

REGULATORY FOCUS

A synopsis of the Financial Conduct Authority's (FCA) latest news and publications issued in December 2016.

ISSUE 102

FCA issue final MiFID II Consultation Paper (CP16/43)

The Financial Conduct Authority issued its third and final MiFID II consultation paper ([CP16/43](#)) on 16 December 2016. Any further consultations will form part of future Quarterly Consultation Papers (published March, June, September and December each year.)

This paper seeks comments and views on a range of technical matters not previously covered in other CPs, paying particular attention to the proposals in the following sectors:

- Conduct of business rules for specialist regimes
- Tied agents
- SME growth markets
- Market data
- Miscellaneous changes to the handbook

Items of interest are:

1. The impact on Corporate Finance Businesses: clarifying which elements of the conduct of business rules apply to them when they are operating as Optional Exemption Firms.
2. The proposal to reorganise COBS 18.5 to form 3 sections, breaking down the rules for Residual CIS Operators, AIFMs and UCITS ManCo, and to introduce further rules. These will deal with the practical challenges of paying for research through a Research Payment Account and certain pre and post transparency issues. In regard specifically to Authorised Funds (because here the practical difficulties are at their most acute), the FCA proposes a 2-year transitional period before full pre and post transparency provisions must be met.
3. Clarification of MiFID II's obligation on all Member States to permit Tied Agents. For background, MiFID's application on tied agents was optional on Member States. The UK and some other Member States permit Tied Agents, but some did not. In addition, MiFID II introduces some further obligations in connection with MiFID Article 3 Firms and Tied Agents. The types of MiFID Instruments permitted for Tied Agents has also widened.

The CP also highlights the FCA's intention:

1. To open the MiFID II authorisation gateway on 30 January 2017.
2. To make the new authorisation and VoP application documentation available in advance of Monday 30 January 2017.
3. That the new Long Form A will be one multi-purpose form which will have separate sections that apply only to those who are members of a firm's management body, or is in a position of control within the Firm.
4. To issue its first Policy Statement on MiFID II in March 2017 and the second in June 2017.

OUR RECENT AWARDS*

EUROPEAN SERVICES -
BEST CONSULTANCY FIRM 2016
CTA Intelligence

BEST EUROPEAN OVERALL
ADVISORY FIRM 2016
HFMWeek

BEST OVERALL ADVISORY FIRM IN
THE U.S. 2014
HFMWeek

BEST ASIAN ADVISORY FIRM FOR
REGULATION AND COMPLIANCE
2014
HFMWeek

BEST EUROPEAN ADVISORY
FIRM FOR REGULATION AND
COMPLIANCE 2014
HFMWeek

BEST ADVISORY FIRM REGULATION
AND COMPLIANCE 2014
HFMWeek

BEST SEC REGISTRATION TEAM -
HONG KONG 2014
Acquisition International

UCITS FUND ADVISOR OF
THE YEAR - IRELAND 2014
Acquisition International

*Awarded to Kinetic Partners, which was
acquired by Duff & Phelps in January 2015

Enforcement Actions

MiFID II Gap Analysis Tool

As mentioned in previous Regulatory Focus editions, Duff & Phelps has developed an online tool in order to assist firms with their preparation for MiFID II. The tool is available for firms to purchase, which they can use independently or with the assistance of Duff & Phelps in order to assess and track their readiness. For more information with regards to the tool, please contact [Caroline Gibbs](#) or [Katherine Davidge](#).

FCA bans and fines an individual £233,600

1 December 2016

On 22 July 2016, the FCA imposed a financial penalty of £233,600 on an individual and withdrew his permission to undertake the CF1 and CF3 roles within the firm at which he was employed. The FCA also prohibited the individual from 'performing any senior management function and any significant influence function in relation to any regulated activity carried on by an authorised person, exempt person or exempt professional firm'.

The decision was made after reviewing the activities that took place at the Firm between the period of January 2010 to January 2013. During this period, advice was provided to customers who were contemplating transferring or switching their existing pension funds via self-invested personal pensions (SIPPS) into unregulated investments such as biofuels and overseas property.

The individual established the business model that was in place at the Firm during the relevant period, and additionally acted as a director and a shareholder of an Unregulated Introducer. This Unregulated Introducer was responsible for referring the majority of customers to the firm and its role was to 'facilitate the sale of alternative investments to customers'.

During the above mentioned period, 1,661 customers invested £112,420,985 in alternative investments. The FCA believes that the personal recommendations process used to advise customers failed to consider the individual customer circumstances, demands and needs, and was therefore inadequate. In the FCA's opinion, the individual failed to ensure that the Firm provided suitable advice to its clients, and failed to ensure that the conflict of interest was managed fairly and was clearly disclosed to customers.

This scenario created a conflict of interest between the individual and the customers of the Firm. The individual also received an enhanced financial benefit due to his position at the Unregulated Introducer as he was receiving both the fees paid by the customers for the Firm's advice as well as the commission paid to the Unregulated Introducer for the introduction.

The Final Decision Notice was published on 1 December 2016 and the individual has referred the decision to the Upper Tribunal, where he and the FCA will present their cases.

The Financial Compensational Scheme (FSCS) has upheld 919 claims of unsuitable advice against the Firm, with compensation of over £40 million paid as at September 2016.

To review the full article, please click [here](#).

Supervision Matters

Individual sentenced to 12 months imprisonment for insider dealing

21 December 2016

A former portfolio manager has been sentenced to 12 months imprisonment, reduced from 18, for insider dealing on the basis of information obtained by him in the course of his employment. A confiscation order was also made for £149,861.27 and costs awarded to the FCA of £83,225.62.

Commenting on the case the FCA Director of Enforcement highlighted that the individual had gone so far as to use mobile phones to instruct the trades, one of which was unregistered, and the other registered in a false name and address. He also established a company in his wife's maiden name in an overseas jurisdiction. Despite this, his crime was still detectable.

The trial judge remarked that the offences were “pre-meditated and blatantly dishonest” and the Director of Enforcement stated such “insider dealing involved gross abuse of the trust place in him and his senior position.”

FCA proposes stricter rules for CFD products

6 December 2016

The FCA has published [Consultation Paper \(16/40\)](#) which proposes stricter rules for firms selling Contract for Difference (CFD) products to retail customers. The Regulator is concerned that more retail customers are opening and trading these complex financial instruments which they do not adequately understand and are not fully aware of the risks involved.

Based on data collected by the FCA from CFD providers in 2015, it was discovered that over 80% of retail clients who invested in CFDs suffered a loss, with the average being £2,200 per client.

The FCA is therefore proposing measures intended to limit the risks of CFD products and protect consumers which include:

- Introducing standardised risk warnings and mandatory disclosure of profit
- Setting a leverage limit of 25:1 for inexperienced retail clients who do not have 12 months or more experience of active trading in CFDs
- Capping leverage at 50:1 for all retail clients and introducing lower leverage caps across different assets according to their risk
- Preventing providers from using any form of trading or account opening bonuses or benefits to promote CFD products.

The FCA has also raised concerns regarding binary bets, and is in the process of preparing policy measures that would complement existing conduct of business rules once these products are brought into the FCA's regulatory scope.

The FCA's full press release can be found [here](#).

FCA launches consultation on changes to its FSCS rules

14 December 2016

The FCA has invited discussion on the future funding of the Financial Services Compensation Scheme (FSCS) and launched a consultation on proposed changes. The FSCS promotes consumer confidence in financial services by providing compensation to consumers when an authorised firm is unable, or is likely to be unable, to pay claims against it. It is funded by levies paid by firms from across the financial services industry. The rules for the FSCS were last reviewed in March 2013, however since this date the size and impact of FSCS levies have risen considerably for some firms.

The FCA invites responses on the following items:

- Feedback on the Professional Indemnity Insurance (PII) market and the coverage that it provides
- Introducing product provider contributions toward intermediation claims
- Changing the FSCS funding classes for intermediation activities
- Updating limits on consumer coverage in light of the pension freedoms
- Exploring the potential for FSCS levies to better reflect the risks posed by particular practices

The FCA is also consulting on the following specific proposals to:

- Amending payment arrangements so that firms may be asked to pay a proportion of the levy on account
- Introducing FSCS coverage for debt management firms
- Extending coverage in respect of fund management
- Applying FSCS protection to advice and intermediation of structured deposits
- Ensuring FCA rules include Lloyds of London appropriately

The deadline for response is 31 March 2017 before the FCA aims to publish its final rules and a further Consultation Paper in Autumn 2017.

The FCA's press release can be found [here](#) and the consultation paper can be found [here](#).

FCA regulation round up 2016

15 December 2016

In the FCA's December "Regulation Round Up" we believe that areas of particular interest will be references to the FCA's Financial Crime Conference and enhancements made to its online invoicing system, in addition to articles already mentioned in this edition of Regulatory Focus.

As highlighted in our [November Regulatory Focus](#), the FCA's Financial Crime Conference took place on 10th November 2016 and the FCA has now published videos of the speakers' speeches and panel sessions. If you would like to view them, please click [here](#).

The FCA has additionally taken the steps to highlight the Treasury's Office of Financial Sanctions Implementation's (OFSI) [consultation](#) on its proposal to impose cash penalties of up to £1million or 50% of the breach, for financial crime breaches. This is just one part of various measures included in the Policing and Crime Bill currently going through Parliament, and the consultation period ends on 26 January 2017.

Separately, the FCA has chosen to inform firms about its enhancement to its online invoicing system. Firms that previously reported fee tariff data on paper returns can now submit these online for the 2017/18 fee year.

Creating and sustaining cultures of compliance: insights from psychology and beyond

16 December 2016

Peter Lukacs, an economist at the FCA, has compiled an article which looks into the social and psychological influences on individual decision making. It suggests that the culture towards poor behaviour within financial services has changed and continues to do so. This is influenced by the higher fines that have been imposed since the financial crisis in 2008, together with appeals for stronger penalties for offenders. The author notes that penalties can significantly deter wrongdoing, but emphasises that an individual's behaviour is also socially and psychologically influenced and this must also be taken into account.

He draws upon behavioural literature which advocates that an individual's behaviour is influenced or restricted by their desire to see themselves as moral and virtuous. It has been suggested that having people sign a declaration to advise that they will report truthfully can reduce dishonesty. On the other hand, the concept of 'moral licensing' can have a different effect. An example was given of a seller within financial services who discloses a conflict of interest; this individual may then feel released from the need to comply with ethical standards as their conflict has already been disclosed which can lead to them giving biased advice in order to pursue their own agenda.

He explores the idea that culture within a firm can also have a strong influence with regards to the behaviour of individuals. Misconduct can be normalised by what people see and experience within the workplace which can make poor behaviour more likely. This is coupled with the compensation structure within firms that can incentivise staff to behave in a certain way, as observed in the PPI scandal. It is suggested that individuals behave differently in group situations which makes the need to have a culture of compliance ever more important. The pressure of responsibility on the individual is extremely vital and the Senior Managers Regime takes a further step in highlighting the importance of the individual's actions and decision making.

If you would like to review the full article, please click [here](#).

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Compliance Consulting

Ian Manson

Managing Director, Compliance Consulting
ian.manson@duffandphelps.com

Jane Stoakes

Director, Compliance Consulting
jane.stoakes@duffandphelps.com