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Brexit Update

Of relevance to
All firms

Useful links

[bankofengland.co.uk/financial-stability-report/2018/november-2018](https://www.bankofengland.co.uk/financial-stability-report/2018/november-2018)

On 25 November 2018, the EU Council of Ministers met in Brussels and agreed to the draft UK Withdrawal Agreement. The draft Withdrawal Agreement must now be ratified by the UK Parliament and assuming it does so, subsequently by the European Parliament.

The UK Parliament will debate the Withdrawal Agreement and vote on it. The House of Commons will debate it between Tuesday 4 December and Tuesday 11 December 2018. There will then be a vote on Tuesday 11 December 2018. The House of Lords will debate the Withdrawal Agreement between Tuesday 4 December and Monday 10 December. However, the motion voted on in the House of Lords is secondary to that in the House of Commons.

The Bank of England has produced some very useful Brexit impact analysis in pages 17 — 33 of its Financial Stability Report November 2018 (see <https://www.bankofengland.co.uk/financial-stability-report/2018/november-2018>).

The Financial Stability Report provides a useful summary of the expected impact of what the Bank of England calls a “Disorderly Brexit” (where the financial sector reverts to World Trade Organisation rules from 30 March 2019) and a “Disruptive Brexit” (where there is some agreement on aspects of transition in financial markets with some market disruption, but the impact is less severe than under a Disorderly Brexit). Although it is not a forecast or prediction, the Bank of England’s analysis of a Brexit scenario under Disorderly and Disruptive Brexit models, suggests the impact on the UK economy and on consumers will be quite negative to very severe.

The Bank of England also provides some useful commentary at pages 29 — 33 on issues to consider in terms of disruption to financial services, including a checklist at page 29 dealing with legal frameworks, cross-border contracts and availability of new financial services.

Impact of Brexit on Financial Services Passports

Under the Brexit Withdrawal Agreement agreed between the UK and the EU on 25 November 2018, the outbound and in-bound passporting rights (from the UK to other EU/EEA Host States and vice versa) under all Directives that provide for passporting rights will remain in place during any Transition Period, providing the Withdrawal Agreement is approved by the UK Parliament and subsequently by the European Parliament.

The passport rights will cease under one of the two possible circumstances set out as follows:

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No Deal Hard Brexit

Passports cease from 30 March 2019 — if the Withdrawal Agreement agreed in Brussels on 25 November 2018 is not approved by the UK Parliament (or subsequently is not approved by the European Parliament);

Transitional Deal

Passports cease from 1 January 2021 — when the Transition Period ends (unless some form of equivalence is negotiated during the Transition Period for the future UK-EU trading relationship).

It has been confirmed that the UK Parliament will vote on the Withdrawal Agreement on Tuesday 11 December 2018.

Single Financial Services Market — Passports Available

Directive/Regulation	Passports Available
Alternative Investment Funds Managers Directive (AIFMD)	For managers: <ul style="list-style-type: none"> ▪ Cross border marketing of EU AIFs to professional investors ▪ Marketing of non-EU AIFs to professional investors in all Member States (in certain cases) ▪ Cross-border management of EU AIFs either on a branch or services basis ▪ Provision of certain specified MiFID services either on a branch or services basis
Insurance Distribution Directive (IDD) (Formerly Insurance Mediation Directive (IMD))	For insurance intermediaries: <ul style="list-style-type: none"> ▪ Establishment of branches or provision of insurance mediation services
Markets in Financial Instruments Directive (MiFID) 2	Right for investment firms to: <ul style="list-style-type: none"> ▪ Provide cross border investment services, including through a tied agent ▪ Establish a branch (subject to a notification procedure) and provide investment services from that branch outside of the passporting provisions for investment firms above, there are several other provisions in MiFID8 which facilitate cross-border activity in the EEA. ▪ A Member State has to ensure that investment firms from another Member State have access to clearing and settlement systems in its jurisdiction on the same basis as investment firms for which it is the home Member State.

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Directive/Regulation	Passports Available
Markets in Financial Instruments Directive (MiFID) 2	<ul style="list-style-type: none"> ▪ A Member State must require that an investment firm from another Member State can have access to a regulated market in its jurisdiction either through a branch or remotely. Member States must require that all members of regulated markets can designate, subject to certain limitations, the system for the settlement of their transactions. ▪ Subject to certain conditions, central counterparties have to clear trades from any trading venue in the EEA on a non-discriminatory basis. Likewise, also subject to certain conditions, trading venues have to provide trade feeds to any central counterparty in the EEA on a non-discriminatory basis. ▪ Subject to certain conditions, any central counterparty or trading venue in the EEA has to be given non-discriminatory access to an EEA benchmark for the purposes of clearing and trading. ▪ Data reporting services providers can provide services across the EEA on the basis of authorisation in a single Member State.
Mortgage Credit Directive (MCD)	For mortgage intermediaries: <ul style="list-style-type: none"> ▪ Establishment of branches or provision of services
Payment Services Directive (PSD) 2	For authorised payment institutions: <ul style="list-style-type: none"> ▪ Establishment of branches or provision of services including the use of agents
Undertaking for Collective Investment Schemes Directive (UCITS V)	For managers of UCITS funds: <ul style="list-style-type: none"> ▪ Management of an authorised UCITS either on a branch or services basis ▪ Provision of certain specified MiFID services either on a branch or services basis For UCITS funds (not included in the data above): <ul style="list-style-type: none"> ▪ Cross border distribution of a UCITS-compliant authorised fund to investors
Electronic Money Directive (EMD)	For authorised e-money issuers: <ul style="list-style-type: none"> ▪ Establishment of branches or provision of services, including the use of agents
Capital Requirements Directive (CRD) IV	For credit institutions: <ul style="list-style-type: none"> ▪ Right to provide banking and investment services ▪ Establishment of branches to provide banking and investment services ▪ In this context banking services include the provision of mortgages and consumer credit (by credit institutions)
Solvency II	For insurance and reinsurers: <ul style="list-style-type: none"> ▪ Establishment of branches or provision of services

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1. Certain financial services or products may be provided on a cross-border basis under the passport system. This means that a firm based in and regulated by the relevant regulator in an EU or EEA country (its Home State) can carry out a relevant service or provide a relevant product into another EU or EEA member state (the Host State) without the need to be separately regulated by the Host State regulator.
2. Passport rights are provided for in the relevant EU Directive that regulates the service or product concerned. EU Directives and Regulations (including implementing regulations) are part of EU law.
3. A regulated firm wishing to utilise a passport must apply to its Home State Regulator. Providing it is satisfied the conditions are satisfied, the Home State regulator will award the passport and notify the regulator(s) in the relevant Host State(s).
4. There are two types of Passport:
 - Service Passport – where there is no permanent establishment (premises and staff) in the Host State; and
 - Branch Passports – where there is a permanent establishment (premises and staff) in the Host State.

FCA — Statement on EU Withdrawal Impact Assessment

Of relevance to
 FCA Regulated Firms

Useful links

[fca.org.uk/publication/impact-assessments/eu-withdrawal-impact-assessment.pdf](https://www.fca.org.uk/publication/impact-assessments/eu-withdrawal-impact-assessment.pdf)

The FCA published its EU Withdrawal Impact Assessment on 29 November 2018. The assessment was requested by the Treasury Select Committee and sets out the impact of the Withdrawal Agreement and future framework on the FCA’s objectives.

The Treasury Select Committee requested the FCA to assess the impact of the UK’s exit from the EU across three areas:

- The UK leaves the EU without an agreement either on the 29 March 2019 or after the transition period on 31 December 2020;
- The draft Withdrawal Agreement; and
- The outline of the political declaration on the framework for the future relationship between the UK and the EU.

<https://www.fca.org.uk/publication/impact-assessments/eu-withdrawal-impact-assessment.pdf>

Additionally, in a letter to the Treasury Select Committee, Andrew Bailey, the FCA Chief Executive, set out five principles for a future regulatory framework. The five principles are:

- Cross border market access: Open markets are an important enabler of healthy competition, supporting FCA objectives;
- Support for the principle of consistent global standards where markets are also global;
- Cooperation between regulatory authorities: A robust framework which provides for continued cooperation will be fundamental in enabling the FCA to meet its own objectives;
- Influence over standards: The FCA should continue to play a part in shaping international standards building on existing relationships with other regulators around the world through multilateral bodies such as IOSCO and the FSB; and
- Opportunity to recruit and maintain a skilled workforce: Being able to recruit and retain the right people from across the world, with the right mix of skills, is important to the health of the FCA, and indeed to the health of the wider UK financial sector.

<https://www.fca.org.uk/publication/correspondence/eu-withdrawal-impact-assessment-letter.pdf>

FCA — Key Findings on Pension Transfer Advice Review

Of relevance to
Pension Advisers

Useful links

[fca.org.uk/publications/multi-firm-reviews/key-findings-our-recent-work-](https://www.fca.org.uk/publications/multi-firm-reviews/key-findings-our-recent-work-pension-transfer-advice)

The FCA has issued the results of its recent work on the standards of pension transfer advice and has concluded that in less than 50% of cases reviewed was the advice given suitable. The levels of unclear (23%) and unsuitable (29%) were up on the previous supervisory exercise undertaken by the FCA and the regulatory has hinted at dire consequences for firms that do not abide by the rules and achieve higher levels of suitable advice.

The target of this latest review was focussed and may not be fully reflective of the overall advisory standards in the industry but it does serve as a warning to firms to ensure that their business models and advice processes are fit for purpose and keep up with regulatory developments.

What should firms be doing?

All firms active in pension transfers should be considering reviewing their business to ensure that the model does not lean towards the provision of unsuitable advice. Governance arrangements should be checked and the advisory process examined to ensure that no systemic issues exist. It may also be necessary to sample review past cases to establish if there is a historical problem and upgrade quality control processes provide assurance that future standards are acceptable. This is particularly pertinent given the forthcoming SM&CR regime where senior management will be directly accountable for the conduct risk standards in the business.

<https://www.fca.org.uk/publications/multi-firm-reviews/key-findings-our-recent-work-pension-transfer-advice>

FCA proposes permanent measures for retail CFDs and binary options

Of relevance to
CFD Firms

Useful links

[fca.org.uk/news/press-releases/fca-proposes-permanent-measures-retail-](https://www.fca.org.uk/news/press-releases/fca-proposes-permanent-measures-retail-cfds-and-binary-options)

The FCA is proposing rules to address harm to retail consumers from the sale of certain complex derivative products with the publication of two consultation papers.

The rules would apply to firms acting in or from the UK and:

- ban the sale, marketing and distribution of binary options to retail consumers
- restrict the sale, marketing and distribution of contracts for difference (CFDs) and similar products to retail customers

The FCA's proposed interventions are the same in substance as the European Securities and Markets Authority's existing, EU-wide temporary restrictions on these products, although the FCA is also proposing to apply its rules to closely substitutable products (including so-called turbo certificates). If confirmed the FCA's rule changes would have permanent effect.

For CFDs sold to retail clients, the FCA is proposing to require firms to:

- limit leverage to between 30:1 and 2:1 by collecting minimum margin as a percentage of the overall exposure that the CFD provides;
- close out a customer's position when their funds fall to 50% of the margin needed to maintain their open positions on their CFD account;
- provide protections that guarantee a client cannot lose more than the total funds in their CFD account;
- stop offering monetary and non-monetary inducements to encourage trading; and
- provide a standardised risk warning, which requires firms to tell potential customers the percentage of their retail client accounts that make losses.

<https://www.fca.org.uk/news/press-releases/fca-proposes-permanent-measures-retail-cfds-and-binary-options>

European Supervisory Authorities propose to amend bilateral margin requirements to assist Brexit preparations for OTC derivative contracts

Of relevance to
All Firms

Useful links

esma.europa.eu/press-news/esma-news/esas-propose-amend-bilateral-margin-requirements-assist-brexit-preparations-otc

The European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority (“ESMA”), together with the European Supervisory Authorities, published a final report with draft Regulatory Technical Standards (“RTS”) on 29 November 2018 proposing to amend the Commission Delegated Regulation on the risk mitigation techniques for OTC derivatives not cleared by a CCP (bilateral margin requirements) under the European Market Infrastructure Regulation.

In the context of the on-going withdrawal negotiations between the EU and the UK, and to address the situation where a UK counterparty may no longer be able to provide certain services across the EU, counterparties in the EU may want to novate their OTC derivative contracts by replacing the UK counterparty with an EU counterparty. However, by doing this, they may trigger the clearing obligation or the bilateral margin requirements for these contracts, therefore facing costs that were not accounted for when the contract was originally entered into.

The draft RTS allows UK counterparties to be replaced with EU ones without triggering the new procedures defined in the bilateral margin RTS. This limited exemption would ensure a level playing field between EU counterparties and the preservation of the regulatory and economic conditions under which the contracts were originally entered into. Its scope, time and intent are aligned with the draft RTS regarding the clearing obligation that ESMA published on 8 November.

<https://www.esma.europa.eu/press-news/esma-news/esas-propose-amend-bilateral-margin-requirements-assist-brexit-preparations-otc>

Retail and Wholesale Banking: FCA Review of Whistleblowing Arrangements

Of relevance to
FCA Regulated Firms

Useful links

[fca.org.uk/publications/multi-firm-reviews/retail-and-wholesale-banking-review-firms-whistleblowing-arrangements](https://www.fca.org.uk/publications/multi-firm-reviews/retail-and-wholesale-banking-review-firms-whistleblowing-arrangements)

The FCA has reviewed how firms have implemented the whistleblowing rules. The FCA has published the findings, including the areas of good practice it observed and areas for improvement, together with its expectations on firms' whistleblowing arrangements.

The FCA has set out what it expects of firms. Firms should:

- have up-to-date written procedures which are readily available to employees, outlining the firm's approach to whistleblowing;
- clearly explain that raising a whistleblowing concern to the FCA or PRA is not conditional on a report first being made using the firm's internal arrangements and that concerns can be raised internally and to the PRA or FCA simultaneously or consecutively;
- have a documented investigation process that explains how they progress whistleblowing cases and provide a clear and consistent approach for those responsible for operating the firm's arrangements to follow. This should include information on how to protect a whistleblower's confidentiality, assess and grade the significance of information provided by whistleblowers and help the whistleblowers' champion when asked to do so;
- document and embed their approach to preventing victimisation across their whistleblowing arrangements. This should ensure that the necessary measures and safeguards are in place to protect whistleblowers from retaliation or being otherwise disadvantaged;
- ensure a whistleblowing report is made annually to its governing body. This report is required to ensure the firm's governing body has ongoing oversight of the operation and effectiveness of its whistleblowing systems and controls. The annual report is required regardless of the number of whistleblowing cases reported and must maintain the confidentiality of individual whistleblowers;
- ensure the whistleblowers' champion has the responsibility for overseeing the production of the annual whistleblowing report and overseeing the integrity, independence and effectiveness of the firm's whistleblowing arrangements. This includes policies and procedures on protecting against victimisation;
- provide appropriate training for UK-based employees, managers of UK-based employees wherever the manager is based, and employees responsible for operating the firms' internal whistleblowing arrangements. This should include the information outlined in SYSC18.3.4G; and
- promptly tell the FCA about contested but lost employment tribunal cases, where the claimant successfully based all or part of their claim on either detriment suffered as a result of making a protected disclosure in breach of section 47B of the Employment Rights Act 1996 or being unfairly dismissed under section 103A of the Employment Rights Act 1996.

<https://www.fca.org.uk/publications/multi-firm-reviews/retail-and-wholesale-banking-review-firms-whistleblowing-arrangements>

Key Dates

Key Date	Topic
21 January 2019	ESMA Technical Advice under the Prospectus Regulation in force, covering the areas of format and content of a prospectus, the EU Growth prospectus and the scrutiny and approval of a prospectus
10 March 2019	Internalised Settlement reporting requirements—ESMA to issue regulatory and implementing technical standards
13 March 2019	Competition and Markets Authority due to complete their investigation into the supply and acquisition of investment consultancy services and fiduciary management services to institutional investors, including pension schemes, charities, insurance companies and endowment funds
11pm on Friday 29 March 2019	Brexit— European Union (Withdrawal) Bill will repeal the European Communities Act 1972 and make other provision in connection with the withdrawal of the UK from the EU
Spring 2019	Financial Guidance and Claims Bill —FCA takes over regulation of Claims Management Services
	Senior Managers & Certification Regime to cover all FSMA authorised firms, replacing the Approved Persons Regime
1 April 2019	FCA requires managers of dual-priced authorised funds to pay box profits to the fund for the benefit of investors or to individual investors who have bought or sold units
6 April 2019	New FCA rules on pension transfer assumptions to use when revaluing benefits
3 July 2020	End of 30-month period during which the US Securities and Exchanged Commission provides market participants with greater certainty regarding their US regulated activities and compliance with MiFID II rules on Investment Research
July 2020	5th Money Laundering Directive to be adopted throughout Europe
October 2020	Pension transfer specialists to obtain the investment advice qualification
31 December 2020	Brexit—end of transitional period

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