COMPLYPORT
COMPLIANCE LEADERSHIP

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FSA Fee Changes

The FSA has published a Consultation Paper ('Regulatory fees and levies: policy proposals for 2010/11' - CP09/26) which includes proposals to change the way that the FSA calculates the fees payable by firms.

It is proposed that fees will consist of two components: a basic minimum fee plus a straight line recovery. The former would be in the region of £1,000 and would cover the basic costs such as the costs of the firm contact centre and the minimal base line monitoring carried out on all firms. The straight line element is based upon fees being in direct proportion to the size of permitted business (under the current regime the fees paid by larger firms tend to taper off as each incremental increase in tariff data is exceeded). Firms that are in more than one-fee block will see an immediate benefit in respect of the basic fee, as the fee will be per firm and not per fee-block. However the straight line component is a little more complicated but Table 5.1 in CP09/26 suggests that the majority of firms will end up paying less or the same.

The FSA will be launching a fees calculator by the end of November (see s5.10) so that firms can calculate what their 2009/10 fees would have been ("Stage 1") had the new proposals already been adopted to allow firms to assess the impact of the proposals.

Corporate finance advisors (fee-block A.14) and 'advisers, arrangers, dealers and brokers' (fee-blocks A.12 & A.13) should be aware that the FSA are considering moving away from a headcount basis to a measure based upon income (see Chapter 8).

Below is a link to the current FSA fees section, where the FSA will eventually be publishing the Stage 1 calculator referred to above, as well as allowing navigation to the 2009/2010 fee calculator.

http://www.fsa.gov.uk/pubs/cp/cp09_26.pdf

http://www.fsa.gov.uk/Pages/Doing/Regulated/Fees/calculator/index.shtml

Getting Closer

This month the FSA published "Close links – feedback on CP07/21" (PS09/17) which contains the new draft rules governing close links reporting. It must qualify as one of the slower feedback Policy Statements given that the original Consultation Paper (CP07/21) was published in December 2007, with

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the consultation period ending on 14 March 2008 (the financial crisis, resource and workloads were given as reasons).

As you will know, under the current regime firms have an obligation to notify changes in close links to the FSA (SUP 11.9) as well as providing an annual close links report (SUP 16.5)

The original intention of CP07/21 included the removal of the annual close links reporting requirement. However it seems that the biggest objection to this proposal came from FSA supervisors ("we previously underestimated the benefits to supervisors the annual report provides"). So, after two years the only changes that the majority of firms will notice is that they will have to comply with SUP 11.9 and SUP 16.5 using a 'Close Links Notification Form' and, in respect of the latter rule, will need to supply a group organisation chart.

The amended rules – which will not come into force until 1 June 2010 – can be reviewed in Appendix 1 of PS09/17. A copy of Close Links Notification Forms, or at least as they stood in 2007, can be found in the appendices of CP07/21.

http://www.fsa.gov.uk/pubs/policy/ps09_17.pdf

http://www.fsa.gov.uk/pubs/cp/cp07_21.pdf

FATF and the UK

The Financial Action Task Force (FATF) has acknowledged the work done by the UK in remedying deficiencies found in 2007. In that year FATF issued a report on the UK's compliance with FATF's 40 Recommendations (and the 9 Special Recommendations). Although hardly a damming report there were a few modest deficiencies found; of most concern to FATF was Recommendation 5 (customer due diligence). The report also included an action plan. The 2009 follow-up report by FATF concluded that the UK has now reached a satisfactory level of compliance with all core and key recommendations. As a reward, FATF has decided that the UK should be removed from the 'follow-up' process and instead need only report on any further improvements in its AML/CTF system on a biennial basis.

http://www.fatf-gafi.org/document/23/0,3343,en_32250379_32236982_44047959_1_1_1_1,00.html

US Regulatory Developments

As you will be aware, AIMA has recently reiterated its support for the proposed registration of hedge fund managers in the US in the interests of financial stability. The move comes as the Private Fund Investment Advisers Registration Act of 2009 won support from the House Financial Services Committee.

In its initial form, the bill, should it have become law, could have had implications for U.K. fund managers responsible for funds that have U.S. investors or that have a business relationship with the U.S. Various subsequent amendments have diluted the potential impact, although some U.K. managers could still be affected. As such, a summary of where matters currently stand may be useful.

Legislation was proposed mid July. At that time, proposed amendments to the Investment Advisers Act

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1940 included removal of an exemption that allowed U.S. investment advisers to not register with the SEC if they had less than 15 clients; removed the 'same State' exemption for investment advisers to a private fund; and introduced to that Act the definition of a 'private fund'. The latter captured entities that previously would not have been categorised as investment companies under the Investment Company Act 1940. The existing $30m assets under management level for mandatory registration with the SEC would remain. However an exemption was put in place for 'foreign private fund advisers' who: have no place of business in the U.S.; have fewer than 15 U.S. clients; assets under management attributable to U.S. clients are less than $25m; and do not hold themselves out as investment advisers in the U.S. A concern at the time was the power being given to the SEC to define 'client' i.e. up to now (based on the Goldstein decision) 'client' was at fund level; the bill would allow the SEC to regard investors in a fund as a 'client'.

By the time it had been approved by the House Financial Services Committee, on a 67 to 1 majority vote, in October, 8 out of 13 proposed amendments had been made to the Bill.

Amendments to note:

The very first amendment was perhaps crucial to the success of the Bill; the Bill had quoted the non-existent Investment Advisers Act of 1934.

The amendment to section 8 confines the definition of 'client' to fund level not investor level.

Section 10 would allow a 1 year transitional period for affected investment advisers from the date of enactment.

Arguably the most important amendment is the introduction of section 7. In this, the requirement to register with the SEC would not apply for advisers with assets under management in the U.S. of less than $150m – the threshold seems to apply per fund managed and not per fund manager. Note that there would be a requirement to maintain records and to provide the SEC with annual or 'other reports'.

To complicate matters, Senator Chris Dodd, Chairman of the Senate Banking Committee, issued a 1,136 page financial regulatory reform bill. Page 291 looks familiar as it cites 'Title IV' as the 'Private Fund Investment Advisors Registration Act 2009'. However differences include (page 301) an exemption from the registration and reporting requirements being given to investment advisers relating to a private equity fund.

The message for now is that it seems likely that 'something' will be passed to become law that will concern private funds/private fund advisers/venture capital fund advisers, but there is still some way to go before the final detail is known.

This link illustrates the Bill with the agreed amendments inserted:

http://www.compliancebuilding.com/2009/10/29/amendments-to-the-private-fund-investment-advisers-registration-act/

If you want to see Senator Dodd's discussion paper then please use the following link:

http://banking.senate.gov/public/_files/AYO09D44_xml.pdf

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Transaction Reporting & Execution

As you'll know from SUP 17.2, provided certain conditions are met then portfolio managers are relieved from the responsibility of transaction reporting and instead rely on third parties e.g. the broker to the transaction report to the FSA.

The Transaction Reporting Users Pack (TRUP) [see Regulatory Roundup of 29 September for details and a link] noted on page 12 that there was the possibility of this exemption ceasing, pending "… the outcome of CESR's consultation on defining 'execution of a transaction'…."

Obviously many firms rely on this exemption and any change here could have a big impact on firms' procedures and systems.

Oddly, the CESR website has been completely silent on this consultation.

Having discussed the matter with the FSA we are pleased to report there is no such consultation in being; we are informed that it was pulled after TRUP went to print.

Cumming and Going

The Regulatory Roundup of 5 November reported on the £8m fine imposed upon UBS (AG) after four employees carried out unauthorised transactions involving customer money 'on at least 39 accounts'.

The FSA has now released details of the ban and fine it imposed on Andrew Cumming, a former client adviser at the firm, for his role in the activities. As will be seen from the Final Notice, he did not make any financial gain from the transactions and nor did he initiate or personally conduct any of the unauthorised transactions. His role was signing documentation in respect of the false loans, having been put 'under significant pressure' by a senior colleague at the firm. The ban effectively means that Mr Cummings is prohibited from performing any controlled function. A combination of the FSA having pity on Mr Cumming's financial circumstances, and the now traditional 30% discount for early admission of guilt/settlement meant that the fine was limited to £30,000 (originally £100,000 was considered).

http://www.fsa.gov.uk/pubs/final/cumming.pdf

Broker abuse

Another FSA fine on an individual, this time for abuse of inside information. Alexei Krilov-Harrison was a broker at Pacific Continental Securities (the latter, as you may be aware, was itself subject to Public Censure in January of this year and only escaped a proposed fine of £2,000,000 because by then it was in liquidation). The issue around the individual involved an AIM listed stock; insider information; and telephone calls to clients - so you can probably guess the rest. The details are in the Final Notice. Again, the maximum fine (originally £40,000) was reduced to £24,000, partly due to the financial circumstances of Mr Alexei-Harrison. Although this individual's motive was for personal gain, the original maximum fine was less than half of that in the Cumming case above.

http://www.fsa.gov.uk/pubs/final/krilovharrison.pdf

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A Reminder

A previous Regulatory Roundup included an article on the new liquidity rules affecting BIPRU firms (BIPRU 12). A reminder that although there are some transitional provisions, the majority of the rules come into force on 1 December 2009. If you have not yet given consideration to the issue then reference to the Regulatory Roundup of 5 November will provide an overview of the essential requirements. Retained clients of Complyport that want to discuss the requirements of BIPRU 12 etc. should get in touch with their usual Complyport contact who can arrange for one of our liquidity team consultants to contact you. We would be happy to discuss with you any additional services we can provide in the reviewing of, or assisting in the preparation of, your documentation. Non retained clients that require assistance with the liquidity rules, or for further information on services that Complyport can provide, please contact Diane Gwilliam.

If any of the topics discussed above raise questions or a need for guidance or support, please feel free to contact Peter Carlisle at peter.carlisle@complyport.co.uk