



Regulatory Roundup

1 April 2011

Issue 28

In Brief:

Bribery Act Guidance: Clarifies certain aspects of the Act and provides useful examples including what could constitute 'adequate procedures'

Delay To Controlled Functions Changes: FSA still updating ONA but remind firms that the delay is not a change of policy

Auditor's Report: Changes made to improve quality of auditors' reports on client assets

Client Money: FSA Action: Broker fined for client money failings

Suitability: FSA issues finalised guidance

FSA Business Plan 2011/12: Reduction of financial crime will remain a priority

Transaction Reporting: FSA propose amendments to reporting OTC derivatives

Prospectus Directive Changes: HMT consulting on prospectus requirements

FSA Data Items: FSA publishes amended guidance on completion of certain data forms

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If any of the topics discussed above raise questions or a need for guidance or support, please feel free to contact [Peter Carlisle](#).

Bribery Act Guidance

Delay To Controlled Functions Changes



Useful links:

[Reg Roundup 26](#)

[BA2010 Guidance](#)

[BA2010 'Quick Start'](#)

The Ministry of Justice has released its long awaited 'guidance' in respect of the Bribery Act 2010 ('BA2010').

As you will be aware from Regulatory Roundup 26, it will be a **defence** for organisations (as per section 7 of BA2010) where '**adequate procedures**' were in place to prevent bribery. The 'adequate procedures' will stem from this now published guidance (as per section 9 of BA2010).

Despite concerns expressed in some quarters, genuine hospitality (dinner, tickets to sporting events etc.) will not be caught by the Act, but 'facilitation payments' – unlike US foreign bribery law - will not be exempt (although 'legally required administrative fees or fast-track services' will not be regarded as facilitation payments).

The guidance confirms that the Act comes into force on 1 July 2011 (three months after publication of the guidance).

Complyport will work with its retained clients to ensure that suitable, and adequate, procedures are in place in a timely manner.

Useful links:

[Reg Roundup 22](#)

[PS10/15](#)

[Controlled Functions
Amendment Instrument](#)

[FSA Statement](#)

Regulatory Roundup 22 updated firms on proposed changes to the Approved Persons regime set out in PS10/15 ('Effective corporate governance').

Highlights included the **removal** of the **CF28** (Systems and Controls) function to be **replaced** by the reintroduced **CF13** (Finance); **CF14** (Risk); and **CF15** (Internal Audit) functions.

The biggest impact was the introduction of the **CF00** (Parent entity significant influence) function. This would replace the current concept of the **extended CF1/CF2** and bring **LLPs** into such a regime for the first time.

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Delay To Controlled Functions Changes (cont.)



Other functions introduced were: CF2a (Chairman); CF2b (Senior independent director); CF2c (Chairman of risk committee); CF2d (Chairman of audit committee); and CF2e (Chairman of remuneration committee).

Altogether the proposals would introduce **nine new controlled functions** to take effect, subject to certain transitional provisions, on 1 May 2011.

Annex 5 of PS10/15 contained a useful table of actions required by firms whether by way of notification to the FSA or via the FSA approval process. All such notifications and applications were to be submitted **via ONA** (the Online Notifications and Applications System). The FSA is undertaking a considerable programme of work on ONA, which means they have been **unable to make the necessary changes** to process the applications for these new functions.

The effect of this is to **delay** the introduction of these nine new functions and the deletion/amendment of existing controlled functions, although the other aspects of PS10/15 that are not system dependent will be implemented. There is no date set for when the new controlled functions will come into being, although the FSA has committed to **giving at least two months' notice** of the new implementation date.

The FSA advise that the postponement should not be taken as a change of policy and assure firms that 'any work they have already undertaken to identify and assign individuals to the new controlled functions has not been wasted'.

Auditor's Report



Useful links:

[Reg Roundup 21](#)

[Reg Roundup 23](#)

[Reg Roundup 26](#)

[CP10/20](#)

[PS11/5](#)

As you will be aware from Regulatory Roundup 21 the FSA has had **concerns** about the **quality of some auditors' client assets reports** – see FSA Consultation Paper CP10/20 “Improving the auditor's report on client assets”.

The FSA has now published the follow up PS11/5 (“Auditor's client assets report”) containing changes to SUP 3 (‘Auditors’).

As will be known, the need for an auditor to submit a client assets report (SUP 3.10) addressed to the FSA applies **even where firms do not hold client monies or client assets**.

Among the changes proposed is the introduction of a **‘template’** for the auditor's client assets report in SUP 3 Annex 1R and the **introduction of SUP 3.11 for firms**. The latter includes the requirement for a firm to consider the **draft** of the report (SUP 3.10.8D will require an auditor to send a firm a draft of its client assets report so that the firm has ‘an adequate period of time’ to consider the findings) and for the **final** report to be reported to the firm's governing body. The auditor must **deliver** the report to the FSA **within four months** of the end of each period covered, with a copy being sent to the firm at the same time.

The **mandate rules (CASS 8)**, where firms control client assets, will be reintroduced to the scope of the auditor's client assets report - but not if the firm is **not** holding client assets/money. The FSA will keep this under review to see whether this should indeed be applied to the latter type of firm.

The new requirements come into force on **1 June 2011** although auditors and firms have the **option not to apply** the requirements where the report concerns a **period** that ends on or before **29 September 2011** (see SUP TP 1.7(2)).

On the matter of client money and assets, firms are reminded that the requirement to complete a **CMAR** (Client Money and Assets Return) begins in June for large and medium firms. For now, small firms will not have to complete a CMAR but will have to notify the FSA of their highest client money balance and value of client assets in July – see Regulatory Roundup 26 for further details. In addition large and medium firms will need to have appointed a CF10a by 1 October; please refer to Regulatory Roundup 23 for more on this new oversight function.



Client Money: FSA Action Suitability



Useful links:

[ActivTrades Plc Final Notice](#)

Whilst on the subject of client money, ActivTrades Plc, a broker specialising in FX, CFDs and futures, has been fined £85,750 for client money failings.

Firms that hold client money may wish to review the Final Notice in the light of their own processes and procedures. In addition sections of the Notice are relevant for firms that do not hold client money.

Areas highlighted in the Final Notice include failure to demonstrate due diligence, and periodic review, in the selection of institutions where client money is deposited (the Notice refers to them as 'well recognised financial institutions'); co-mingling of client and corporate money; performing monthly rather than daily reconciliations; not being able to provide documentation that supported the reconciliations; and not paying interest on client money balances (this affects retail clients – see CASS 7.2.14R).

Two other areas worthy of note could be applied to activities other than client money: a failure to have specific procedures in place and inadequate management information being supplied to the Board.

Useful links:

[Finalised Guidance on Assessing Suitability](#)

The FSA has issued finalised guidance on 'Assessing suitability'.

The requirements regarding 'Suitability' can be found in COBS 9.2 and apply to a firm which makes a personal recommendations and/or which manages investments. Although the 'Overview' suggests that the guidance will be relevant to firms with retail customers, it is worth bearing in mind that the **suitability requirements also apply to professional clients** in respect of MiFID business (although COBS 9.2.8 permits a firm to assume certain criteria when dealing with a professional client).

The guidance includes selected examples of good and poor practice including comment on the use of standardised allocation models by **discretionary investment managers** (page 21).

Readers may also be interested in the article in this Regulatory Roundup on the FSA Business Plan which reveals the FSA's continued interest in discretionary and advisory investment management services in the light of 'suitability'





Useful links:

[FSA Business Plan 2011/12](#)

[Reg Roundup 15](#)

[Reg Roundup 26](#)

[Reg Roundup 27](#)

The FSA has published its **business plan** setting out its priorities for 2011/12.

Obviously regulatory reform is uppermost in the plan (section 1 contains further details on what is coming up) which is one reason why the FSA is not planning to embark on any new discretionary issues.

Lord Turner's foreword advises that in the **wholesale markets** area there will be **no major shifts in philosophy or approach** following changes in the regulatory structure; the existing system "is not bust, and does not need fixing". **However** there is a reality check in that praise is given to the '**credible deterrence**' approach with greater use of the FSA's civil enforcement and criminal prosecution powers – an approach which will be continued into the FSA's successor bodies – note below the reference to Margaret Cole.

The reduction of **financial crime** remains an FSA priority and we are told in section 5 that the regulator will continue to address financial crime **systems and controls issues** through **enforcement** activity and increasingly intensive, ongoing supervision. The FSA intends to publish 'Financial Crime: A Guide for Firms' this year which will contain examples of good and poor practice to help firms better understand what is expected of them. The last publication of a paper in a similar vein was last year's 'The Small Firms Financial Crime Review' which is still a useful source of reference – Regulatory Roundup 15 contains a link to the latter.

Section 4 warns that the FSA will **extend its review** of the **suitability** of wealth management firms' clients' portfolios, covering both **discretionary and advisory management services**. Note also the article on 'Suitability' in this Regulatory Roundup.

Appendix 3 contains an organisation chart showing the **change in management structure** at the FSA being brought in, w.e.f. April, to reflect the new regulatory architecture that is set to become operational at the beginning of 2013 (see past Regulatory Roundups e.g. issue 27 for further details). A footnote advises that **Margaret Cole**, Director of Enforcement, will assume the interim role of Managing Director of the Conduct Business Unit until Martin Wheatley joins (see Regulatory Roundup 26).



Transaction Reporting Prospectus Directive Changes



Useful links:

[Market Watch 38](#)

[TRUP](#)

[Reg Roundup 11](#)

[Reg Roundup 17](#)

A fairly short edition of Market Watch concentrates on transaction reporting issues.

MiFID investment firms are reminded that they need to have a **BIC** – see Regulatory Roundups 17 & 11 for further details on this. It is proposed that the **option** to identify entities with an FSA Reference Number (**FRN**) **will be removed**. The FSA will consult on this during 2011.

Following a rethink, the FSA will **no longer require** portfolio management firms to transaction report **inter-fund transactions**. The Transaction Reporting User Pack (**TRUP**) will be amended accordingly (see second bullet in s7.4.1 of current TRUP).

The FSA advise that they receive ‘a significant number’ of **OTC derivatives transaction reports** without the underlying ISIN being provided. It is therefore proposed that **an additional validation** will be introduced requiring the ISIN to be provided when instrument types X (other); F (future); or O (option) are selected. The FSA ‘will give the industry enough notice before the change becomes effective’.

Elsewhere the paper covers: the need for firms to regularly review the integrity of their transaction reports; monitoring obligations when reporting is outsourced; and a proposed change to **CDS pricing reporting**.

Useful links:

[Prospectus Regulations 2005 re FSMA](#)

PR 1.2 of the Handbook reminds us of the need to issue a prospectus before transferable securities are offered to the public, subject to the certain exemptions listed.

The requirement derives from FSMA s85 which in turn was driven by the Prospectus Directive (PD). FSMA s86 and Schedule 11A lists various exemptions including where the offer is made to fewer than 100 persons; open-ended collective investment schemes; and where the total consideration of the offer is less than €2.5m.

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Prospectus Directive Changes (cont.)

FSA Data Items



Useful links:

[HMT Consultation](#)

Following changes to the PD, which do not have to be implemented until 1 July 2012, HM Treasury has decided to consult on two elements of the revision with a view to introducing them as soon as possible. It is proposing increasing the 'persons' threshold to 150 and the 'consideration' threshold to €5m. HMT believes that this will benefit companies, both quoted and unquoted, in reducing the costs associated with raising funds – it is estimated that the cost of producing a prospectus can range from 7% to 12% of the funds raised for consideration levels below £10m. Since the PD was implemented in 2005 the LSE believes that 98% of further fund raising by AIM companies has been by way of private placements rather than by way of public offers, which, of course, dilutes the interest of existing shareholders.

The consultation period ends 9 June.

Useful links:

[Regulatory Reporting changes](#)

The FSA has published amended guidance for the completion of certain FSA data forms.

It is all of a fairly minor nature e.g. the guidance to the completion of **FSA002** (Income statement) has been enhanced to avoid double counting when completing data elements 9 (Performance fees) and 10 (Investment management fees). Details can be found via the attached link.



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If any of the topics discussed above raise questions or a need for guidance or support, please feel free to contact [Peter Carlisle](#)

Or for details of any other of Complyport's services, please contact [Philip Chapman](#)

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