

ALLEN & OVERY



Key Regulatory Topics: Weekly Update

17 January– 23 January 2020

SEMINARS

You ain't seen nothin' yet: countdown to Brexit (27 February)

Continuing our series of talks on the implications of Brexit for financial services providers, focusing in particular on EU banks, we will discuss the current state of play, including the Withdrawal Agreement, transitional period and the likely outcome of negotiations of the future UK-EU trade agreement, an update on the regulation of EU market participants in the transitional period and beyond, and a discussion of changes to the legislative and regulatory rule sets in light of the revised Brexit Statutory Instruments and 'standstill' directions made by the UK regulators.

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BREXIT

EU (Withdrawal Agreement) Bill 2019-20 receives Royal Assent

On 23 January, the EU (Withdrawal Agreement) Bill 2019-20 received Royal Assent and was enacted as the EU (Withdrawal Agreement) Act 2020. On 22 January, the House of Commons disagreed with all five of the House of Lords' (HoL) amendments and the HoL agreed not to insist. The government can now proceed to ratify the withdrawal agreement as the other statutory preconditions such as a 'meaningful vote' have been repealed so will not apply in relation to ratification. The EP is expected to give its consent to the agreement on 29 January, at which point the Council of the European Union can adopt a decision by qualified majority to authorise the conclusion of the withdrawal agreement.

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CONSUMER/RETAIL

First 2020 update on Citizens Advice 'loyalty penalty' super complaint:

On 21 January, The Competition and Markets Authority (CMA) published its second six-monthly report on the CMA, Ofcom and the FCA's progress in addressing the loyalty penalty issue across five key markets. The cross-sector issue is essentially the practice of charging long-term, loyal and disengaged customers more than newer ones or those who renegotiate. The FCA has an on going consultation regarding a single easy access rate for cash savings accounts. However, the CMA notes that more still needs to be done in all sectors to make sure that loyal and, in some cases vulnerable, customers are not let down. The CMA repeats its call on the government to give it the extra powers promised in 2019 to fine companies that have been found to be breaking consumer protection law. The next update is scheduled to take place in July.

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FCA Dear CEO letter to financial advisors on key areas of concern

On 21 January, the FCA published a Dear CEO letter to financial advisers, setting out the FCA's approach to tackling key areas of concern and the actions firms are expected to take. Financial advisors are a key priority for the FCA, with a notable increase in the number of cases where the actions of firms are resulting in significant harm to consumers. The FCA's areas of focus will be: (i) the suitability of advice and associated disclosure; (ii) defined benefit transfer advice; (iii) pension and investment scams; (iv) the adequacy of firms' financial resources and professional indemnity insurance; (v) the implementation of the ban on mass marketing of speculative mini-bonds; (vi) SM&CR compliance; and (vii) Brexit preparation.

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FCA Statement on Assessing Suitability Review 2

On 21 January, the FCA published a statement which builds upon the commitment in its business plan to review the market for pensions and investment advice for a second time – the Assessing Suitability Review 2. The review will focus on the advice that consumers receive around retirement income and will involve a representative sample, to build a view of the retirement income advice market. The FCA aim to publish a report setting out the results of the review in 2020.

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FCA calls on lenders to adopt modified affordability assessments, assisting mortgage prisoners

On 17 January, the FCA published further data on the mortgage prisoner population. This is following its 2019 Mortgage Market Study, which led the FCA to change its rules to allow lenders to assess affordability based on a borrower's track record of making mortgage payments. The study found that around 140,000 borrowers were unable to switch to a better deal, even though they were up to date with their mortgage payments. Taking into account the remaining mortgage term; the amount of interest currently paid; and commercial lending criteria, the new data suggests approximately 14,000 mortgage prisoners could make a meaningful saving. The FCA believes that increased adoption of the new rules by the major market lenders, which have so far shown little desire to adopt the changes, is essential in enabling mortgage prisoners to pay less interest.

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FINANCIAL CRIME

Please see our section on Payment Services and Payment Systems for the EBA's update to its guidelines on fraud reporting under PSD2.

HMT 5MLD transposition consultation responses

On 23 January, HMT published the responses to their 2019 consultation on the implementation of 5MLD and the transposition into domestic law through the MLRs 2019, summarising the different responses received and setting out the government's approach. One of the key changes, which responses broadly supported, was the extension of the MLRs to letting agents and the art sector, although certain activities such as advertising remain out of scope. Regarding cryptoassets, responses largely agreed with the extension, with open-source software and by extension non-custodian wallet providers remaining outside of scope. The document also covers, among other topics: (i) the various amended CDD requirements and PEP definition; (ii) the trust registration service; (iii) the requirement to report beneficial ownership information discrepancies; and (iv) the proposed national register of bank account ownership.

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New Report calls for Computer Misuse Act reform for cybercrime defence

On 22 January, the Criminal Law Reform Now Network, led by academic lawyers in Birmingham and Cambridge universities, published its new report entitled 'Reforming the Computer Misuse Act (CMA) 1990. The out-dated CMA exposes the UK's economy and critical infrastructure to internal and international cyber-attacks and the report calls for its urgent reform. The report identifies problems across offences, defences, sentencing and prosecutorial guidance which prevent investigators from dealing effectively with online threats, while over-punishing immature defendants. The report details a number of recommendations including: (i) the introduction of a civil financial penalties scheme; (ii) the introduction of offence-specific guidelines; (iii) changes to definitions in the offence and defence provisions; (iv) and the creation of a new offence of corporate failure to prevent offence.

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European Commission to initiate infringement proceedings against member states for failing to transpose MLD5

On 21 January, the EC published the opening remarks of Valdis Dombrovskis, European Commissioner for Financial Stability, Financial Services and Capital Markets Union (CMU), at an Economic and Financial Affairs Council (ECOFIN) press conference. Mr Dombrovskis focused on three main topics, the European Green Deal, digital taxation and Anti-money Laundering. Mr Dombrovskis was concerned that with the 10 January deadline for transposition of 5MLD having passed, a few Member States are yet to have transposed it. As early as February, Mr Dombrovskis proposes to initiate infringement proceedings against the aforementioned Member States, as these rules are vital to ensure the integrity of the EU financial system.

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MLD5: UK Trust Registration Service consultation

On 21 January, the House of Lords published a question posed to HM Treasury regarding timing of MLD5 implementation. The key focus of the answer related to the timing for the technical consultation on the details of the implementation of measures related to trust registration. HM Treasury confirmed that the consultation will launch in early 2020 and will ensure the Trust Registration Service contains a robust and proportionate framework which will be transposed into domestic law during 2020.

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New SFO chapter on 'Evaluating a Compliance Programme'

On 17 January the Serious Fraud Office (SFO) published new guidance in its Operational Handbook entitled 'Evaluating a Compliance Programme'. The guidance states that if the SFO is investigating an organisation, it will need to assess the efficacy of the organisation's compliance programme (which will inform decisions on the case) by considering whether: (i) it is in the public interest; (ii) the organisation has a defence of 'adequate procedures' against the charge of a failure to prevent bribery under section 7 of the Bribery Act; and (iii) the organisation should be invited into deferred prosecution agreements (DPA) negotiations and what conditions it should include. The guidance acknowledges a number of key features of compliance arrangements and what prosecutors factor in their review. Prosecutors must assess the compliance programme in the past, the present and how it could change going forward, with the assessment arranged around the six principles of the adequate procedures defence.

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FINTECH

Please see our section on Financial Crime for the new report calling for reform to the Computer Misuse Act.

FCA and BoE artificial intelligence forum terms of reference

On 23 January, the FCA published the terms of reference for the Financial Services Artificial Intelligence Public-Private Forum (AIPPF), which it is establishing with the BoE to facilitate constructive dialogue with the public and private sectors to better understand the use and impact of artificial intelligence (AI) and machine learning (ML) including potential benefits and constraints to deployment, as well as the associated risks. The AIPPF will seek to identify where principles, guidance, regulation or good practice examples could be useful in supporting safe adoption AI/ML, as well as how on-going industry participation could be most useful. Membership will be as representative as possible of the UK financial sector, with participants being invited following a selection process set out in the document. The forum will be co-chaired by Sir Dave Ramsden, BoE Deputy Governor for Markets & Banking and Christopher Woolard, FCA Executive Director, Strategy and Competition.

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Central bank group to assess potential cases for central bank digital currencies

On 21 January, the BoE announced the launch of a central bank group to assess potential cases for central bank digital currencies (CBDCs), collaborating with The Bank of Canada, the Bank of Japan, the Sveriges Riksbank, the Swiss National Bank, the ECB and the Bank for International Settlements (BIS). The group will assess CBDC use cases; economic, functional and technical design choices, including cross-border interoperability; and the sharing of knowledge on emerging technologies. It will coordinate with relevant international institutions and forums, especially the FSB and Committee on payments and Market Infrastructure (CPMI).

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FUND REGULATION

FCA Dear CEO letter to asset managers on key areas of concern

On 22 January, the FCA published a Dear CEO Letter (dated 20 January) to asset management firms outlining the key risks of harm that they pose to their customers or the markets in which they operate. The FCA state that overall standards of governance, particularly at the level of the regulated entity, generally fall below our expectations. In addition, inadequate investment in technology and operational resilience has led to deficient systems which could cause harm to market integrity or loss of sensitive data. As a result, supervisory priorities will focus on: (i) liquidity management and compliance with recently published policy statements; (ii) governance and compliance with SM&CR; (iii) compliance with the new asset management market study requirements; (iv) product governance and compliance with MiFID II; (v) LIBOR transition and exposure to LIBOR risk (vi) operational resilience, especially cyber-attack and technological risk; and (vii) Brexit preparations.

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FCA Dear CEO letter to alternative investment firms on key areas of concern

On 22 January, the FCA published a Dear CEO letter (dated 20 January) to alternative investment firms outlining the key risks of harm that they pose to their customers or the markets in which they operate. These firms predominately manage alternative investment vehicles or alternatives assets directly, or advise on these types of investments or investment vehicles. The FCA states that overall standards of governance are generally below expected levels and CASS oversight controls are not always robust creating a risk of loss to client money. Supervisory priorities will therefore focus on: (i) investor exposure to inappropriate products or levels of investment risk; (ii) client money and custody asset control frameworks and compliance with the CASS sourcebook; (iii) market abuse controls; (iv) threats to market integrity due to high-risk investment strategies; (v) financial crime mitigation; and (vi) Brexit preparations. Firms may be asked to participate in one or more pieces of related work.

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MARKETS AND MARKETS INFRASTRUCTURE

ESMA publishes responses to joint consultation paper on PRIIPs KID

On 21 January, ESMA published the responses received to the Joint ESAs Consultation Paper concerning amendments to the PRIIPs KID which closed on 13 January. The main aims of the review are to: (i) allow the appropriate application of the PRIIPs KID by UCITS and relevant non-UCITS funds, subject to the potential end of the temporary exemption of such funds from the requirements of the PRIIPs Regulation; and (ii) address the main regulatory issues that have been identified since the implementation of the PRIIPs KID to those products that are currently in scope.

[Read more](#)

ESMA consultation on securitisation repository data completeness and consistency thresholds

On 17 January, ESMA published a consultation paper on draft guidelines on securitisation repository data completeness and consistency thresholds under the Securitisation Regulation ((EU) 2017/2402)). The guidelines explain how securitisation repositories can verify whether a data submission is 'sufficiently representative' of the underlying exposures in a securitisation by using the threshold system. In particular, the guidelines set out: (i) the proposed calibration for data completeness thresholds to be applied by securitisation repositories; (ii) explanations as to how and when ESMA intends to revise these thresholds; and (iii) an example of how the representativeness verification of these thresholds would be applied to a sample exposure report. The deadline for comments is 16 March 2020.

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PAYMENT SERVICES AND PAYMENT SYSTEMS

PSR response to feedback on its role and objectives

On 23 January, Chris Hemsley, managing director of the Payment Systems Regulator (PSR) gave a speech in response to recent stakeholder feedback regarding the regulator's role and how it can improve. Mr Hemsley highlights that the PSR will continue to collaborate with the FCA and BoE, with further clarification on its strategy and how it complements its fellow regulators to be provided via a draft strategy statement later this year. Mr Hemsley discusses the developing 'access to cash' issue, one of its key priorities on how to ensure easy, free access to cash even as its use declines. PSR will focus on developing longer term models, welcoming the industry initiatives launched by LINK and UK Finance. The PSR also intends to publish a policy statement outlining its role in the development and supervision of the New Payments Architecture by

Pay.UK, with a call for input to be published in the coming days. Mr Hemsley also provides clarity as to what the PSR wishes to see in the voluntary Contingent Reimbursement Code, implemented to reimburse victims of authorised push payment scams. On its part to protect consumers, the PSR has introduced the Confirmation of Payee requirements that must be implemented by the end of March.

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EBA updates guidelines on fraud reporting under PSD2

On 22 January, the EBA updated its 2018 guidelines on fraud reporting, under PSD2. The EBA has introduced two new data fields into its reporting templates for transactions where secure customer authentication (SCA) is not applied for reasons other than an exemption to SCA the Regulation. The amendments will apply to the reporting of payment transactions initiated and executed from 1 July 2020.

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Euro Banking Association seeks clarification on e-money definition

On 21 January, the Euro Banking Association published a note looking at the EBA Fraud Guidelines, created to reflect the findings of a number of PSD2-SMART2 workshops. The participants: (i) identified a number of open questions on the reporting requirement for e-money transactions as well as on the underlying concepts and scope; and (ii) were concerned that the e-money definition in the EMD provides only limited guidance on which payment instruments fall within its scope and thus which fraudulent payment transactions should be in the e-money category when reporting. Banks from nine EU countries have endorsed the note, which the Euro Banking Association hopes will be the foster discussion on the topic.

[Press Release](#)

[Published Note](#)

PSR consults a proposal to vary specific direction 10 on confirmation of payee

On 20 January, the Payment Systems Regulator (PSR) published a consultation paper on a proposal to vary Specific Direction 10 (SD10) on confirmation of payee. The purpose of SD10 is to reduce losses due to authorised push payment scams and accidentally misdirected payments. It proposes two changes: (1) to introduce an additional basis for a directed PSP to ask for an exemption from an obligation under the direction where it is not reasonable or proportionate to require the PSP to comply (currently, only exceptional circumstances qualify); and (2) to exempt HSBC UK Bank plc from the obligation for accounts held with it that form part of HSBC Group's Private banking brand. The deadline for comments is 29 January 2020.

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PRUDENTIAL REGULATION

Please see our section on Remuneration for the ECB Supervisory Board Chair's letter on SSM firms' variable remuneration policies.

PRA policy statement on updating Pillar 2 capital framework

On 23 January, the PRA published a policy statement on updating the Pillar 2 capital framework, providing feedback to responses to its earlier consultation paper on the same subject (CP 5/19). The PRA has made some minor changes to its proposal following the responses received as further clarification was sought on setting the PRA buffer using the hurdle rate in stress, buffer interactions and usability of risk weighted assets. The PRA has also added a reference to its policy on managing climate-related financial risks. The PRA does not consider any of the changes to be significant enough to have any material impact on the costs or benefits on firms or mutuals. The changes take immediate effect and the policy will not need to be amended under the EU Withdrawal Act. The appendices listed below were also updated.

[Policy Statement](#)

[Statement of policy \(SoP\): the PRA's methodologies for setting Pillar 2 capital.](#)

[Supervisory statement: \(ICAAP\) and \(SREP\)](#)

[Supervisory statement 6/14: implementing CRD IV: capital buffers](#)

EBA discussion paper on future changes to EU-wide banking sector stress test

On 22 January, the EBA published a discussion paper on future changes to the EU-wide banking sector stress test. Most of the features of the EU-wide stress test have remained unchanged since its establishment. Concerns of the current framework include: (i) a lack of clarity and prioritisation of its objectives; (ii) how results are actually used to implement change; (iii) the application of methodological constraints for some risks; and (iv) its resource-intensive nature. The proposed new framework of the EU-wide stress test is based on two legs: the supervisory leg and the bank leg. The supervisory leg would be a

basis for supervisory decisions, directly linked to the Pillar 2 Guidance setting, and a constrained approach. The bank leg would allow more flexibility and would focus on providing disclosure and fostering market discipline. If the final assessment indicates that changing the current framework would bring very few benefits, or would reduce its current advantages, the EBA will retain the current EU-wide stress test framework. The earliest any framework would be introduced is in the 2022 EU-wide stress test and most likely in a staged approach. The EBA is holding a public hearing on the paper on 21 February 2020. The deadline for comments to the discussion paper is 30 April 2020.

[Discussion Paper](#)
[Public Hearing](#)

ECB recommendation on dividend distribution policies

On 21 January, ECB published a recommendation (dated 17 January) on dividend distribution policies, which relates to credit institutions paying dividends in 2020 for the 2019 financial year. It explains that credit institutions need to continue preparing: (i) for a timely and full application of the CRR and CRD IV; and (ii) for the end of the transitional period provided by the IFRS 9 Regulation to mitigate the potentially significant negative impact on CET1 capital resulting from expected credit loss accounting under IFRS 9. The same method that was set out in ECB recommendation ECB/2019/1 should be applied, due to the importance of a conservative distribution policy in adequate risk management and a sound banking system. It is addressed to: (a) significant supervised entities and significant supervised groups, as defined in the Single Supervisory Mechanism (SSM) Framework Regulation; and (b) NCAs and designated authorities with regard to less significant supervised entities and less significant supervised groups, as defined in the SSM Regulation. Credit institutions that are not able to comply with the recommendation because they consider themselves legally required to pay-out dividends should immediately contact their joint supervisory team.

[Read More](#)

ECB consults on draft guideline on the materiality threshold for credit obligations past due for LSIs

On 20 January, the ECB opened a consultation on a draft guideline to define the absolute and relative components of the materiality thresholds of credit obligations past due for less significant institutions (LSIs) within the single supervisory mechanism (SSM). It establishes a single threshold for all LSIs, both for retail and non-retail exposures irrespective of the method used to calculate capital requirements. It was designed in alignment with the definition given by the ECB for significant institutions (SIs) in Regulation (EU) 2018/1845 in order to ensure consistency, comparability and a level playing field across the SSM. A set of FAQs have been published alongside the consultation. The deadline for comments is 17 February 2020.

[Public Consultation and Draft Guideline](#)
[FAQs](#)

Validation errors in branch return form for international banks

On 17 January, the PRA updated their banks, building societies and investment firms webpage, having identified that the branch return form published on 12 September last year, contains incorrect validations in Part 3. The corrected version of the form has now been published, with a PRA consultation on the changes expected to take place in March.

[Read more](#)

REMUNERATION

ECB Supervisory Board Chair's letter on SSM firms' variable remuneration policies

On 21 January, the ECB published a letter from Andrea Enria, ECB Supervisory Board Chair, on the variable remuneration policies of credit institutions in the single supervisory mechanism (SSM). Firms need to adopt a prudent, forward-looking stance when deciding on a remuneration policy, considering the policy's potentially detrimental impact on their ability to maintain a sound capital base, especially taking into account the transitional requirements set out in CRD IV and the transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds under the CRR. The ECB expects firms to take into account the potential impact on capital demand due to future changes in the EU's legal, regulatory and accounting frameworks.

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OTHER DEVELOPMENTS

FSB 2019 global monitoring report on non-bank financial intermediation report

On 19 January, the FSB published its *2019 global monitoring report on non-bank financial intermediation (NBFI)*, presenting the results of its annual monitoring exercise to assess global trends and risks. It covers data up to the end of 2018 from 29 jurisdictions. Key findings include: (i) total global financial assets grew by 1.4% to \$378.9 trillion, driven largely by banks; (ii) the narrow measure of NBFI grew by 1.7%, significantly slower than the 5 year average (2012-2017) of 8.5%; (iii) lending by other financial intermediaries (OFIs) grew by 3%, largely driven by the Euro area; and (iv) interconnectedness between banks and OFIs through credit and funding relationships has been largely unchanged since 2016. Investment funds and money market funds remain the largest OFI providers of credit to banks.

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