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Every action we take, everything we do, is either a victory or defeat in the struggle to become what we want to be.
- Ninon de L'Enclos

The FCA will continue to work closely with Europe, and will expand its involvement in global policymaking. But many of you will know that the FCA has also initiated a debate in recent months about the future of regulation in the UK.

It has been 10 years since the financial crisis and the subsequent reforms the FCA have put in place, and now is the right time to review the approach to regulation. And Brexit provides added impetus to look at things again.

UK's exit from the EU delayed

The EU and the UK agreement to extend the date for the UK's departure from the EU means firms do not need to act to implement Brexit contingency plans for 31 October 2019.

The FCA will be extending the date by which firms and funds should notify it for entry into the temporary permissions regime (TPR[1]) to 30 January 2020. Fund managers will have until 15 January 2020 to inform the FCA if they want to make changes to their existing notification.

Firms should continue to comply with existing regulatory reporting requirements.

Regulation in a changing world Christopher Woolard's speech

The FCA wants the market to work well and to function as its customers expect, for both customers at home and for the UK as one of the world's largest financial centres. Globally the FCA know this is a selling point for UK plc: a proportionate, predictable and well-designed regulatory system with high standards provides the basis for a competitive financial sector.

But the rules of the game have been shifting, especially in the 10 years since the financial crisis. As a regulator of this vital industry, the FCA need to not only respond to these changes – but also to anticipate them. To do that, the FCA needs to have an open discussion about the type of regulation that will best deliver for the public today and tomorrow.

The changing context

The shape that Brexit takes is clearly vitally important. Regardless of the public's perspective, Christopher stressed that the FCA takes no position on the substance of Brexit itself, leaving the European Union may provide UK with an opportunity to do things differently. Although Brexit will shape the context in which the FCA operate, there are other factors at play that in many respects are far bigger and mean the FCA need to engage with this work now.

Christopher outlined three in particular:

1. The first wave of post-crisis regulation is done. Firms are better capitalised and the personal responsibility of their leaders is more embedded. This is a good time to look at what has worked well, and what could be improved;

2. The change in consumer need and attitude so Long-term low interest rates mean the search for return is stronger, just as the tolerance for loss lessens. Consumers are getting older, have less saved and inherit assets later in life; and

3. Innovation has gathered pace so we're moving from an era of digitisation – services moving online – to a truly digital industry drawing on artificial intelligence and machine learning. This transformation is reflected in the new products finding their way direct to consumers over the internet (some good, some bad, some downright fraudulent).

The future of regulation

1. The FCA is to clearly state what outcomes want to see in markets. Most of us don't want to think too much about the products we buy or services we use. But we know if we don't shop around, we may get a worse deal.

   Firms have a responsibility towards to their customers. But the FCA doesn't operate a 'zero-failure' regime. Consumers need to know that risk comes with return; in particular purchasing products outside of the regulatory boundary means you're more likely to lose out.

   Christopher highlighted that the FCA will be issuing an open invitation for firm's thoughts and ideas, as well as setting out some of FCA's own thoughts and ideas. The FCA will publish detailed papers, including an analysis of future market dynamics, a Discussion Paper about our Principles, and a Consultation Paper on the Duty of Care.

2. The FCA is to use everything available in the regulatory toolkit Parliament has given it. In recent years, the FCA have used their tools and powers more creatively in things like the Senior Managers Regime, Project Innovate and price caps. Nonetheless, the FCA must face up to the fact that disclosure has been the go-to solution of regulators and politicians in the UK and Europe for the last 20 years, making up the bulk of the FCA's requirements. But behavioural economics suggests its impact is limited.

3. The third step concerns working with other agencies. Consumers don't care whether the problem lies with legislation, regulation, or industry practices – they simply want them all to work in their interests. So, the FCA are increasingly working with Government, fellow regulators like the Information Commissioner's Office (ICO), and enforcement agencies to think about the right outcomes, rather than each body delivering narrow solutions in respect of their mandates.

4. The fourth step is for the FCA to look at their requirements. The FCA have their Principles, the handbook and a lot of rules. Not to mention, the hundreds of pages of binding technical standards onshored as part of Brexit preparations. The FCA are aware that this affects small business – those lacking Compliance departments – most. While they see the benefits that regulation brings to their firms, many struggle to understand how FCA regulation applies to them.

   The FCA are exploring if there is more, they can make of their Principles to be clearer about their expectations.

5. Much of the FCA Handbook is technology neutral, and the FCA have enabled innovation over the last few years. But the FCA's rules feel increasingly analogue in a digital world. Therefore, the FCA sees the opportunity it presents to bridge the information asymmetry between customers and providers.

[1] Note: The TPR will come into force when the UK leaves the EU, if there is no transition period.

The FCA will be the anti-money laundering and counter terrorist financing (AML/CTF) supervisor for crypto asset businesses, from 10 January 2020.

The Treasury has announced, in the Economic Crime Plan, that the FCA will be the anti-money laundering and counter terrorist financing (AML/CTF) supervisor of UK crypto-assets businesses under The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs).

Evidence of increased risks from growing use of cryptoassets for illicit activity, as well as risks to consumers and markets has resulted in the Government and financial regulators moving to minimize those risks. Key points from the Consultation Paper:

- It falls outside the normal cycle of fees consultation so that the FCA can establish the registration fees for 10/1/20.
- The FCA's responsibility under the new regime will be limited to AML/CTF registration and supervision only.
- As the Treasury has not finalised the activities to be included in the scope of the MLRs, the FCA do not know exactly which businesses will constitute a 'cryptoasset business' and may be required to pay a fee. However, the FCA is consulting on the basis of the Treasury's consultation proposals in April 2019, to ensure they can introduce registration fees when the gateway opens for applications.
- The Treasury are yet to publish their response to their April consultation on 5MLD transposition, setting out the cryptoasset activities that will be included in scope of the MLRs. All activities consulted on in April 2019 are listed below, but the Treasury may decide to reduce or extend the range of activities the FCA oversees.

Cryptoasset activity	As described in the Treasury consultation
Cryptoasset exchange provider	A business that provides the following services: • exchanging fiat currency (government-issued currency) for a cryptoasset (or vice versa) • exchanging 1 cryptoasset for another cryptoasset.
Cryptoasset Automated Teller Machine (ATM)	Physical kiosks that allow users to exchange cryptoassets and fiat currencies
Custodian Wallet Providers	A business that looks after the customer's tokens in its IT system or server and, may administer or transfer the token on behalf of the customer.
Peer to Peer Providers	A business that provides an online marketplace which facilitates the exchange of fiat currencies and cryptoassets (both fiat-to-crypto and crypto-to-crypto) between prospective buyers and sellers.
Issuers of new cryptoassets, e.g. Initial Coin Offering (ICO) or Initial Exchange Offering (IEO)	A business that sells a cryptoasset, promoted or sold as a new type of cryptoasset or one that will become useable in the future, in exchange for fiat currency.
Publication of open-source software e.g. Non-Custodian Wallet providers	A business that provides software such as an application, that may be downloaded and used by a customer on their device to store or administer a token, e.g. a non-custodian wallet application that a customer can download onto a device to store the private key in relation to a token.

Turning technology against financial crime

In a speech by Megan Butler, Executive Director of Supervision – Investment, Wholesale and Specialists at the FCA, she highlighted that the FCA cannot be sure exactly how much money is laundered through the UK, but the best estimate puts it in the range of hundreds of billions of pounds.

Fraud accounts for around one third of all crimes experienced by individuals, and in the last year the FCA have seen a 17% increase in fraud offences, driven by an increase in bank and credit account fraud to 3.8 million offences.

The FCA's endeavour is to monitor entry, devise controls and erect barriers powerful enough to stop criminals from causing further harm. The task is daunting. New technologies are exciting and innovative, giving unprecedented access to new products and services and flexibility in how we use them. More than 5 million people chose to lead an almost cashless lifestyle this year according to UK Finance. However, these technologies also give criminals sophisticated tools to bend the financial system to their own ends – the anonymity granted by virtual currencies being one well-known example.

<u>The FCA's role as the regulator</u>

Beyond setting rules, publishing guidance, supervising firms and sharing intelligence, regulators are also exploring innovative approaches to combatting financial crime. It is clear that this threat needs a collaborative response. That's why the FCA have set up the Sandbox to support firms and their efforts to innovate in RegTech.

The FCA have run two successful TechSprints, which looked at how the fight against financial crime could be aided by better information sharing – whether that be through relatively mature technologies like distributed ledgers or more nascent concepts such as homomorphic encryption. In fact, the latest, which we held in July, focussed specifically on how 'privacy enhancing technologies' (PETs) can facilitate the sharing of intelligence between firms, regulators and international law enforcement agencies without compromising data protection requirements.

The solutions it produced included:

- The use of multi-party computation to drive real-time analysis of payments to combat authorised push payment fraud
- Federated learning technologies to share and identify financial crime typologies across multiple entities
- Using PETs to establish a 'golden pool' of data, supporting better identification of beneficial ownerships by eliminating discrepancies between public registers and firms' own records
- Tougher encryption, enabling firms to make enquiries about higher risk customers to uncover discrepancies in their on-boarding and due diligence processes

Gabriel users share suggestions for our new data collection platform

Over 1,000 users and other Gabriel stakeholders shared their thoughts on the current system in an online survey. The feedback will help in the development of the new platform.

The feedback highlighted these key areas for improvements:

1. Accessing Gabriel – the need to improve the speed of the system and support when accessing the system.
2. Viewing your Gabriel reporting schedule – largely related to the need for changes in the layout of the schedules and in viewing previous data submissions.

3. Submitting data – included the need for better guidance when making a data submission and advancements to the system's data validation processes.

The FCA claims that the new platform will allow them to fix issues quicker and sooner. They will also improve the support and guidance given on Gabriel, and will also be able to see previous submissions made. Early changes to the platform will be technology based, so, for now, there will be no change in how firms provide data.

Developments in the UK Tax Treatment of Fee Rebates and Trail Commissions -The Hargreaves Lansdown Case

UK investment managers paying fee rebates, loyalty bonuses or similar payments to UK investors and certain non-UK investors in collective investment schemes should note recent case law developments regarding the tax treatment of such sums.

Background

In 2013 HMRC announced that fee rebates (and other similar payments to fund investors made by persons other than the fund itself) constitute annual payments for income tax purposes and, in the case of payments made to UK investors and certain non-UK investors, should be paid subject to 20% withholding in respect of basic rate income tax.
In brief, annual payments are sums payable under a legal obligation, which: are recurring or capable of recurrence; constitute income in the hands of the recipient; and are received as "pure income profit" (meaning, broadly, that they are received without the recipient having to do anything in return, over and above the making of an investment).

The Hargreaves Lansdown Case

The Asset Manager argued that HMRC's approach was "an unnecessary and unwarranted attack" on investors, and so challenged HMRC's position in respect of "loyalty bonuses" paid by it. The Asset Manager was successful at the First Tier Tax Tribunal, but on 9 August, the Upper Tribunal overturned this decision, concluding that the First Tier Tax Tribunal had erred in law in deciding that the loyalty payments did not constitute annual payments.

Consequences

The Upper Tribunal's decision reinforces HMRC's position regarding the treatment of fee rebates, loyalty bonuses, the passing on of trail commissions and similar arrangements. UK managers making, or considering making, such payments to UK investors and certain non-UK investors should be aware of the strict contractual interpretation applied by the courts in this context, and should consider whether a withholding obligation applies in respect of such payments.

Since HMRC will look to recover any uncollected withholding from the payer of annual payments, advice should be taken where necessary, and appropriate reserves should be put in place in the case of any uncertainty.

Information for SIPP operators in light of Berkeley Burke administration

On 18 September 2019 the directors of Berkeley Burke SIPP Administration Limited ('BBSAL'), appointed two Joint Administrators. On 2 October 2019 the administrators decided to discontinue BBSAL's appeal of the High Court's judgment about the firm's judicial review of a Financial Ombudsman Service final decision (Berkeley Burke SIPP Administration Limited vs Financial Ombudsman Service Limited).

In light of the administrators' decision, the FCA reminded firms of the 'Dear CEO' letter published in October 2018. This case dealt with Self Invested Pension Plan (SIPP) operators' due diligence obligations when accepting customers' investments, and referenced the Principles for Businesses and / or other rules set out in the FCA's Handbook. If the outcome of this case calls into question a SIPP operator's ability to meet financial commitments as they fall due, they should contact the FCA immediately.

The FCA reminded firms of their obligations to treat complainants fairly and handle complaints according to the rules set out in the Dispute Resolution Handbook. Where a firm receives an ombudsman decision, it should, in accordance with Principle 6, consider whether it ought to act with regard to the position of customers who may have suffered detriment from, or been potentially disadvantaged by, such problems but who have not complained and, if so, take appropriate and proportionate measures to ensure that those customers are given appropriate redress or a proper opportunity to obtain it. If a firm pursues a sale of part or all of its business or assets, it should pay due regard to its implications for customers who may have compensation claims. All directors should comply with their statutory and non-statutory duties as well as complying with the relevant provisions of the FCA Handbook, these include, where a firm is at risk of insolvency, their duties to creditors, such as customers to whom compensation is or may be due.

Update on the LF Woodford Equity Income Fund

On 15 October 2019, Link Fund Solutions Ltd (LFS), the Authorised Corporate Director (ACD) of the LF Woodford Equity Income Fund (WEIF) announced that it will not seek to re-open the WEIF and instead, it will look to wind-up the fund as soon as practicable. LFS considers the winding-up of the WEIF to be in the best interests of all investors and will enable the return of cash to investors at the earliest opportunity. LFS expects the winding-up to begin in mid-January, subject to regulatory approvals. LFS will now request formal approval from the FCA to wind-up the fund.

On 3 June 2019, LFS decided to suspend dealings in the WEIF in order to protect all investors in the fund following an increased level of redemptions. The suspension was designed to give Woodford Investment Management Limited time to reposition the fund's portfolio into more easily sold investments. This would have allowed the WEIF to meet redemption requests. Failure to do so before the re-opening of the fund would risk a further suspension and unequal treatment of investors. Since the suspension on 3 June 2019, the FCA has been in regular contact with LFS while the firm pursued the resolution of this matter.

LFS set various targets for making progress with the repositioning of the fund. Because sufficient progress was not made, LFS has decided it is in the best interests of all investors to seek to wind-up the WEIF rather than continue to reopen the fund.

Winding-up the fund will allow the return of money to investors through a number of distributions, likely to begin in January 2020. This means investors should receive some of their money back sooner than had the fund remained suspended for a longer period. Following LFS's decision to wind-up the WEIF, Woodford Investment Management Ltd will no longer be the investment manager of the fund, with immediate effect and the fund will also be renamed as a result.

The FCA fines an electronic and voice inter-dealer broker £15.4 million

An electronic and voice inter-dealer broker has been fined £15.4 million for failing to conduct its business with due skill, care and diligence, failing to have adequate risk management systems and for failing to be open and cooperative with the FCA. The Rates Division of the broker carried out 'name passing' broking which comprised a significant part of the firms overall business, employing many brokers and generating significant revenues for the firm.

Following an FCA investigation, the FCA found that, between 2008 and 2010, the Rates Division had ineffective controls around broker conduct. Lavish entertainment and a lack of effective controls allowed improper trading to take place, including 'wash' trades (a 'wash' trade involves no change in beneficial ownership and has no legitimate underlying commercial purpose) which generated unwarranted and unusually high amounts of brokerage for the firm. Senior management wrongly believed sufficient systems and controls were in place and obvious red flags of broker misconduct and opportunities to probe were missed. For example, when the firm made inquiries of one broker about the basis for exceedingly high brokerage on one trade the broker responsible said 'you don't want to know' and no steps were taken to identify the reasons.

A spokesman from the FCA explained that this was a long and complex case against the firm. The firm also breached Principle 11 of the FCA's Principles for Businesses by failing to be open and cooperative with the FCA. The FCA requested broker audio tapes in August 2011, and despite having the majority of the audio required by the FCA, they didn't produce the tapes until 2014. This breach is also considered to be serious. Principle 11 is a fundamental plank of the operation of the regulatory system. The firm agreed to resolve this matter and therefore qualified for a 30% discount under the FCA's settlement discount scheme. Without this discount, the fine would have been £22 million.

FCA urges victims of illegal loan scheme to come forward

An Individual was convicted of illegal money lending offences in February 2018 and sentenced to three and a half years in prison. The FCA began confiscation proceedings against the individual in order to recover the financial benefit he obtained from his criminality. Money recovered under the confiscation order can then be used to compensate victims.

The Executive Director of Enforcement and Market Oversight at the FCA said that the individual targeted vulnerable people, and now the individual has been jailed the FCA want to compensate the victims. The FCA have been in contact with victims already but they believe that there are more out there. "We ask anyone who borrowed money to come forward so we can quantify relevant amounts and present the evidence to the court."

Any individual who look out a loan with the individual, or any of their companies, and who has not yet contacted the FCA, should do so by 15 November 2019. Individuals will need to supply sufficient information and supporting documents to demonstrate their loss to the FCA.

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- Outsourced compliance solutions
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- GDPR assistance
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- Financial Crime

UK and Ireland

- Consumer Credit Authorisation, whether you have an interim authorisation or not
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- Dublin also provides Fund UCITS IV Reporting, MLRO and Company Secretarial Services.
- Related Training

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