FMConsult compliance solutions

2021 Regulatory Bulletin Issue 1

"Everyone experiences tough times; it's a measure of your determination and dedication how you deal with them and how you can come through them"

- Lakshmi Mittal

Happy New Year from all at FMConsult!

With the Brexit Transition Period now over Regulators are working hard to release statements and guidance to Firms that trade to and from the UK to provide clarity to all. All Firms should be aware of Regulatory changes that have been made and which of those apply to them.

UK Regulatory News

FCA publishes final Brexit instruments and Temporary Transitional Power (TTP) directions

The FCA made further EU exit-related changes to its Handbook and Binding Technical Standards.

These changes ensure that a functioning regulatory and legal framework for financial services continues to be in place after the transition period.

This update follows the publication in September of the FCA's Quarterly Consultation Paper (CP20/18) containing draft, onshoring-related instruments. The final instruments are largely unchanged from CP20/18.

The TTP directions were also made and published. The TTP applies transitional provisions to financial services legislation for a temporary period. The TTP will be applied on a broad basis from the end of the transition period until 31 March 2022.

Firms will be able to see which changes will apply to them by reviewing the new Handbook site alongside the updated TTP information.

Regulatory change for firms as Brexit transition period ends

As of 11pm on 31 December 2020, the transition period ended and EU law no longer applies in the UK. For many financial services businesses, this means changes to existing systems and services.

Passporting between the UK and EEA states has ended and the temporary permissions regime (TPR) has now come into effect for those firms and funds that notified us that they wanted to enter this regime.

Alongside the TPR, the Government has created the financial services contracts regime (FSCR). This allows, for a limited period, EEA passporting firms not in the TPR to continue to service UK contracts.

The extent to which UK firms can continue to provide services to customers in the EEA depends on local law and local regulators' expectations. The FCA expects UK firms to take the steps available to them to make sure they act consistently with these local laws and expectations. The FCA are clear that firms' decisions need to be guided by obtaining appropriate outcomes for their customers, wherever they are based.

Firms should also be prepared for the regulatory changes that have come into force.

FCA publishes first consultation on new prudential regime for UK investment firms.

The FCA is seeking views on its proposed rules to introduce the UK Investment Firm Prudential Regime (IFPR) for FCA prudentially-regulated investment firms.

This is the first of 3 consultations that the FCA will issue to introduce the regime in January 2022. Final rules will be published over the course of this year.

The new regime will streamline and simplify the prudential requirements for solo-regulated investment firms in the UK. At present, there are many different regimes which apply depending on size of firm and type of investment business. However in any simplification there are some firms requirements that will increase – in particular **if you are currently a CAD-exempt firm you may find a significant increase in Capital requirements** – please contact FMConsult for further details.

The new rules will extend the framework for prudential requirements to consider the potential harm FCA investment firms pose to clients, consumers and the market. It's important that FCA investment firms minimise the harm they could cause consumers.

Introducing the IFPR means that there will be a single prudential regime for all FCA investment firms. It should reduce barriers to entry and allow for better competition between investment firms.

It is critical that firms adequately prepare for the regime. The FCA is keen to receive feedback. The consultation period closes on Friday 5 February 2021.

Existing firms should note that the FCA have been checking to see whether firms, including ACDs are making use of the Wind-down Guidance.

FCA establishes Temporary Registration Regime for cryptoasset businesses.

The FCA is advised customers of cryptoasset firms which should have applied to the FCA, but have not done so, that they had to withdraw their cryptoassets or money by 10 January 2021.

From 10 January 2020, the FCA became the anti-money laundering and counter terrorist financing supervisor for cryptoasset firms. From this date, 'existing cryptoasset businesses' (i.e. firms operating immediately before 10 January 2020) have had to comply with the Money Laundering Regulations; such firms were required to be registered with the FCA by 10 January 2021.

New businesses (who began operating after 10 January 2020), are required to obtain full registration with the FCA before conducting business.

The Temporary Registration Regime is for existing cryptoasset businesses which have applied for registration before 16 December 2020, and whose applications are still being assessed. This is to enable those existing businesses to continue to trade after 9 January 2021 until 9 July 2021, pending the FCA's determination of their application.

Firms that did not submit an application by 15 December 2020 will not be eligible for the temporary registration regime. They will need to return cryptoassets to customers and to have stopped trading by 10 January 2021. Firms that do not stop trading by that date are at risk of being subject to the FCA's criminal and civil enforcement powers.

SM&CR and coronavirus: the FCA expectations for solo-regulated firms - December 2020 update

As firms have adapted to the impact of the pandemic over the past few months, the FCA's expectation is that firms' application of the SM&CR rules returns to normal.

As before, the FCA does not require firms to have a single Senior Manager responsible for their coronavirus response. Firms should allocate these responsibilities in the way which best enables them to manage the risks they face.

As most firms have now adapted to the new ways of working, the FCA now expect firms to apply the notification requirements as normal and submit a Form J when significant changes are made to SoRs.

The FCA previously issued a Modification by Consent to the 12-week rule to support firms using temporary arrangements during the crisis. If temporary arrangements made as a result of the pandemic lasted longer than 12 weeks, firms could notify us that they consented to an extension of the 12-week rule. The modification by consent is still available. However, a firm cannot consent to the modification after 30 April 2021 and all modifications consented to before then will come to an end on that date.

FCA introduces rule to enhance climate-related disclosures.

The FCA has published a Policy Statement and final rule and guidance promoting better climate-related financial disclosures for UK premium listed commercial companies.

Companies will be required to include a statement in their annual financial report which sets out whether their disclosures are consistent with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD), and to explain if they have not done so.

The rule will apply for accounting periods beginning on or after 1 January 2021, meaning the first annual financial reports subject to the FCA's rule would then be published in spring 2022.

Along with PS20/17, the FCA are issuing a Technical Note clarifying existing disclosure obligations in EU legislation and the FCA's Handbook.

FCA confirms speculative mini-bond mass-marketing ban.

The FCA has confirmed proposals to permanently ban the mass-marketing of speculative illiquid securities - including speculative mini-bonds - to retail investors.

A temporary ban was introduced without consultation from 1 January 2021 following serious concerns that speculative mini-bonds were being promoted to retail investors who neither understood the risks involved, nor could afford the potential financial losses.

Protecting consumers from harm in the investment market was identified as a priority in the FCA's 2020/21 Business Plan. As part of that work, the FCA is currently reviewing feedback to its Call for Input on how the consumer investments market can be improved. The FCA has also made clear that online platforms, such as Google, play an increasingly significant role in communicating financial promotions to consumers. These firms need to do more to stamp out fraud and misleading adverts and bear clear legal liability for the financial promotions they highlight.

Statement on use of the Temporary Transitional Power to modify the UK's derivatives trading obligation.

The UK has implemented the G20 commitment to improve over-the-counter derivatives markets by onshoring the Markets in Financial Instruments Regulation (MiFIR) derivatives trading obligation (DTO) under the EU Withdrawal Act. The UK DTO applies to the same classes of derivatives as the EU DTO.

The FCA welcomes the announcement that the UK and EU have agreed a Trade and Cooperation Agreement and the associated Joint Declaration on financial services regulatory cooperation. The FCA continues to view the agreement of mutual equivalence between the UK and EU as the best way to avoid disruption for market participants and avoid fragmentation of liquidity in DTO products, reducing costs for investors.

Where firms that are subject to the UK DTO trade with, or on behalf of, EU clients that are subject to the EU DTO, they will be able to transact or execute those trades on EU venues providing that:

- firms take reasonable steps to be satisfied the client does not have arrangements in place to execute the trade on a trading venue to which both the UK and EU have granted equivalence; and
- the EU venue has the necessary regulatory status to do business in the UK – such venues include those that are a Recognised Overseas Investment Exchange, have been granted the relevant temporary permission, or are certain that they benefit from the Overseas Person Exclusion.

This modification of the application of the UK DTO applies to UK firms, EU firms using the UK's temporary permissions regime (TPR), and branches of overseas firms in the UK.

The FCA expects firms and other regulated persons to be able to demonstrate they are taking all reasonable steps during the first quarter of 2021 to ensure compliance with the UK DTO.

FCA publishes coronavirus financial resilience survey data.

The FCA has published the results of its coronavirus financial resilience surveys. The surveys were sent to solo-regulated firms to inform the FCA of the impact of coronavirus on firms' financial resilience. In response to the crisis, the FCA has been monitoring the effects of the economic downturn on firms' solvency by rapidly increasing the data it collects on firms. The surveys have been sent to 23,000 solo-regulated firms to understand the real-time effect the pandemic is having on the finances of the firms the FCA prudentially regulates.

The survey results show that between February 2020(pre-lockdown) and May/June 2020(during the impact of the first lockdown), firms across the sectors experienced significant change in their total amount of liquidity. Retail Investments, Retail Lending and Wholesale Financial Markets sectors saw an increase in liquidity between the 2 reporting periods. Insurance Intermediaries & Brokers, Payments & E-Money and Investment Management sectors saw a decrease in available liquidity.

When asked whether they expected coronavirus to have a negative impact on their net income, 59% of respondents had said that they did.

The Payments & E-money sector has the lowest proportion of profitable firms, followed by Wholesale Financial Markets, Investment Management, Insurance Intermediaries & Brokers, Retail Lending and Retail Investments.

Retail Lending had made most use of the available government support (49% of Retail Lending firms had furloughed staff and 36% had received a government backed loan), followed by Insurance Intermediaries & Brokers (44% had furloughed staff and 19% had received a loan), Retail Investments (37% had furloughed staff and 15% had received a loan), Payments & E-Money (36% had furloughed staff and 11% had received a loan), Wholesale Financial Markets (16% had furloughed staff and 11% had received a loan) and finally Investment Management (8% had furloughed staff and 3% had received a loan).

FCA publishes evaluation of its work on the financial advice market

The FCA has published an evaluation of the impact of the Retail Distribution Review (RDR) and the Financial Advice Market Review (FAMR).

Both the RDR and FAMR (the latter carried out in collaboration with HM Treasury) sought to improve the distribution of retail financial services products, and the FCA committed to evaluate their impact, to test whether they delivered their desired outcomes. The aim of the RDR was to establish a resilient, effective and attractive retail investment market that consumers had confidence in and trusted.

The objective of FAMR was to identify ways to make the UK's financial advice market work better for consumers. The evaluation found evidence of some improvements in the market since the conclusion of FAMR.

The evaluation also found that while more consumers are getting the support they need, further innovation could help even more consumers make better use of their finances.

- Many consumers are still holding money in cash that could be invested to provide potentially higher returns, but they have not sought or received the help with their finances that would help them to make better investment decisions.
- The industry offers a range of services but there is significant clustering around certain service types and price points. More innovation in services can help drive greater competition between firms across the market.
- More tailored guidance services and simpler advice services could help to attract more consumers towards the help they need. However, during our review, some firms raised concerns about understanding the point at which more general forms of consumer support become advice, suggesting this limits their ability to innovate.

FCA responds to independent reviews into its regulation of two Firms.

The FCA has accepted the nine recommendations addressed solely to the FCA in one of the Reviews (Firm 1) and the five lessons identified by the other Review (Firm 2).

The review of firm 1 has assessed the FCA's actions, policies and approach when regulating the Firm between April 2014 and January 2019. In December 2018, the FCA ordered the Firm to withdraw its promotional material. On 30 January 2019, the Firm entered administration.

The Review of Firm2 has assessed the Financial Services Authority's and the FCA's approach and response to intelligence, and the FCA's approach to and involvement in the mediated negotiations before the launch of enforcement investigations in March 2015.

Charles Randell, Chair of the FCA, said:

'*There are a number of things we could have done better in our supervision of these two firms and both reports highlight the need for the FCA to continue to change to better protect consumers from harm. We accept all the recommendations that have been made to the FCA and we are profoundly sorry for the mistakes we have made. Over the last few years we have already made significant changes in our approach to supervising firms. We have learned considerable lessons from what happened'.*

Nikhil Rathi outlined key actions the FCA will take in the next six months:

- Restructuring the FCA to join up its policy, supervision and competition functions
- Becoming a more data-enabled regulator through the recruitment of a Chief Data, Information and Intelligence Officer and the establishment of a separate programme of change that transforms the way they handle and prioritise information and intelligence
- Undertake a "use it or lose it" exercise, with firms that have not used their regulatory permissions to earn any regulated income for the last 12 months at risk of having their Authorisation revoked
- Take forward new measures to tackle pension scams with DWP, once the Pension Schemes Bill has received Royal Assent
- Enhance training for all frontline Supervisory, Authorisation and Enforcement staff
- Recruit additional prudential specialists to act as quality assurance and assess firms with complex business models

Work with the Government to tackle scams advertised and promoted on Google and other online platforms; and disrupt scams and warn consumers of the risks by stepping up our own consumer campaigns

FCA fines leading British Bank £26 million over treatment of customers in financial difficulty

The FCA has fined the Bank £26 million for failures in relation to their treatment of consumer credit customers who fell into arrears or experienced financial difficulties.

The Bank has pro-actively redressed these customers, paying over £273 million to at least 1,530,000 customer accounts since 2017. The redress programme is close to completion.

Between April 2014 and December 2018 the FCA found that the Bank:

- failed to follow its customers' contact policies for customers who fell into arrears
- failed to have appropriate conversations with customers to help understand the reasons for the arrears
- failed to properly understand customers' circumstances leading it to offer unaffordable, or unsustainable, forbearance solutions

The FCA requires consumer credit firms to take adequate measures to properly understand customers' financial difficulties and show forbearance and due consideration to customers in arrears or in financial difficulties.

The Bank has contacted all customers whom they think may be due for compensation. The FCA has monitored this programme.

The FCA took the redress programme into account when setting its fine. The Bank qualified for a 30% discount and the fine would otherwise have been £37,223,500.

FCA fines a stockbroking firm £8.96 million over safeguarding and compliance failures

The Firm has been fined for failing to adequately protect client assets, carrying out a regulated activity without permission and making a false statement to the FCA. Customers affected by the breaches were all retail customers, who require the greatest level of protection.

The breaches occurred between August 2017 and April 2019, after the firm changed its business model. Client money was swept across from the UK Firm to its affiliate, a firm based in the United States.

The client assets, which were subject to UK rules, were held in the Firm's general pool, which contained both firm and client money and which was held for both UK and non-UK clients. The firm did not at all times have permission to safeguard and administer custody assets, and failed to notify the FCA of the breach when applying for the correct permission.

The firm made a false statement to the FCA. Without making adequate enquiries to check whether this was correct, the firm inaccurately informed the FCA that its auditors had confirmed that it had adequate systems and controls in place to protect client assets.

The firm took remedial action at various points after discovering the breaches. There was no actual loss of client assets and the UK Firm stopped holding client assets from 1 January 2020.

The firm agreed to settle and qualified for a 30% discount, without which the fine would have been £12,804,600.

FCA fines and prohibits hedge fund Chief Investment Officer for market abuse

The FCA has fined a former portfolio manager, partner and Chief Investment Officer, £100,000 for market abuse and prohibited him from performing any functions in relation to regulated activity.

Following an investigation, the FCA found that the Chief Investment Officer engaged in market abuse by creating a false and misleading impression as to the supply and demand for equities between 20 January and 15 May 2017.

On multiple occasions, the Chief Investment Officer placed large misleading orders for Contracts for Difference, referenced to equities, which he did not intend to execute. At the same time, he placed smaller orders that he did intend to execute on the opposite side of the order book to the misleading orders.

Through his large misleading orders, the Chief Investment Officer falsely represented to the market an intention to buy/sell when his true intention was the opposite. He was aware of the risk that his actions might constitute market manipulation, but recklessly went ahead with those actions anyway.

The trading undertaken by the Chief Investment Officer was identified by the FCA's internal surveillance systems. The FCA ingests order book data from the leading UK equity trading venues and then runs surveillance algorithms, designed to identify potentially abusive behaviours, across that consolidated data set.

FCA fines an Independent financial advice firm £107,200

Independent financial advice firm is fined for providing its customers with unsuitable pension switching and transfer advice and failing to manage its conflicts of interest.

Between March 2010 and December 2012, the Warrington-based firm recommended that 114 customers transfer their pensions into self-invested personal pensions (SIPPs), without providing any advice on the underlying investments which were to be held in those SIPPs. These investments were often high-risk, esoteric and illiquid. The total amount invested in this way by customers was just over £6,000,000.

The FCA found that the Firm were aware that the Investments were potentially high-risk and failed to take reasonable care to ensure the suitability of its advice for these customers. Accordingly, the Firm breached Principle 9 of the FCA's Principles for Businesses (the Principles).

To date, the Firm has paid redress of £2,668,819.97 to 41 customers who have been impacted by this failing.

Between January 2013 and November 2017, the Firm also failed to ensure that it identified and managed potential conflicts of interest fairly between itself and its customers, in breach of Principle 8 of the FCA's Principles.

Insider dealing convictions upheld by the Court of Appeal

On 16 December, the Court of Appeal (Criminal Division) upheld the convictions of two Individuals for insider dealing.

After an FCA investigation and a trial at Southwark Crown Court, in June 2019, the two individuals were each convicted of five offences of insider dealing in 2013/4 and were sentenced to 3 years' imprisonment. They appealed their convictions alleging insufficient disclosure by the FCA before, during and after the trial made their convictions unsafe and they were released on bail pending the court's decision.

The Court of Appeal dismissed the appeals and found there was no irregularity or unfairness.

The two individuals must now complete their sentences of imprisonment. They are now required to surrender to custody to serve the remainder of their sentences.

One of the individuals was employed as a senior compliance officer at an investment bank and abused her position to access inside information on compliance systems which she passed to her family friend (the other individual), an experienced day trader of financial securities.

Irish Regulatory News

GDPR - New SCCs

The European Commission has published the draft standard contractual clauses for transferring personal data to non-EU countries ("SCCs") for consultation. The final draft of the SCCs is expected to be published in early 2021 and the current draft of the SCCs indicates that the SCCs must then be applied to any new contracts entered into with a grace period of 12 months to replace and update existing standard contractual clauses.

The SCCs published by the European Commission significantly improve the various existing standard contractual clauses for international transfers of personal data.

GDPR – Twitter update

The Irish Data Protection Commission (DPC) has announced the conclusion of its inquiry into Twitter which began in January 2019 following a notification by Twitter that it had unintentionally made some users' private tweets public. The DPC found that Twitter's failure to adequately document the breach and notify the breach on time to the regulator constituted and infringement of Articles 33(1) and 33(5) of the GDPR. The DPC imposed an administrative fine of €450,000 on Twitter in what was described as an "*effective, proportionate and dissuasive measure*".

"Dear CEO" letter to Schedule 2 firms - low level of compliance with Anti-Money Laundering and Counter Financing of Terrorism obligations

The Central Bank has published the outcome of supervisory engagements undertaken in respect of Schedule 2 Firms to assess compliance with their obligations under Criminal Justice (Money Laundering and Terrorist Financing) Act 2010 (CJA 2010). The "Dear CEO" letter outlines the Central Bank's expectations of firms in relation to Anti-Money Laundering/Counter Financing of Terrorism (AML/CFT) and Financial Sanctions (FS) requirements and details follow-up actions to be taken by CEOs and Boards in response to the findings outlined.

The examination, which comprised of both inspections and review meetings, found an overall lack of compliance across all areas of the AML/CFT control framework. There is also poor understanding of the requirements from Board and senior management levels, including at those firms who outsourced their AML/CFT and FS activities to third parties.

The examination identified a number of failings across Schedule 2 Firms, including:

- failure to demonstrate Boards had taken responsibility for the implementation and ongoing oversight of AML/CFT and FS in a number of firms. In many instances, AML/CFT and FS was only included on the Board's agenda following notification from the Central Bank of the upcoming supervisory engagement exercise.
- lack of ongoing and comprehensive assessment and documentation of ML/TF risks that are specific to each firm's consumers and business activities. In a number of instances, this was exacerbated by reliance on 'off the shelf' risk assessment frameworks.
- failure to put in place and implement firm-specific AML/CFT and FS policies and procedures, and failure to review and update these on an ongoing basis.

Director of Enforcement & Anti-Money Laundering, Seána Cunningham said the central bank: "*will continue to engage directly with those firms where compliance weaknesses and failures have been identified to ensure that they are addressed.* ***We also require all firms to review the content of this letter to ensure that they assess their own compliance with the issues identified***."

Statement on the end of Brexit transition period

While most financial services providers are well prepared for the end of the transition period, it means that UK authorised firms will no longer be able to provide financial services to Irish customers on a cross-border basis (passporting). Any customer who currently uses the services of a UK-based financial services provider, and has not yet been contacted by them, is advised to contact their provider to confirm whether they have obtained all necessary authorisations to allow them to continue to provide services to their Irish customers.

In the case of insurance, the Government has enacted the Withdrawal of the United Kingdom from the European Union (Consequential Provisions) Act 2020. Among other things, this Act introduces a temporary run-off regime of 15 years for those insurance firms that meet the conditions set out in that legislation. This will mean that for any customers who hold a policy with a UK service their policy can remain valid for this period.

From 1 January 2021, due to European regulatory requirements, Irish creditors with direct debits in place for UK customers may need to provide their bank with additional information to avoid payment requests being rejected.

Central Bank of Ireland and IOSCO report on retail market conduct issues arising from Covid-19.

The International Organization of Securities Commission's (IOSCO) Retail Market Conduct Task Force (RMCTF), has published the Retail Market Conduct Task Force Report: Initial Findings and Observations about the Impact of COVID-19 on Retail Market Conduct.

The IOSCO Report details common retail market conduct risks caused or exacerbated by COVID-19 including the unique market environment emanating from the pandemic, the impact on firm and investor behaviour, common drivers of retail misconduct, and corresponding challenges and opportunities for regulators.

In addition, the Report identifies a number of common themes experienced during COVID-19 which highlight the vulnerabilities and risks for retail investors, market participants and regulators, such as high market volatility, heightened financial and psychological stressors, social distancing and remote work requirements.

To mitigate the identified risks and promote investor protection, the Report details practical regulatory tools member organisations can utilise such as:

- proactive supervisory monitoring, including of offerings targeting vulnerable investors;
- targeted and effective enforcement action;
- close cross-border cooperation and regulatory coordination; and
- leveraging the experience from previous crises to enhance agile regulatory approaches.

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UK and Ireland

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- Dublin also provides Fund UCITS IV Reporting, MLRO and Company Secretarial Services.
- Related Training
- Prudential Regulatory Advice

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