# 2014 Regulatory Bulletin Issue 10

***"If you could kick the person in the pants responsible for most of your trouble, you wouldn't sit for a month." Theodore Roosevelt***

Firms may need to take on board Teddy's words of wisdom as the FCA have looked to clarify their usage of attestations, by indicating that the relevant senior people at the firm will have to take more responsibility in ensuring the firm is compliant in individual areas of compliance.

There has also been a major reward handed out to a whistle-blower, a conference regarding MiFID II and a consultation paper on the proposed changes to the remuneration data for firms

## FCA clarify the use of Attestations

In a letter to the FCA practitioner panel, Clive Adamson has attempted to clarify how the FCA intends to use attestations as a formal supervisory tool. An attestation is a request from a regulator, such as the FCA, to a named senior individual (or sometimes the board) to personally attest a certain set of facts relating to the firm.

- The regulator's increased use of attestations is driven by its aim of ensuring that senior managers of regulated firms are clearly accountable and focussed on specific issues that the regulator has taken a keen interest in.
- Attestations will be requested from the most relevant senior manager at the firm (usually whoever is responsible for the area of the business that the issue has arisen).
- The FCA does not want attestations to become onerous procedures although it does acknowledge the 'potentially significant impact on individuals and firms flowing from attestations' however firms will have an obligation to co-operate or risk FCA action.
- The FCA will revise its internal guidance, ensure that attestations are subject to a central quality assurance function at the FCA and will publish data on their use on a quarterly basis (all of which is similar to the systems that are in place for the use of skilled person reports).

## $300k paid as an award to whistle-blower by The Securities and Exchange Commission

The employee reported concerns of wrongdoing to appropriate personnel within the company, including a supervisor. But when the company took no action on the information within 120 days, the whistle-blower reported the same information to the SEC. This information led directly to an SEC enforcement action and is the first award for a whistle-blower with an audit or compliance function at a company.

Sean McKessy, Chief of the SEC's Office of the Whistle-blower. *"Individuals who perform internal audit, compliance, and legal functions for companies are on the front lines in the battle against fraud and corruption. They often are privy to the very kinds of specific, timely, and credible information that can prevent an imminent fraud or stop an ongoing one…these individuals may be eligible for an SEC whistleblower award if their companies fail to take appropriate, timely action on information they first reported internally."*

The SEC's whistle-blower program rewards high-quality, original information that results in an SEC enforcement action with sanctions exceeding $1 million. With the awards ranging from 10-30% of the money collected in a case. By law, the SEC will protect the confidentiality and identity of any whistle-blower.

## MiFID II conference:

After two and a bit years the European Union reached agreement on the level 1 text of MiFID II. The legislation provides a wide ranging package of important reforms covering both retail and wholesale investment markets, with new obligations for a range of firms providing investment services. At a recent conference, speakers addressed some of the key issues summarised below.

**New Markets**

MiFID II looks to increase the transparency in two large new markets - bond trading and derivative trading, at both the pre- and post-trade stages of a transaction.

In commodity derivatives, MiFID II brings a whole new regulatory regime, including pre- and post-trade transparency and commodity position reporting requirements, and a system of position limits

Computerised trading, both widely used algorithmic trading and more specialist high-frequency trading (HFT), will be given enhanced scrutiny by European regulators. New rules will tackle a range of concerns about market integrity, protection of ordinary investors and prevention of market abuse

One of the major areas of change derived from MiFID II is Wholesale Conduct:

**Best Execution**

The Commission has created a number of provisions designed to help improve firms' best execution policies, enhance disclosure of order routing behaviour and enable better client scrutiny of execution quality.

**Dealing Commission:**

MiFID II takes steps to remove the incentives on asset managers that could influence their decisions to trade against the interest of their clients, when purchasing research from pots of money generated by that trading.

ESMA's current proposal would mean all valuable research must be paid for by fund managers themselves, rather than by clients transaction fees (i.e. commission sharing).

**Retail investor protection**

MiFID II is designed to enhance retail investor protection. A revised conduct of business rules addressing inducements and suitability requirements; new requirements around product governance and disclosure of costs and charges to investors when purchasing financial instruments and services, and a number of organisational requirements (telephone taping, remuneration of staff and conflicts management).

**Other proposals include:**

- top-down requirements, based around the idea that senior management should take on clear responsibility for investor protection.
- detailed organisational or conduct of business requirements; specifying – or prohibiting – particular responsibilities and practices.
- direct regulatory intervention in the market; notably the product intervention powers given to national authorities and to ESMA.
- Many are focused on changing the experience of consumers directly, such as by giving them more information. This last category reflects a desire to strengthen consumer engagement and competition - particularly in the retail investment market.

*"The mindset of senior managers, system designers and staff at all levels throughout different organisations will need to reflect the new responsibilities being created when it comes to areas like product governance and staff remuneration."*

When implementing these rules it is important to consider the drivers for change behind them in regards to investor protection and ensuring that the consumer outcome is at the forefront of a firm's business model.

## Updates regarding Connect

Connect is the new FCA online notifications and applications system and will replace the majority of applications that are currently submitted on the Online Applications and Notifications (ONA) system.

Dates for your diary:

- It goes live on **1 October**.

From 1 October firms will submit the following applications and notifications to the FCA on Connect:

- Approved Persons
- Appointed Representatives
- Variation of Permissions
- Cancellations
- Standing Data

Passporting applications will remain on ONA. Applications that are submitted on paper, such as Waivers and Change in Control, will remain on paper.

**1 December 2014**

Users will not be able to create new applications on ONA from the 1 October. However, they can submit draft applications created before the 1 October on ONA until the 1 December. From the 1 December draft applications will no longer be available in ONA.

**Moving your account to Connect**

ONA accounts will be transferred to the new Connect system for all users. Once the FCA has moved the account to Connect, the account holder will receive an email asking to set a new password. Once the password has been reset the user will be able to login and start a new application.

For people who have multiple firms to submit on behalf of, they will now be able to see all of these when they start an application. All of the holders associated firms will be migrated along with your account.

## Suspicious transaction reports up by 28%

Since the Market Abuse Directive in 2005 firms seeing suspicious transactions must report these to the regulator so it can review these and other similar transactions for evidence of market abuse.

The number of suspicious transaction reports increased to 1,409 in the year ending on 31 March 2014, the end of the regulator's financial year, from the 1,099 reported over the same period in 2013 a rise of 28%.

## Private Bank sets aside £110m to cover potential compensation

A private bank previously stated that they would be conducting a suitability review, agreed with the FCA, of all their investment advice from 1957 to November 2012. With this review currently in process the private bank have now set aside £110m to cover any compensation costs.

The Bank's chief executive had previously written to all UK clients to warn of possible suitability issues back in June. In the letter he said *"As we approached the RDR it became very clear to me that we needed to put in place a service that looked and felt very different to the process we had before. We wanted to set the standard for what we thought it should look like in the new world."*

## FCA calls for debt management firms to "raise their game."

The FCA have stated that authorisation for consumer credit firms will be far more rigorous under the FCA with the emphasis being on creating a sector that works well for both firms and consumers.

Victoria Raffe, director of authorisations at the FCA, said *"These firms are advising consumers who have often reached rock bottom, so it's important that firms get it right. Many firms are falling well short of our expectations and they will need to raise their game if they want to continue operating."*

The FCA has stated it expects firms to meet required standards, including:

- a business model where customers benefit fully from the service offered, and fees are fair and transparent
- provision of suitable advice that takes into account a client's circumstances
- debt solutions to be appropriate, affordable and sustainable
- advice to be provided by trained staff whose interests are in getting the best outcomes for the customer, rather than driven by incentives
- appropriate systems and controls that will protect client money
- notifying the FCA if they have obtained a book of customers from a firm or a legal entity undertaking debt management

- telling customers about free debt services and signposting them to the Money Advice Service for more information in their first communication with the customer.

**FCA and PRA have published a joint consultation paper on remuneration data collection**

The European Banking Authority (EBA) has issued new final guidelines in relation to data collection for high earners and remuneration benchmarking. The new guidelines amend the existing template and request more detailed information, including additional data on business areas and the breakdown of remuneration.

The PRA and FCA propose to revise their existing rules on the High Earners Report. This will require those listed below to submit data on all their employees that earn a total remuneration of €1m or more in a financial year. This applies for all subsidiaries and branches within a group based in the EEA or an EEA branch of a firm with its head office outside of the EEA.

- Banks and Building societies
- IFPRU investment firms (including IFPRU Limited Licence and IFRPU Limited Activity firms)
- BIPRU firm, exempt CAD firm, a local and any other firm that is not a credit institution or an investment firm which is a consolidation group containing the above.

The Benchmarking Report template has been revised to collect more detailed data, with additional business area data on remuneration broken down into different categories of staff. Plus more information must be disclosed about the form in which total fixed remuneration is delivered.

Currently, this is only covered by a PRA rule, as the scope makes the requirement unlikely to be applicable to FCA regulated firms. However, to ensure consistency and alignment between the PRA Rulebook and the FCA Handbook, the FCA is proposing to introduce the amended rule to mirror the PRA.

**FCA Enforcement Cases**

**Financial adviser banned and fined £300,000**

The advisor misled clients about the likely performance of their investments, by guaranteeing a return or providing inappropriate financial projections of future returns. He continued to reassure investors and advise them to invest, even when he knew (through his controlling interest) his companies were in financial difficulties. He also led clients to believe that the investments were approved or endorsed by the wealth management firm he worked for, which was not the case. He also advised the clients to invest without assessing whether the investments were suitable for their needs, and failed to alert them to the possible risks.

The adviser was deemed to lack honesty and integrity and was therefore fined and banned for performing and function related to regulated activities in the financial services.

Tracey McDermott, director of enforcement and financial crime, said *"People go to advisers because they want expert help on how to make the most of their money. They are entitled to expect that their adviser will act in their best interests, not his own. Advisers should think very carefully and make clear and full disclosure if they are intending to advise clients to invest in ventures in which they have an interest."*

**Former director, of a financial advisory firm banned and fined**

During 2005 UCIS Funds were promoted to thousands of retail investors, without adequate checks being made to ensure the investors were eligible for these promotions. Over 800 consumers invested around £30 million in the three UCIS, which subsequently failed.

Consequently the former director was fined £350,000 and banned from any involvement in FCA authorised firms, after the FCA found that he lacked honesty and integrity. The man knew that his activities created a risk of the UCIS fund being sold to investors for whom the products were not suitable. He recklessly devised a structure that was likely to provide false assurance that a firm's involvement was authorised

Tracey McDermott, director of enforcement and financial crime at the Financial Conduct Authority, said *"[the former director] deliberately flouted regulatory requirements, which were designed to safeguard retail investors, in favour of selling high risk UCIS for potentially lucrative gains. The UCIS have failed and the investors, many of whom should never have been exposed to these high risk investments in the first place, have paid a heavy price for his actions."*

**Insider dealers jailed and ordered to pay £3.2m in confiscation**

Seven defendants have been fined and sentenced to between 3 months and 6 year, following a case into insider dealing, making a combined profit of £732,044.59 on trading between 1 May 2006 and 31 May 2008.

The total amount confiscated exceeds the profits generated as a result of the application of the confiscation regime which allows the court, in appropriate cases, to assume that the profits from other trading that took place within the same period represent the proceeds of crime.

Tracey McDermott, director of Enforcement and Financial Crime said *"The FCA has made it clear that we will use all of the tools at our disposal to ensure that our markets are clean. These individuals engaged in a sophisticated scheme to try and make easy money by exploiting inside information As a result they have not only lost their liberty, their livelihoods and their reputations but they have also now been ordered to pay significant sums in confiscation. This should be a clear message to others that insider dealing does not pay."*

**Irish News**

**CP86: Consultation on Fund Management Company Effectiveness - Delegate Oversight**

The Central Bank has published a consultation (CP86) entitled 'Fund management companies effectiveness - delegate oversight'.

The aim of these measures is to encourage and support the continuous improvement of fund management company effectiveness by providing guidance on good practices, removing overlapping managerial functions, widening the net for potential fund management company directors and tightening the authorisation process.

Once the consultation is complete it is expected new regulatory guidance will be provided in relation to the following areas:

a) Delegation arrangements - New, prescribed requirements for:

   (i) initial and on-going oversight of investment management functions;
   (ii) distribution and marketing activities; and
   (iii) risk management functions.

b) Key management functions - Streamlining current 10/16 key management functions - to be consolidated (for both UCITS management companies and AIFMs) into six key management functions with more detail on what each function must entail.
c) Board composition - Adjustments to Irish resident director/independence requirements;
d) new requirements on board expertise and collective composition.

The Central Bank welcomes comments and views from all interested parties. The closing date for submissions on this Consultation Paper is 12 December 2014.

**Thematic Review of data integrity of regulatory returns by investment firms, fund service providers and stockbrokers**

The Central Bank recently issued a letter to the industry regarding the outcome of a Thematic Review of data integrity of regulatory returns submitted to the Central Bank by investment firms, fund service providers and stockbrokers. The review examined the following areas: the structure of the finance function; the oversight of financial and regulatory returns by the Board of Directors and senior management; and the production and reporting of management information within the firm.

The Central Banks review found that:

- A number of firms had inadequate or no procedures for the production of regulatory returns, or that the procedures did not provide enough detail.
- Relevant staff could not demonstrate a detailed knowledge of the firm's regulatory reporting obligations or the methodologies used to calculate these reports.
- Some firms did not discuss the regulatory reporting process at Board meetings, or that financial reporting did not include the firms' capital position.

The Central Banks made a number of recommendations in relation to the above findings, in addition they advise firms to review their existing procedures to ensure that due care and attention is given to the production, oversight and reporting off all regulatory returns.

**FMConsult News**

FMConsult is currently recruiting highly experienced Compliance executives for roles in its UK and Irish Offices.

All offices provide clients with:

- Compliance monitoring services
- Company authorisation services
- Fund authorisation services
- Outsourced MLRO services
- Outsourced compliance solutions
- Regulatory project assistance (e.g. Investment Restrictions, Money Laundering, Client Money, ICAAPs)

UK and Ireland also provide:

- Investment & Operational Risk management services
- Fund restructuring services
- Internal Capital Adequacy Assessment Process (ICAAP) review and development;
- ACD / Management Company structuring and governance review
- Fund and firm re-domiciliation advice
- AIFMD impact assessment and implementation project
- AIFM Authorisation
- AIFM monitoring

Dublin also provides Fund UCITS IV Reporting, MLRO and Company Secretarial Services.

# 2014 Regulatory Bulletin Issue 10

**Join Our LinkedIn Group**
Ask to join our LinkedIn Group for News and Updates on regulatory compliance and risk, or follow us on twitter **@FMConsultNews**

**FMConsult website**
For more information on the services we provide and detailed profiles of our team, please visit our website

**Opt Out of newsletter**
Please let us know if you do not wish to receive further newsletters.


**FMConsult Contacts:**

**Dallas J. McGillivray**
Group Managing Director
& Authorisation Services
Tel: 020 7220 9073
dmcgillivray@fmconsult.co.uk

**Andrew (Andy) Hicks**
Director, Head of Monitoring Services
Tel: 020 7220 9074
ahicks@fmconsult.co.uk

**Colette Panebianco**
Director FMConsult USA
cpanebianco@fmconsult.us

**Satrajit Roy**
Director FMConsult Arabia
Tel: +97150 9209315
sroy@fmconsult.ae