# 2018 Regulatory Bulletin Issue 8

***"Innovation distinguishes between a leader and a follower."***

***Steve Jobs***

The FCA has announced the creation of the Global Financial Innovation Network (GFIN), building on the FCA's proposal earlier this year to create a 'global sandbox'. The network will seek to provide a more efficient way for innovative firms to interact with regulators, helping them navigate between countries as they look to scale new ideas.

## Banking, insurance and other financial services if there's no Brexit deal

HM Treasury have released a notice to provide stakeholders with information about the impact of the UK leaving the EU without a deal, and the government's approach to ensuring that we have a functioning financial services regulatory framework in any scenario.

**After 29 March 2019 if there's 'no deal'**

When the UK leaves the EU, it will be outside of the EU's framework for financial services regulation. In a 'no deal' scenario, UK firms' position in relation to the EU would be determined by the relevant member state rules and any applicable EU rules that apply to third countries (countries outside of the EEA) at that time.

In order to ensure that a functioning legislative regime is in place the Temporary Permissions Regime (TPR) will allow EEA firms currently passporting into the UK to continue operating in the UK for up to three years after exit, while they apply for full authorisation from UK regulators.

The government has already laid draft secondary legislation that will establish a temporary recognition regime (TRR) for central counterparties (CCPs). This regime will allow non-UK CCPs to continue to provide clearing services to UK firms for a period of up to three years while those CCPs apply for recognition in the UK.

The government will also be bringing forward legislation to deliver transitional arrangements for:

- Central Securities Depositories
- Credit Rating Agencies
- Trade Repositories
- Data Reporting Service Providers
- Systems currently under the Settlement Finality Directive
- Depositaries for authorised funds.

**Financial services firms and funds**

At this stage, firms should continue to plan on the basis that an implementation period will be in place from March 2019 to December 2020, and continue to follow guidance from the regulators.

For any firm that does not wish to continue carrying out regulated activities in the UK, or is unsuccessful in applying for authorisation, provision will be made for them to discontinue their UK regulated activities in an orderly m

Under EU legislation it is possible for fund managers to delegate portfolio management services to a third party in another country, including countries outside the EU. In relation to funds and managers authorised under the relevant EU legislation, there are requirements for cooperation between the supervisory authorities in the relevant EU member state and the non-EU country concerned.

**Individual and business customers- UK-based customers of UK based providers**

For UK-based customers accessing domestic services in the UK provided entirely by UK-based providers, there is unlikely to be any change as a result of exit. If UK customers will be affected by their firm's planning for exit, then this should be clearly communicated to customers by the firm.

**Individual and business customers - UK-based customers of EEA firms operating in the UK**

For UK-based customers who access banking, insurance, investment funds and other financial services with EEA firms currently passporting into the UK, the temporary permissions regimes will enable these firms to continue to provide those services to UK customers for up to three years after exit.

**Individual and business customers - EEA customers (including UK citizens living abroad) of UK firms operating in the EEA**

In the absence of action from the EU, EEA-based customers of UK firms currently passporting into the EEA, including UK citizens living in the EEA, may lose the ability to access existing lending and deposit services, insurance contracts due to UK firms losing their rights to passport into the EEA, affecting the ability of their EEA customers to continue accessing their services. This could impact these firms' ability to continue to service their existing products.

The government has committed to putting in place unilateral action, if necessary, to resolve these issues as far as possible on the UK side. For example, the government has committed to continue to treat prospectuses that are valid in the UK before exit as valid for the remainder of the 12 months from their date of approval, including where that includes a period after the UK exits the EU.

## Preparing your firm for Brexit

**Firms conducting business in the EEA should consider the following:**

- Do you currently provide any regulated products or services to customers resident in the EEA?
- Do you have customers or counterparties based in the EEA, including UK expatriates now based in an EEA country?
- Are you marketing financial products in the EEA? This includes products marketed on a website aimed at consumers in the EEA.
- Do you have agents in the EEA or interact with any intermediary service providers in the EEA?
- Does your firm transfer personal data between the UK and the EEA or vice versa?
- Does your firm have membership of any market infrastructure (trading venues, clearing house, settlement facility) based in the EEA?

- Are you part of a wider corporate group based in the EEA, or does your firm receive any funding from an entity in the EEA?
- Do you outsource or delegate to an EEA firm or does an EEA firm outsource or delegate to you?
- Are you party to legal contracts which refer to EU law?

## The FCA sets out stance on Cross-Border Booking Arrangements

The FCA has published a "Dear CEO" letter to firms, advising them of its position in relation to the use of cross-border booking models in the context of Brexit.

The European Central Bank (ECB) (which carries out a supervisory role in relation to Eurozone banks) has set out fairly detailed expectations for banks wishing to relocate to the Eurozone. In particular, the ECB expects that EU products and transactions with EU clients are booked in the EU, and that risk management capabilities related to such products are located in the EU.

The FCA, in contrast, is not seeking to restrict market access, and simply is concerned that firms with a UK presence structure themselves so as to enable the FCA to supervise their UK business effectively, and to continue to meet the FCA's high-level threshold conditions.

Additionally, the FCA wants to see that, when formulating their plans, firms consider not only their business needs, but also the best interests of their clients.

The FCA states that it is open to a broad range of legal structures and booking models, provided that underlying conduct risks are managed appropriately, and effective governance arrangements are in place. According to the FCA's letter, this means firms need to be able to demonstrate how they have observed and implemented the following principles in relation to their booking models:

- Firms should set out a clear rationale for their booking arrangements, document them, and have them approved by the Board
- Risk management should be appropriate for the firm's booking activities, including hedging arrangements
- Firms should ensure a broad alignment of risk and returns at the entity level
- Firms should have adequate systems and controls in place to ensure that booking arrangements are followed
- Firms should consider whether responsibility for oversight of booking arrangements should be explicit in Senior Managers' Statements of Responsibilities
- Booking arrangements should not be an impediment to the firm's recovery and resolution

## FCA statement on selling high-risk speculative investments to retail clients following ESMA's action on CFD products

In June 2018, the European Securities and Markets Authority (ESMA) finalised temporary measures to restrict the sale, marketing and distribution of contracts for difference (CFDs) to retail clients. These measures now apply across the EU.

In common with other regulators across Europe, the FCA know that other products can create the same kinds of risks to consumers as CFDs, particularly where they expose the investor to significant leverage. ESMA's recent Q&A on its product intervention also highlighted these risks. These substitute products could be sold under a variety of labels but share common features with CFDs and these features may cause large trading losses to retail clients.

The FCA are concerned that firms may consider getting around ESMA's measures by selling other similarly complex products to retail clients. ESMA's Q&A makes clear that firms "should pay particular attention to the leverage made available to retail clients and consider whether the product is offered on terms that act in the best interests of the client" for products that have comparable features to CFDs, such as Turbo Certificates.

The FCA will therefore work with ESMA and other European regulators to monitor and assess the sale of these alternative, speculative products to retail clients.

## FCA collaborates on new consultation to explore the opportunities of a Global Financial Innovation Network

The FCA has, in collaboration with 11 financial regulators and related organisations, announced the creation of the Global Financial Innovation Network (GFIN), building on the FCA's proposal earlier this year to create a 'global sandbox'.

The network will seek to provide a more efficient way for innovative firms to interact with regulators, helping them navigate between countries as they look to scale new ideas. It will also create a new framework for co-operation between financial services regulators on innovation related topics, sharing different experiences and approaches.

## FCA consults on rules and guidance to improve conduct and communications in payment services and e-money firms

The FCA is consulting on rules and guidance to improve conduct standards and communications in the payment services and e-money sectors.

The Consultation Paper proposes to extend the application of the Principles for Businesses and certain specific rules about promotions and communications so that they cover wider categories of businesses that the FCA regulate (including businesses authorised or registered under the Payment Services Regulations or the Electronic Money Regulations). This includes broader types of activities (including the provision of payment services and the issuing of electronic money where they are not connected to an activity regulated under the Financial Services and Markets Act (FSMA)).

The FCA has also proposed new guidance to help ensure that firms do not mislead consumers when they are advertising payment services that involve a currency conversion. This delivers on a commitment by the FCA made last year, to act on concerns about firms' use of currency converter tools in relation to their currency transfer services.

These measures should help customers to better understand that standards the FCA expects of firms in the market, and will make it easier for the FCA to intervene when it sees harm. The FCA's disciplinary powers under FSMA would apply to breaches of the proposed new rules,including those relating to marketing and communications, and this would reinforce the effectiveness of the FCA's enforcement approach across the markets for payment services and electronic money.

## FCA announces new rules for peer-to-peer lending

The FCA has announced new plans which will see a crackdown on P2P lending and the loan-based crowdfunding industry in general following concerns that consumers are at risk of investing in things they do not understand.

P2P lending was last reviewed by the FCA in December 2016, announcing at the time, its plans to address the gap in protections for customers. Since then it has monitored the situation and noted the variety of loan-based crowdfunding business models, of which some are becoming increasingly complex. Whilst the FCA regulates loan-based crowdfunding (also known as P2P lending) and investment-based crowdfunding (which falls outside of the FCA's present review), the FCA does not regulate donation-based or reward-based crowdfunding (hence, both of these fall outside of the FCA's review).

As part of its ongoing monitoring, the FCA has also noted poor practice among some firms in the crowdfunding industry. The proposals detailed below aim to improve standards in the sector whilst still leaving scope for further innovation.

The consultation is aimed at establishing views on the following proposals:

- Proposals to ensure investors receive clear and accurate information about a potential investment and understand the risks involved
- Ensure investors are adequately remunerated for the risk they are taking
- Transparent and robust systems for assessing the risk, value and price of loans, and fair/transparent charges to investors
- Promote good governance and orderly business practices
- Proposals to extend existing marketing restrictions for investment-based crowdfunding platforms to loan-based platforms

## Regulators warn public of pension scammer tactics as victims report losing an average of £91,000 in 2017

A new campaign to tackle pension scams has now been launched as the latest figures reveal that victims of pension scammers lost an average of £91,000 each in 2017.

The Financial Conduct Authority (FCA) and The Pensions Regulator (TPR) have joined forces to urge the public to be on their guard when receiving unexpected offers about their pension and to check who they are dealing with. The two regulators have launched a new ScamSmart advertising campaign targeting pension holders aged 45-65, the group most at risk of pension scams. This comes as a new poll commissioned by the regulators reveals that almost a third (32%) of pension holders aged 45 to 65 would not know how to check whether they are speaking with a legitimate pensions adviser or provider.

## Enforcement cases

**Upper Tribunal upholds FCA decision to fine and ban Chief Executive of advisory firm**

On 31 July 2018, the Upper Tribunal upheld the Financial Conduct Authority's (FCA) decision to Director and CF1 of the advisory firm from performing any FCA significant influence or senior management function, on the basis of his fundamental lack of competence and capability to perform such functions. The Tribunal also directed the FCA to impose a fine on the individual of £60,000 on the basis that he had breached the FCA's Statement of Principle 7 by failing to ensure that the company complied with its obligations under the regulatory regime.

Between January 2010 and January 2013, the company provided advice to 1,661 customers who were considering transferring or switching their pension funds via self-invested personal pensions (SIPPs).

The Tribunal found that the customers were given wholly unsuitable advice to transfer pension benefits into a SIPP which was to be invested in either a single, or a very small number of, inherently risky overseas property investments.

The Tribunal also found that the Chief Executive had a significant financial interest in the outcome of the unsuitable advice the company was giving to customers.

To date, compensation totalling over £55.6 million has been paid by the Financial Services Compensation Scheme (FSCS) in relation to claims upheld against the company. This does not cover all the losses suffered by investors, which the FSCS assesses at more than £106.5 million.

**FCA brings charges over alleged futures-trading scheme**

Investors were lied to as part of a criminal unauthorised futures-trading scam, the UK's financial watchdog has alleged in court.

The defendant appeared at the City of London magistrates' court on Tuesday to face three charges filed by the Financial Conduct Authority. He faces two counts of fraud and one of operating a collective investment scheme without authorisation, the FCA said in a statement. He faces jail time if convicted.

Over nine years, he ran three funds which the FCA said never got the proper regulatory authorisation to seek outside investment.

According to the indictment, between 2008 and 2017, he made misleading statements to investors, "namely that they were making profits on their investments" and that "he had been trading profitably in futures for many years and/or would invest their funds in financial futures".

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- Related Training

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