review of open-ended funds

16th December

The Financial Policy Committee's (FPC) December Financial Stability Report set out the initial findings of a joint FCA and Bank of England review into open-ended investment funds and the risks posed by their liquidity mismatch.

The FPC considers that the mismatch between redemption terms and the liquidity of some funds' assets leads to investors, who redeem ahead of others, gaining an advantage – particularly in stress scenarios.

In order to ensure greater consistency between the liquidity of a fund's assets and its redemption terms, the FPC has identified that:

- The assessment of the liquidity of funds' assets should reference the price discount needed to secure a quick sale of a representative sample of those assets, or the time period needed to secure a sale which avoids a material price discount. The Securities and Exchange Commission has recently adopted liquidity measures based on this concept.
- The price that redeeming investors receive for their units in the fund should reflect the discount needed to sell the required portion of a fund's assets in the specified redemption notice period, ensuring fair outcomes for redeeming and remaining investors.
- Redemption notice periods should reflect the time needed to sell the required portion of a fund's assets without discounts beyond those captured in the price received by redeeming investors.

This joint review will now consider how these principles can be implemented in a proportionate manner, and the FCA will use the conclusions, expected during 2020, to develop their rules for open-ended funds.

Read the full article here.

Announcement from John Swift QC inviting submissions from interested parties

18th December

An independent review has begun into the FCA and its predecessor the FSA's supervisory intervention on Interest Rate Hedging Products. The review will provide an assessment of the FCA and FSA's actions relating to their Interest Rate Hedging Product Redress Scheme, as well as setting out the lessons that should be learned from the review.

The Terms of Reference for the Review, which describes the nature of the review and the specific questions being considered, can be found here.

John Swift QC, the Independent Reviewer, has requested that individuals share their views on the topic by emailing IndependentInvestigation.InterestRateHedgingProducts@fca.org.uk. Any views should be sent by 31 January 2020.

Read the full article here.

FCA and PRA publish Decision Notices given to former CEO who paid excessive remuneration to his wife to reduce his tax liability

18th November

The FCA and the PRA have banned and fined the former CEO of a small mutual insurer £78,318 and £76,180 respectively. Following a joint investigation, the regulators' decision-making committees found that the individual transferred excessive amounts of his own remuneration to his wife between February 2010 and July 2016 to reduce his own tax liability. The former CEO also took steps to conceal the arrangement. By deliberately arranging unjustified payments to his wife, the regulators believe that the individual acted without integrity to his financial benefit.

As CEO of the mutual insurer, the individual paid his wife a proportion of his own salary in compensation for providing some out of hours administrative support and occasional hospitality at home. Although this was reasonable pre-2010, from February 2010 the individual transferred increasing amounts of his salary, and in most years all or part of his bonus, to his wife in order to reduce his tax liability. As a result of this arrangement between 2010 and 2016, the individual paid approximately £18,000 less in income tax than he should have done.

The individual concealed the level of payments made to his wife from the mutual insurer's Board and Remuneration Committee. For example, false minutes were created to give the misleading impression that the mutual insurer's Remuneration Committee had agreed the salary of his wife from 2013 to 2015 inclusive. The individual then responded recklessly to an information request from the PRA by sending the false Remuneration Committee minutes.

The individual has referred the Decision Notices to the Upper Tribunal, where each party will present their respective cases. Any findings in the Decision Notices are therefore provisional and reflect the FCA's and PRA's respective findings as to what occurred and how they consider the individual's behaviour should be characterised.

The full article can be found here.

FCA fines Firm £1.9m for fund failings

20th November

The FCA fined an asset management firm £1,867,900 for failing to treat more than 4,500 retail investors fairly in two of its funds. This contravened Principle 6 (Treating Customers Fairly) of the FCA's Principles for Business.

In November 2011, the Firm's appointed investment manager reduced the active management of its Japan and North American Funds. The subsequent treatment of retail investors in these funds was substantially different from its treatment of the institutional investors in the same funds.

The Firm informed nearly all institutional investors affected by this change and offered to manage these two funds for them without charge. The Firm did not communicate the change in investment strategy to any retail customers. The Firm charged these investors the same level of fees for nearly five years as it had before the change in investment strategy, without providing the same level of active management.

Mark Steward, Executive Director of Enforcement and Market Oversight at the FCA, said:

'The FCA requires firms to treat all its customers fairly, not just some customers. In this case, retail investors paid fees for active investment management they did not receive. For retail clients, the Japan and North American funds were in effect operating as "closet trackers" as the fees charged to them were inappropriate given the diminished level of active management. The matter is aggravated by the length of time the Firm took to identify the harm being caused to the retail investors and to fix it.'

The Firm charged investors £1,784,465.32 more than if they had invested in a passive fund. The Firm has now disclosed the matter to all affected customers and compensated them for the additional costs.

The situation revealed serious weaknesses in the Firm's systems and controls in relation to the management, oversight and governance of an area of its business which included the Japan and North American Funds. This was in contravention of Principle 3 of the FCA's Principles for Business. These weaknesses resulted in the issue not being identified and resolved for considerable time.

4,713 direct retail investors, 75 intermediary companies with underlying non-retail investors and two institutional investors in the Japan and North American Funds were affected by the Firm's decision to retain their level of fees.

Read the full article here.

FCA secures confiscation order totalling £291,070 against convicted fraudster

27th November

A confiscation order of £291,070.36 was made against an individual in Southwark Crown Court.

The individual was sentenced to 5 years imprisonment for defrauding investors of just under £3 million, in relation to unauthorised investment schemes he operated between 2008 and 2017. The confiscation order follows the initial prosecution by the FCA.

Mark Steward, Executive Director of Enforcement and Market Oversight at the FCA, commented:

"The FCA will continue to take steps to ensure that proceeds of criminal activity are confiscated from the criminals we prosecute so that victims can be compensated as far as possible."

The Court established that the individual had derived a benefit of £3,010,982.18 from his criminal conduct; the total realisable assets for confiscation was £291,070.36, as the individual had spent the rest of the victims' monies maintaining his comfortable lifestyle.

The monies will be used to compensate the 14 victims of his crimes. The individual will be liable to a further 2.5 years in prison if the confiscation order is not paid on time.

FCA fines former Managing Director £45,000 for failure to notify personal trades

20th December

The FCA has fined a former Managing Director of a publicly listed company £45,000 for failure to notify personal trades, which were conducted in the individual's capacity as a Person Discharging Managerial Responsibility (PDMR) at the company.

Under the Market Abuse Regulation, PDMRs, as well as those who are closely associated to PDMRs, are required to notify the FCA and the issuer of every personal account transaction conducted above a certain threshold. The notification, which covers transactions in the issuer's shares, debt instruments, derivatives and other linked financial instruments, must be made within 3 business days of the transactions being carried out.

It was discovered that the individual sold shares worth a total of £71,235 on 3 occasions between 24 August 2016 and 18 January 2017, without informing the FCA or the issuer within the required timeframe. The FCA did not, however, find that the former Managing Director traded whilst in possession of any confidential inside information. As a result of the individual's agreement to resolve the matter, the fine was reduced to £45,000, representing a 30% discount.

Mark Steward, FCA Executive Director of Enforcement and Market Oversight, stated that 'transparency of trading by directors and other responsible officers is a key element of market integrity and helps to police the market against illegal insider trading'. Senior managers promptly notifying the FCA and issuers of personal account transactions allows the FCA to deliver effective market supervision and maintain market confidence.

The full article can be found here.

New appointments to FCA board announced

5th November

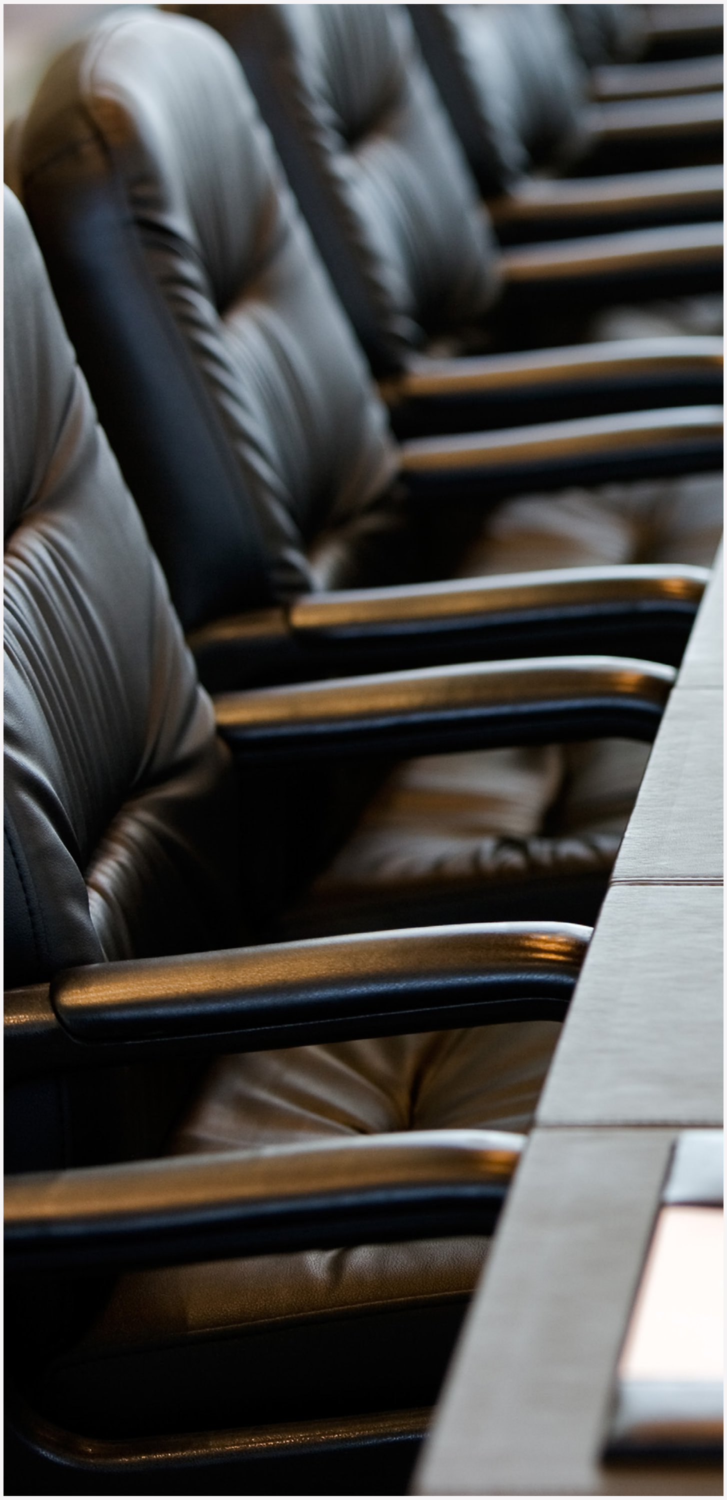
The Economic Secretary to the Treasury, John Glen, has made three new appointments to the Board of the FCA. Liam Coleman, Alice Maynard CBE and Tommaso Valletti will take up roles as Non-Executive Directors to the Board of the FCA and serve 3-year terms, from 5 November 2019.

Alice Maynard, who was jointly appointed by HM Treasury and the Department for Business, Energy and Industrial Strategy, has a wide range of experience as a Non-Executive Director and advisor across various regulated industries. Alice is also currently a Board member of HMRC and Transport for London and was previously the Chair of the charity, Scope.

Liam Coleman has held senior leadership roles in banking, including as the CEO of the Co-Op Bank. He is currently the Chair of Great Western Hospitals NHS Trust.

Tommaso Valletti is a highly experienced competition and regulatory economist, who has varied experience across academia and multilateral development banks. Most recently, Mr. Valletti was one of the two most senior competition experts at the European Commission.

The full article can be found here.



Meeting the pace of technological change

6th November

Nick Cook, Director of Innovation at the FCA, delivered a speech on the FCA's reactions to technological change within the financial services sector. This speech was delivered at the Chief Data Officer Exchange Financial Services Conference.

Nick outlined the work the FCA has undertaken over the last 5 years to develop its initiative offering regulatory feedback to innovative business models into an entire division seeking to disrupt financial markets in the interests of consumers - including the Regulatory Sandbox, the Advice Unit, TechSprints and direct support.

When the Regulatory Sandbox opened for its sixth cohort, in October, it sought to encourage developments in areas of regulatory interest by specifically calling out propositions that:

- Address issues such as access, exclusion and vulnerability
- Respond to the challenges posed by climate change
- Overcome regulatory challenges, helping regulated firms comply with their obligations

However, it was noted that whilst some areas of the market had embraced these opportunities to engage with the FCA, for example retail banking, there had been significantly fewer engagements with other sectors such as asset management and retirement savings. One reason for this may be that the Regulatory Sandbox isn't relevant to their needs, which leads the FCA to question whether changes should be made to their 'innovation' offering to broaden its relevance?

Mr. Cook also outlined the relatively slow take up of RegTech within the financial services market and noted that challenges faced by firms include:

- Length of the sales cycle
- Complexity of information technology systems in some larger institutions
- Making the step from Proof of Concept to Proof of Value
- Lack of access to high-quality synthetic data assets to test against

The FCA is exploring what role it ought to play in supporting the creation of a digital testing environment, to support the development of RegTech, and whether it could be scaled across jurisdictions.

In conclusion Mr. Cook highlighted the importance of regulators understanding that technology is often the architect of new challenges faced, as well as the solution. As physical borders become increasingly irrelevant the FCA must accept that it cannot achieve its goals alone, it must be part of a global community of regulators seeking to bring about disruption on an international scale, and to this end chairs the Global Financial Innovation Network.

You can read the full speech here.

Statement on MiFID II inducements and research

8th November

The FCA published a statement expressing their approval of the US Securities and Exchange Commission's (US SEC) extension of no-action relief relating to the Markets in Financial Instruments Directive II (MiFID II) inducements and research provisions.

The SEC staff 'no action letter' was due to expire on 3 July 2020, but the US SEC announced an extension until 3 July 2023, to address the potential conflict between US regulation and MiFID II.

For the remainder of the current and extended period of no-action relief, broker-dealers subject to the US regime may receive payments for unbundled research from firms subject to MiFID II or equivalent EU member state rules without being considered an investment adviser under US law. This will also apply to UK firms should EU withdrawal occur before or during the extended period.

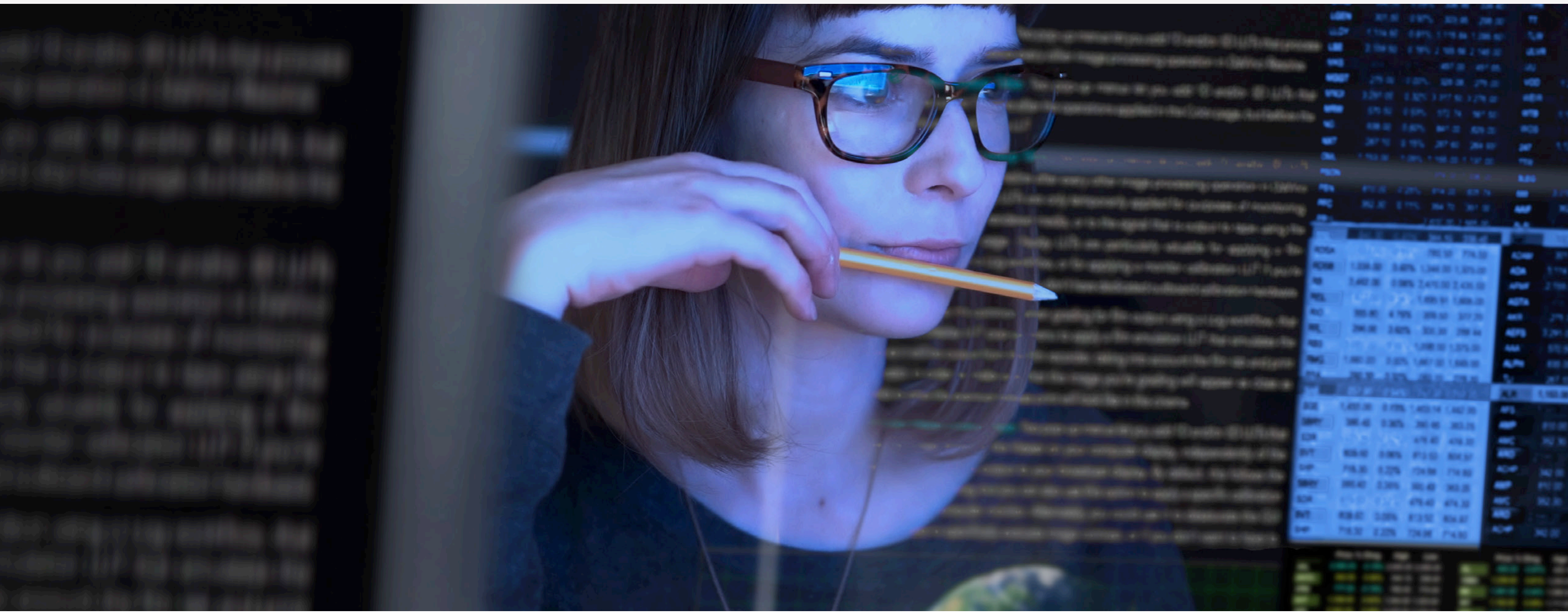
In September 2019, the FCA published a multi-firm review which found that rules have improved asset managers' accountability over costs, saving millions for investors. The FCA state they will conduct further work in 1-2 years' time to assess firms' ongoing compliance with rules and developments in the market research market.

Notes:

MiFID II requires investment firms to either bear research costs directly from their own resources, or adequately disclose and account for research charged to its clients.

The FCA extended the MiFID II inducements and research provisions by applying them to collective portfolio managers subject to the Undertakings for Collective Investment in Transferrable Securities (UCITS) Directive or Alternative Investment Fund Managers Directive (AIFMD). The no-action relief continues to apply where payments for unbundled research are received from firms subject to the FCA's extended application (and also firms subject to MiFID II, or equivalent member state rules).

Read the FCA article here, the US SEC press release here and the SEC staff no action relief letter here.



ESMA advises the European Commission (EC) on the supervisory regime for third country CCPS

8th November

ESMA published three sets of technical advice to the EC concerning third-country central counterparties (TC-CCPs) under the revised European Market Infrastructure Regulation (EMIR 2.2).

The technical advice covered the following areas:

- Guidance around the indicators to be considered in determining whether a TC-CCP is systemically important for the EU or a Member State's financial stability (tiering).
- How to assess comparable compliance, including principles for ESMA's assessment of comparable compliance, and a potential four-step approach to this assessment. Comparable compliance allows a Tier 2 TC-CCP to comply with EMIR requirements by complying with the regulations and requirements of its home country, subject to a specific assessment by ESMA. In practice, to benefit from comparable compliance, Tier 2 TC-CCPs will have to evidence how compliance with the requirements applicable in their home country also satisfies the requirements under EMIR.
- An outline of the fees ESMA will charge for relevant supervisory and administrative costs.

In its press release announcing the publication of the advice, Steven Maijoor, ESMA Chair highlighted the importance of capturing the risks associated with CCPs, stating that its proposals will ensure "proportionate supervision is in place for all CCPs".

The Advice has now been sent to the EC for the development of the corresponding Delegated Acts under EMIR 2.2.

The full press release from ESMA can be found here.

Next steps in transition from LIBOR

21st November

Edwin Schooling Latter, Director of Markets and Wholesale Policy at the FCA, delivered a speech focusing on the importance of firms reducing the risks of continuing to use LIBOR (London Inter Bank Offered Rate). This speech was delivered at the Risk.net LIBOR Summit in London.

Edwin noted that progress has been made with preparations to transition away from LIBOR, for example:

- There is a liquid swaps & futures market based on SONIA (Sterling Overnight Interbank Average Rate).
- New floating rate sterling bonds are now based on SONIA.
- £4.2 billion of LIBOR-referencing securities have been converted to SONIA.
- The first LIBOR loans have been converted to SONIA.

However, there remains much to do before the end of 2021, when market participants must stop referencing LIBOR, including:

- Significant volumes of new LIBOR swaps maturing after the end of 2021 continue to be issued, despite new sterling LIBOR bond issuance appearing to have ceased. Market makers will be encouraged to make SONIA the market convention from Q1 2020.
- Corporate lending continues to reference LIBOR and a target of Q3 2020 has been set for this to cease.
- Further progress is needed in the loans and swaps markets as the risks of continuing to rely on contracts which reference LIBOR beyond the end of 2021 are rising.
- It is unclear precisely how LIBOR will 'end' and market participants are encouraged to prepare for all possible variations, including where LIBOR continues to be published beyond the end of 2021 but no longer meets the Benchmark Regulations 'representative' test.

In conclusion, Edwin noted that the best way to avoid LIBOR-related risks was to move away from LIBOR altogether, but that contractual fall backs may offer a temporary solution for those not yet ready to leave LIBOR. The months ahead are critical in ensuring a successful and smooth transition from LIBOR by the end of 2021.

You can read the full speech here.

MIFID investment firms will need to use a new form to notify FCA of management body changes for Non-SMF Directors

2nd December

From 9 December 2019, MIFID investment firms and optional exempt firms must use a new form to submit information to the FCA when appointing or withdrawing Non-SMF Directors to or from their management body. The form can be found here.

In the event that a firm's management body changes, the form must be downloaded, completed and emailed to the FCA via NonSMFNotification@fca.org.uk. This new process, which is temporary, will be replaced during Q1 2020, when firms will instead be able to submit the form via Connect, the FCA's online platform.

The FCA consulted on the changes in June 2019, with final rules being published in September 2019.

To read the full article click here

FCA meets firms to discuss feedback on Gabriel and improvements to new data collection platform

5th December

The FCA published a video from the roundtable events it held with firms to discuss feedback received through its July 2019 survey on the replacement of Gabriel. The roundtables took place in London, Manchester and Edinburgh. These events provided an opportunity to discuss the changes the FCA will be making to accessibility, notifications, the look and feel of the system and automated saving of data.

The Gabriel replacement project will involve moving over 120,000 users and data from over 52,000 firms to a new platform. The FCA will communicate in good time before any action is required by firms and other Gabriel users to start using the new system.

The FCA will also continue to communicate with and involve stakeholders in its plans to deliver and improve the new data collection system.

To read the full article click here.

ESMA issues 2019 report on Accepted Market Practices under MAR

13th December

ESMA has published today its second annual report on the application of accepted market practices (AMPs) in accordance with the Market Abuse Regulation (MAR).

Under MAR, ESMA has a prescribed a role in monitoring the application of AMPs by submitting an annual report to the European Commission on how AMPs are applied in relevant markets.

In order to establish an AMP under MAR, a National Competent Authority must notify ESMA and other NCAs of their intention at least three months before the AMP is intended to take effect. ESMA is required within two months of the receipt of the notification by an NCA to issue an opinion, either positive or negative, on the intended AMP and publish it on its website.

ESMA's report provides an overview of the establishment and application of AMPs in the EU after MAR became applicable, including the AMPs established under the Market Abuse Directive that remained applicable afterwards. The report examines, for example, AMPs established by the Spanish Comisión Nacional del Mercado de Valores (CNMV), the Portugese Comissão do Mercado de Valores Mobiliários (CMVM) and the French Autorité des Marchés Financiers.

AMPs are a defense against allegations of market manipulation dealings in financial markets carried out for legitimate reasons. Activity in conformity with an established AMP will not constitute market abuse.

To see the full annual report, click here.

ESAs transform the way competent authorities cooperate with each other on AML/CFT matters

16th December

The three European Supervisory Authorities (European Banking Authority, European Insurance and Occupational Pensions Authority and European Securities and Markets Authority), published Joint guidelines on cooperation and information exchange, establishing colleges of anti-money laundering and countering the financing of terrorism (AML/CFT) supervisors to ensure effective cooperation and information exchange between competent authorities. These colleges of AML/CFT supervisors ("Colleges") will provide a platform for sharing information.

Recent AML/CFT cases involving EU banks suggest that supervisors are failing to communicate effectively with their EU counterparts in relation to firms operating internationally. The Guidelines will ensure that supervisors from different Member States will have a formal cooperation framework and effective AML/CFT supervision of firms that operate on a cross-border basis.

These Guidelines require supervisors to form Colleges for firms operating in more than three Member States. They also contain rules governing the establishment and operation of Colleges which will bring together AML/CFT supervisors of the same firm, and other relevant parties, such as prudential supervisors and AML/CFT supervisors from third countries, ensuring that all supervisors have access to comprehensive information about the firm to inform their risk assessment and supervisory approach. The Colleges will allow supervisors to agree on a common approach and coordinated actions.

The full article is available here.

HMRC letters in respect of money received from offshore investment funds

20th November

In response to information received from overseas tax authorities regarding UK tax payers holding investments in offshore funds, HMRC have sent a number of 'nudge letters' to UK investors to remind them of their UK tax obligations arising from their investments in these funds.

The correct UK tax treatment of any income or gains from these funds will depend on whether the fund has UK reporting fund status or not. Broadly speaking, gains made on disposal of units in a non-reporting fund are subject to income tax while gains in a reporting fund receive capital gains tax treatment. Any ERI allocated by a reporting fund will also need to be included in the UK tax return together with any interest and dividends received. Investors will need to ensure that the details in tax reporting packs provided to them includes all amounts arising from investments in offshore funds.

If you (or your client) receives a nudge letter, you should check whether any additional income from offshore fund holdings should be included in the 2018/2019 tax return. If this has already been filed, the return can still be amended. You should also check that any previous tax returns are correct. While the HMRC's letter is not saying that tax has been underpaid, they do undertake a risk assessment before sending these letters out.

Where there has been failure to disclose tax liabilities arising from assets held abroad, penalties of up to 200% may apply.

Duff & Phelps' tax specialists can help you understand whether there is any disclosure required regarding an offshore investment and if there has been any under reporting of UK tax. Our team can also advise on the best course of action if underpayment has occurred.

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EUROPEAN SERVICES - BEST CONSULTANCY FIRM
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