FIG Bulletin

Recent developments
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Hogan
Lovells

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1. Financial Conduct Authority

1.1 FCA PS17/1 and PRA PS2/17: Implementation of the Enforcement Review and the Green Report

On 1 February 2017, the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) published a policy statement, FCA PS17/1 and PRA PS2/17, which responds to comments they received on their April 2016 consultation paper, FCA CP16/10 and PRA CP14/16, following the publication of HM Treasury's December 2014 review of enforcement decision-making at the financial services regulators, and Andrew Green QC's report into the FSA's enforcement actions following the failure of HBOS (the Green Report) and explains what changes are going to be made to their enforcement policies and processes.

The FCA and PRA received 13 responses to the consultation paper, which were broadly supportive of the proposals, many of which were amendments to existing enforcement process and centred on increasing transparency. Comments were also received making more general points about the enforcement process. The FCA will consider these comments in a further review of the Enforcement Guide (EG). It intends to start this piece of work once it has completed its financial penalty policy review, and has had an opportunity to bed in its partly contested cases process.

The consultation paper and policy recommendations covered the full lifecycle of an investigation. The FCA and PRA have made, or are making, changes to implement recommendations and address relevant responses to the joint FCA and PRA consultation in the following areas:

- how decisions are made on whether to refer an issue to Enforcement and Markets Oversight or the Regulatory Action Division for investigation;
- the provision of more information to the subject of an investigation about why they have been referred for investigation;
- regular updates throughout an investigation, as well as ensuring there is increased engagement with the subject;
- effective levels of dialogue between Enforcement and Supervision during an investigation;
- producing more detailed guidance on the process for joint FCA/PRA investigations.

The FCA is also introducing a process for partly contested cases. This will allow a person under investigation to agree certain elements of a case (whether penalty, facts, liability or a combination of these issues) and contest the other elements before the Regulatory Decisions Committee. They will still have the ability to obtain a discount on the penalty that will reflect the extent that issues have been agreed. In addition, the FCA is providing a mechanism for those under investigation to proceed more directly and quickly to the Upper Tribunal, providing external adjudication that is wholly independent of the FCA. The FCA is also abolishing penalty discounts at stage 2 and 3 of settlement, and retaining the same panel that gave the warning notice to hear representations and decide whether to give a decision notice.

For the PRA, further work is underway or planned for 2017 to ensure that other recommendations are implemented, including follow-up work on the 2016 consultation on an Enforcement Decision-Making Committee, production of a short guide to PRA enforcement procedures, including referral criteria and a review of the PRA's approach to settlement.

The FCA has incorporated the feedback received from the consultation paper into the changes to the FCA Handbook. The final changes to the Decision Procedure and Penalties manual (DEPP) and the EG are set out in the Decision Procedure and Penalties Manual and Enforcement Guide (Review) Instrument 2017, FCA 2017/4, which is also set out in appendix 1

to the consultation paper. The majority of these changes came into effect on 31 January 2017, with the remainder coming into force on 1 March 2017.

1.2 CP17/3: Proposed handbook changes to reflect the new regulatory framework for insurance linked securities

On 31 January 2017, the FCA published a consultation paper, CP17/3, on its proposals for the changes required to the FCA Handbook to incorporate the new regulated activity of insurance risk transformation. This includes changes to the application provisions of parts of the Handbook to incorporate insurance linked securities (ILS), some additional rules the FCA proposes to create, proposals for fees for the registration of protected cell companies (PCC), and a number of consequential changes.

ILS are financial instruments, which are sold to investors, where the value of the security is linked to an insurable loss event. They are an alternative form of risk mitigation for insurance and reinsurance firms, offering a means for them to transfer risk to the capital markets through insurance special purpose vehicles (ISPVs). In November 2016, HM Treasury proposed a new regulated activity of insurance risk transformation, as part of designing a new framework to attract ILS business to the UK.

The proposals will affect ISPVs, firms that undertake activities on behalf of ISPVs, professional advisers to ISPVs, firms considering becoming involved in setting up ISPVs or issuing ILS, and insurers seeking to use ISPVs as part of their risk mitigation strategy.

The proposed changes to the Handbook include:

- **Principles for Businesses**: amending the application of the FCA's Principles for Businesses to include activities directly arising out of the regulated activity of insurance risk transformation, which includes issuing ILS;
- **Financial Services Compensation Scheme (FSCS) disclosure requirements**: to create a rule that ISPVs must disclose to ILS investors the limitations of FSCS coverage in relation to these products;
- **Financial Ombudsman Service (FOS) jurisdiction**: to create a rule in the Dispute Resolution: Complaints sourcebook to bring offering and issuing of ILS within the scope of the FOS compulsory jurisdiction. The FOS proposes to mirror the changes which the FCA is making to the compulsory jurisdiction in its voluntary jurisdiction;
- **Senior Management Arrangements, Systems and Controls sourcebook (SYSC)**: to amend the Handbook so that ISPVs are subject to the requirements of SYSC 3, rather than SYSC 4-10, to bring them in line with reinsurers;
- **new cell notification for PCCs**: that PCCs be required to submit a new cell notification form to the FCA at the same time as they submit it to the Prudential Regulation Authority.

Comments are requested by 14 March 2017. The FCA intends to publish the rules in a policy statement once HM Treasury's regulations have been finalised (the FCA's timetable is dependent on the publication of final regulations by HM Treasury).

1.3 Investment advisory firms practices when acquiring new clients from other firms: FCA supervisory review findings

On 1 February 2017, the FCA published a report giving the findings from its recent supervisory review of investment advisory firms' practices when acquiring clients from other firms.

From an initial nine firms identified as acquiring clients from other firms the FCA carried out a targeted review of six of them. It says that it knows this sample may not be

representative of the wider market, but it wants to share its findings so that firms can consider the key points raised when acquiring new clients.

The FCA reviewed the activities of six advisory firms which had recently acquired clients through the purchase of another legal entity or through acquiring another firm's client bank. With a focus on the points set out in the introduction to the report, it analysed firms' pre-acquisition approach and post-acquisition processes and procedures. It also assessed (for replacement business) if the needs of individual clients were being appropriately considered when recommendations to transfer or switch investments were made.

The FCA says that while it did see some good practices, it was disappointed overall that none of the firms assessed were able to consistently show that clients' needs were suitably considered. The FCA found that, while firms focused on the commercial benefits, they did not focus enough on how clients were impacted by the acquisition. Where firms had clearly considered potential disadvantages to clients and designed their practices to mitigate these, this approach was not consistent across all of the aspects that the FCA assessed. This resulted in a potential detriment for clients whose needs had not been appropriately considered.

Following the review, the FCA provided feedback to the firms assessed, setting out areas for improvement. All firms involved in the review have since taken action to improve their practices. The FCA expects all other relevant firms to now consider the content of the report, and assess whether they need to improve their own practices and procedures.

1.4 MiFID II forms: FCA direction

On 30 January 2017, the FCA published a direction under sections 55U and 60 of the Financial Services and Markets Act 2000 (FSMA). The purpose of the direction is to:

- create the "Long Form A - UK and Overseas Forms (not Incoming EEA) for MiFID authorisation applications";
- amend the Supervision manual (SUP) to add the Long Form A and associated notes for completion;
- specify when the Long Form A and notes are to be used.

The Long Form A has been introduced as a result of relevant MiFID II regulatory technical standards and implementing technical standards, which will require firms to submit information for the approval of individuals who will be members of the management body or effectively direct the business of MiFID firms. Firms should use this form from 30 January 2017, which is when the authorisation gateway opened.

The direction says that HM Treasury has not yet amended the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO) to include the new MiFID II activities. In view of that, authorisation applications from firms applying to undertake activities brought into the scope of regulation by MiFID II, including operating an organised trading facility or carrying out activities in relation to the new proposed investment types of structured deposits, binary bets and emission allowances, will be treated as drafts until the HM Treasury's proposed changes to the RAO have come into force. Applications from firms seeking to obtain permission to carry out any of the existing MIFID activities, or to carry out activities in relation to the existing investment types, will continue to be treated as final and so will any accompanying Form As.

1.5 MiFID II: market data reporting and the market data processor: FCA update

On 30 January 2017, the FCA updated the webpage on its new market data processor

(MDP) system, under MiFiD II to include an MDP application form.

To submit an application:

- the MDP must have already received the market interface specification;
- a new entity applying for authorisation or recognition must submit a relevant MiFID II application in order to receive a case reference number for inclusion in the MDP on-boarding application form.

1.6 Consumer Credit Act 1974 retained provisions: FCA review update

In its January 2017 Regulatory Round-up, among other things, the FCA gives an update on its February 2016 call for input on the planning phase of its review of retained provisions of the Consumer Credit Act 1974.

The FCA says that it is planning to outline the scope for the review, and approximate timelines taking it up to 1 April 2019, in the first half of 2017. It will also publish a summary of the responses to the call for input in the first half of 2017.

2. Bank of England and Prudential Regulation Authority

2.1 PRA PS3/17: The implementation of ring-fencing: reporting and residual matters - responses to CP25/16 and chapter 5 of CP36/16

On 1 February 2017, the Prudential Regulation Authority (PRA) published a policy statement, PS3/17, which provides feedback on responses received to its July 2016 consultation paper, CP25/16 on the implementation of ring-fencing: reporting and residual matters. It also provides feedback on responses received to chapter 5 (on ring-fencing -consequential and reporting amendments) of its October 2016 Occasional Consultation Paper, CP36/16.

The PRA received seven responses to CP25/16. Overall, it does not consider that the responses received necessitate significant changes to its proposals. The PRA has, however, made minor amendments to the proposed rules and supervisory statements consulted on in CP25/16 in light of the feedback received and to add further clarity. Each chapter of the policy statement describes the most important issues raised by respondents and notes the main areas where the PRA has made amendments in the rules and supporting policy documents.

In July 2016, HM Treasury made a number of amendments to the ring-fencing secondary legislation. As a result of these amendments, the PRA identified a need for consequential changes to the PRA's ring-fencing regime, including to the reporting requirements proposed in CP25/16. The PRA consulted on these changes in chapter 5 of CP36/16. The PRA received three responses, which are discussed in chapters 4 and 5 of the policy statement. The PRA has incorporated the amendments proposed in chapter 5 of CP36/16 into the final rules and reporting templates published in the appendices to the policy statement.

The relevant rule changes have been made in the PRA Rulebook: CRR Firms and Non-Authorised Persons: Ring-Fencing Instrument 2017, PRA 2017/3, which comes into force on 1 January 2019.

The PRA has also published the following documents as a consequence of the amendments made by the policy statement:

- an update of Supervisory Statement (SS) 34/15: Guidelines for completing regulatory reports;
- an update of SS8/16: Ring-fenced bodies;
- an update of SS31/15: The internal capital adequacy assessment process and the supervisory review and evaluation process;
- an updated version of SS32/15: Pillar 2 reporting, including instructions for completing data items FSA071 to FSA082. Please note that this updated version takes effect from 1 January 2019 and is available for information only; and
- an updated version of the statement of policy on the PRA's methodologies for setting Pillar 2 capital.

2.2 PRA PS2/17 and FCA PS17/1: Implementation of the Enforcement Review and the Green Report

On 1 February 2017, the PRA and the Financial Conduct Authority (FCA) published a policy statement, FCA PS17/1 and PRA PS2/17, which responds to comments they received on their April 2016 consultation paper, FCA CP16/10 and PRA CP14/16, following the publication of HM Treasury's December 2014 review of enforcement decision-making at the financial services regulators, and Andrew Green QC's report into the FSA's enforcement actions following the failure of HBOS (the Green Report) and explains what changes are going to be made to their enforcement policies and processes.

For full details, see item 1.1 above.

2.3 Leverage ratio: PRA statement and related rule modification direction

On 27 January 2017, the PRA published a statement inviting firms to consent to a variation of the temporary rule modifications granted in August 2016 (see this PRA statement) in relation to the exclusion of certain central bank claims from the total exposure measure for the purposes of the leverage ratio. The PRA has also published the revised rule modification direction.

The purpose of the variation is to align leverage reporting and disclosure requirements with the new definition of the total exposure measure. The modification is available to any firm that was granted the original rule modifications, which includes all firms currently subject to the UK leverage regime.

The PRA strongly encourages all firms subject to the UK leverage ratio framework to consent to the variation of their existing rule modifications. It intends to continue to publish a list of all firms that have consented to the rule modification.

This variation of the original rule modification would apply from 1 April 2017, in order for firms to incorporate these changes into their reporting and public disclosures of their results covering the first quarter of 2017. As a consequence, for leverage ratio reporting and disclosure purposes, the revised definition of total exposure measure would be used for the calculation of the leverage ratio for the full first quarter of 2017 and thereafter.

3. Banking and payment services

3.1 PSD2 implementation: HM Treasury consultation paper and draft regulations

On 2 February 2017, HM Treasury published a consultation paper on the UK Government's proposals for implementation of the revised Payment Services Directive (PSD2). The UK is required to implement PSD2 by 13 January 2018.

Draft regulations showing the Government's proposed approach to implementation, using copy-out wherever possible, have also been published. These draft regulations revoke the existing Payment Services Regulations 2009 (PSRs) and replace them with a new set of Payment Services Regulations. The Government considers that this is likely to make the UK legislation easier to use. Large parts of the new draft regulations reproduce the equivalent parts of the PSRs. The draft also indicates, against individual regulations, the related regulations in the existing PSRs and relevant articles in PSD2. A table showing the correlation between Articles in the PSD and PSD2 can be found in Annex II of PSD2 (see page 117 onwards).

In consequence of the amendments to the provisions in the existing PSRs, provisions in other existing legislation will need to be amended. The draft regulations contain some of the more significant consequential amendments to other legislation (including some of the amendments to the Electronic Money Regulations 2011), the final regulations will include all necessary consequential amendments.

Comments are requested by 16 March 2017. The Government aims to finalise and lay the final implementing legislation in Parliament in early 2017 to provide industry with as much time as possible to adjust to any changes required.

On its PSD2 webpage the Financial Conduct Authority says that it expects to consult on necessary changes to its guidance and Handbook rules early in the second quarter of 2017.

3.2 Retail Banking Market Investigation Order 2017 published by the CMA

In August 2016, the Competition and Markets Authority (CMA) published the final report of its retail banking market investigation and announced a package of reforms to make banks work harder for their customers, and help people take control of their banking using innovative new services.

On 2 February 2017, the CMA published the Retail Banking Market Investigation Order 2017 which formally implements these reforms and sets out the strict timetable for introducing key advances such as open banking, the monthly maximum unarranged overdraft charge, standardised business current account opening procedures, and banks having to publish service quality statistics.

An explanatory note, which provides an explanation of how the Order is expected to operate, has also been published, together with a table containing a list of the remedies within the Order and the timetable for implementation. Key dates in the implementation include the launch of the Open Up Challenge run by Nesta later in February 2017, the first stage of the Open Banking data release in March 2017 and a maximum monthly charge on unarranged overdrafts coming into force in August 2017.

The CMA consulted on the draft Order in November 2016 and it has published a summary of responses to the consultation.

3.3 Prudential reform: House of Commons Treasury Select Committee Chair writes to Chancellor of the Exchequer about European Commission proposals

On 27 January 2017, the House of Commons Treasury Select Committee announced that its

Chairman, Andrew Tyrie, has written to the Chancellor of the Exchequer, Philip Hammond, in response to a letter from Sam Woods, Deputy Governor for Prudential Regulation at the Bank of England and Chief Executive Officer of the Prudential Regulation Authority (PRA), about the European Commission's November 2016 prudential reform proposals.

In his letter, which is dated 19 January 2017, Mr Woods responds to an earlier letter from Mr Tyrie which requested the PRA's view on:

- a proposed requirement for EU intermediate parent undertakings to be established in certain circumstances; and
- the treatment of certain exposures under a proposed EU minimum leverage ratio requirement.

Mr Woods' letter provides a technical view on each, and highlights certain other aspects of the proposals.

Mr Tyrie's letter to the Chancellor of the Exchequer says that he would be grateful to know if it is the Government's intention to resist the implementation of the Commission's proposals. He also asks whether HM Treasury agrees with the PRA's assessment of the Commission's proposals, particularly with respect to intermediate holding companies and the leverage ratio.

3.4 Conditions for establishment in the provision of banking services: OECD report

On 27 January 2017, the Organisation for Economic Co-operation and Development (OECD) published a report on the conditions for establishment of subsidiaries and branches in the provision of banking services by non-resident institutions.

The report says that a range of measures having implications for non-resident banking or credit institutions were introduced or in force in the aftermath of the financial crisis. They include changes in the authorisation process or in the scope of permitted activities, as well as financial requirements, governance and risk management requirements, operational requirements, and ownership and control requirements. A larger number of jurisdictions have adopted measures that affect branches of non-resident banking institutions as compared with subsidiaries of non-resident banking institutions, but the margin of difference is not large in absolute terms as far as individual reform categories are concerned. The report has sought to assess these developments and the broad consistency of country requirements with the OECD Codes of Liberalisation

4. Brexit

4.1 The UK's exit from and new partnership with the EU: Department for Exiting the European Union White Paper

On 2 February 2017, the Department for Exiting the European Union published a White Paper on the UK's exit from and new partnership with the EU. The paper is divided into twelve chapters, reflecting the twelve priorities for the negotiations which were set out by the Prime Minister in a speech on 17 January 2017.

Paragraphs 8.22 to 8.26 on pages 42 and 43 in chapter 8 of the document (which is entitled "Ensuring free trade with European markets") relate to financial services.

In the White Paper, among other things, the Government says that:

- it is aiming for the highest possible trade in financial services between the UK and EU Member States;
- in highly integrated sectors such as financial services there will be a legitimate interest in mutual cooperation arrangements that recognise the interconnectedness of markets. The Government will seek to establish strong co-operative oversight arrangements with the EU and will continue to support and implement international standards to continue to safely serve the UK, European and global economy;
- as part of the exit negotiations it will discuss with the EU and Member States the UK's future status and arrangements with regard to EU agencies, including the European Supervisory Authorities (ESAs) (that is, the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority);
- it wants to have reached an agreement about the UK's future partnership by the time the two year Article 50 process has concluded. From that point onwards, it believes a phased process of implementation, in which the UK, the EU institutions and Member States prepare for the new arrangements that will exist between them, will be in everyone's mutual interest. This will give businesses enough time to plan and prepare for those new arrangements. This might be about, among other things, the future legal and regulatory framework for business. However, the Government is clear that no deal for the UK is better than a bad deal for the UK. In any eventuality it will ensure that the UK's economic and other functions can continue, including by passing legislation as necessary to mitigate the effects of failing to reach a deal.

4.2 Impact of Brexit for the EU banking industry: AFME report

On 2 February 2017, the Association for Financial Markets in Europe (AFME) published a report it commissioned from PwC which outlines the operational impacts and transformation challenges that Brexit poses to the provision of banking services in the EU.

PwC gathered information from previous case studies and from 15 banks spanning a range of sizes, activities, origins and legal entity structures. They include EU27 headquartered, UK headquartered and non-EU headquartered banks in broadly even measure.

The report concludes that:

- Brexit presents clear challenges to the EU banking industry and the uninterrupted supply of banking services around the EU;
- Brexit is likely to result in a significant transformation activity as banks, clients, market infrastructure and regulators simultaneously carry out their plans to prepare for the UK’s departure from the EU;
- while banks are planning to take steps during the two year withdrawal period to minimise the impact of a "hard Brexit" on the provision of client services and disruption to the market, these are interim

mitigating measures and will not fully replicate the current ability of banks to service clients based on current access across the single market. During this period banks will need to work closely with regulators to agree a pragmatic approach to facilitate the required structural transformation within a compressed timetable;

- once the terms of the permanent relationship between the UK and EU are known, banks will need further time to put in place strategic solutions to comprehensively service clients in the long term and to facilitate an orderly transition;
- given the complexity and scale of the changes required, a transition period of three years would be needed to give banks (as well as other industry participants) time to transition to the new permanent arrangement.

4.3 New BBA quick briefs

On 31 January 2017, the British Bankers' Association (BBA) published two Brexit "quick briefs", part of a series of short papers intended to inform readers about key commercial, regulatory and political considerations around Brexit.

The latest quick briefs are:

- Data protection and transfer (Brexit Quick Brief 5);
- Time to adapt - the need for transitional arrangements? (Brexit Quick Brief 6).

5. European Union

5.1 TARGET2-Securities harmonisation: ECB seventh progress report

On 31 January 2017, the TARGET2-Securities (T2S) advisory group of the European Central Bank (ECB) published its seventh progress report on T2S harmonisation.

The report focuses mainly on the implementation results for the T2S harmonisation activities between the third and fourth T2S migration waves, covering the period between September 2016 and the end of January 2017, with particular focus on how T2S markets comply, or plan to comply, with all relevant T2S harmonisation standards by the time they migrate to T2S.

5.2 CRD IV: EBA reminds competent authorities of key deadlines and the ITS to be used for running the 2017 supervisory benchmarking exercise of internal approaches

On 30 January 2017, the European Banking Authority (EBA) reminded competent authorities of the key deadlines and the implementing technical standards (ITS) to be used for running the 2017 supervisory benchmarking exercise of internal approaches.

Despite the pending approval by the Commission of the amended ITS on benchmarking, the EBA says that compliance with the proposed deadlines will ensure a smooth and timely start of the 2017 benchmarking exercise.

All EU institutions using internal approaches to calculate capital requirements will be subject to an assessment of their internal approaches and are, therefore, required to submit to their competent authorities the data on those portfolios according to the following deadlines:

- market risk measures remittance date: banks must submit risk measures data (VaR/sVaR/IRC /APR/P&L time series) to competent authorities by 11 April 2017. VaR, s-VaR, IRC and APR must be computed as from 6 February 2017 to 17 February 2017. Banks using historical simulation must compute the daily P&L yearly series from 15 February 2016 to 17 February 2017;
- credit risk: banks must submit low default portfolio figures to competent authorities by 11 April 2017 (the low default portfolios data remittance date). Banks must provide figures as of 31 December 2016.

5.3 CRD IV: EBA 2015 report on high earners in EU banks

On 2 February 2017, the European Banking Authority (EBA) published its 2015 report on high earners (that is, earning those more than EUR 1 million in a financial year) in EU banks, which it is required to publish under Article 75(3) of the CRD IV Directive.

The EBA has analysed the data provided to it for the year 2015, and compared it to the 2014 data. The main results of this analysis are as follows:

- the number of high earners who have been awarded EUR 1 million or more in annual remuneration for 2015 increased significantly, from 3,865 in 2014 to 5,142 in 2015 (an increase of 33.04%). This was mainly driven by changes in the exchange rate between EUR and GBP, which led to an increased staff income paid in GBP when expressed in EUR;
- the population of high earners that are staff identified as having a material impact on the institution's risk profile was almost the same as in 2014. Around 86% of high earners were identified staff in 2015 as against 87% in 2014. This confirms that the percentage increased significantly after the regulatory technical standards on identified staff entered into force in 2014 (the figure in 2013 was 59%).

5.4 Insurance Distribution Directive: EIOPA technical advice

On 1 February 2017, the European Insurance and Occupational Pensions Authority (EIOPA) published its technical advice to the European Commission on possible delegated acts concerning the Insurance Distribution Directive (IDD), together with a covering letter.

EIOPA considers it of the utmost importance that the interests of consumers are taken into account throughout the product lifecycle, that third party payments, such as commission, do not have a detrimental impact on the quality of services provided to customers, and that products sold are suitable and appropriate for the individual customer. It recommends concrete policy proposals relating to the following four areas:

- **product oversight and governance (POG)**: in line with the proportionality principle, EIOPA says that manufacturers of all types of insurance products should establish processes to ensure that all phases of the production cycle are undertaken with the consumers' needs in mind. Based on its POG preparatory guidelines, EIOPA further clarifies the criteria for insurance intermediaries acting as manufacturers, and the level of granularity expected from manufacturers in defining the target market;
- **conflicts of interest**: EIOPA defines potential situations in which conflicts of interest may arise between distributors and their customers in the course of the distribution of distributing insurance-based investment products (IBIPs), requiring distributors to take appropriate measures to prevent, manage and, as a measure of last resort, to disclose conflicts of interest to avoid any harm to customers;
- **inducements**: EIOPA specifies the criteria to assess whether inducements have a detrimental impact on the quality of services to customers. The purpose of these criteria is to provide guidance to market participants on when detrimental impact might occur. The proposed criteria do not amount to a prohibition on the receipt or payment of inducements. EIOPA also clarifies that detrimental impact has to be assessed by taking into account all factors which may increase or decrease the risk of customer detriment;
- **suitability or appropriateness of IBIPs**: EIOPA says that insurance intermediaries or undertakings should gather the appropriate information from their customers for the conduct of appropriateness or suitability assessments of IBIPs. Only where it is non-complex is it possible for an IBIP to be sold without such assessments being carried out. EIOPA specifies the criteria to identify non-complex IBIPs.

EIOPA consulted on the technical advice in July 2016 and has also published a final report on the consultation.

In the covering letter EIOPA says that it will be shortly be launching a consultation on draft guidelines under Article 30(7) and (8) of the IDD on IBIPs that incorporate a structure which makes it difficult for the customer to understand the risks involved, to ensure the final guidelines are issued by 23 August 2017. This consultation paper was published on 2 February 2017, see item 5.5 below. Given the close relationship between the guidelines and the technical advice on "other non-complex products", EIOPA says that it may be helpful to further consider its technical advice on this issue at a later date in the light of feedback to the consultation on the draft guidelines. EIOPA suggests that one option for the Commission would be to issue a separate delegated act relating only to Article 30(3)(a)(ii) of the IDD, taking into account that it may have a more limited impact on national implementation as it is linked to a Member State derogation.

EIOPA will monitor the issues raised in its technical advice and assess, on the basis of

sound evidence following implementation of the IDD level 1 and level 2 measures in February 2018, the need to issue guidance to further specify particular issues raised in the advice.

5.5 Insurance Distribution Directive: EIOPA consults on complex insurance-based investment products

On 2 February 2017, the European Insurance and Occupational Pensions Authority (EIOPA) published a consultation paper on guidelines on complex insurance-based investment products (IBIPs) that incorporate a structure which makes it difficult for the customer to understand the risks involved.

These guidelines are developed in line with Articles 30(7) and (8) of the Insurance Distribution Directive (IDD). The IDD requires that normally an assessment of the suitability or appropriateness of an IBIP for the customer should be carried out by the insurance intermediary or undertaking as part of the sales process. However, where various conditions are satisfied, including that the IBIP is not complex, the IBIP may be sold without a suitability or appropriateness test, that is, on an execution-only basis.

The guidelines cover the assessment of all types of IBIPs. They include criteria to identify product features, which may be difficult for the customer to understand. They address, for example, the nature of the charges paid by the customer and ability for the customer to surrender the product before maturity. IBIPs which include such features will be deemed complex and therefore not eligible for sale via execution-only.

In view of the minimum harmonisation aim of the IDD as well as the fact that for execution-only sales specifically customers do not benefit from the protection of some of the relevant conduct of business rules, national competent authorities may maintain or introduce more stringent national provisions in this area in order to protect consumers.

These guidelines are addressed to national competent authorities. EIOPA says that although specific provisions describe obligations to be met by insurance undertakings and intermediaries, they are not to be read as imposing any direct requirements upon those financial institutions.

Competent authorities within a Member State that has not chosen to exercise the derogation in the first sub paragraph of Article 30(3) of the IDD should regard the guidelines as not applicable.

Comments are requested by 28 April 2017.

5.6 Effective dialogue between insurance supervisors and audit firms: official translations of EIOPA guidelines

On 2 February 2017, the European Insurance and Occupational Pensions Authority (EIOPA) announced the publication of its guidelines on facilitating an effective dialogue between insurance supervisors and statutory auditors into all official languages of the EU.

Competent authorities must confirm to EIOPA whether they comply or intend to comply with the guidelines, with reasons for non-compliance, within two months of the publication of the translated versions. In the absence of a response by this deadline, competent authorities will be considered non-compliant and reported as such.

The guidelines will become applicable by 31 May 2017.

5.7 EMIR: ESMA consults on future guidelines for portability between trade repositories

On 31 January 2017, the European Securities and Markets Authority (ESMA) published a consultation paper on future guidelines on the transfer of data between trade repositories

(TRs) authorised in the EU under the Regulation on over-the-counter derivatives, central counterparties and trade repositories (known as EMIR).

The need to transfer data to another TR may arise for different reasons. The guidelines on which ESMA is consulting therefore address separately the situations where the transfer is due to a withdrawal of registration of the TR from the cases in which the transfer is done on a voluntary basis and under normal market conditions. The incentives and motivations for the relevant parties in each of the two cases would be different and therefore there is a need for a specific approach in each particular situation.

The proposed guidelines establish high-level principles that would need to be followed by the TR participants, reporting entities, counterparties and central counterparties, on the one hand, and the TRs on the other hand.

In this context, the purpose of the proposed guidelines is to:

- ensure that the competitive multiple-TR environment is guaranteed, and that TR participants can benefit from competing offers;
- ensure the quality of data available to authorities, including the aggregations carried out by TRs, even when the TR participant changes the TR to which it reports and irrespective of the reason for such a change; and
- ensure that there is a consistent and harmonised way to transfer records from one TR to another TR and support the continuity of reporting and reconciliation in all cases including the withdrawal of registration of a TR.

Comments are requested by 31 March 2017. ESMA expects to publish a final report on the guidelines by end of quarter 2/beginning of quarter 3 of 2017.

5.8 EMIR and CRA Regulation: ESMA letter to the European Commission on the EMIR review and sanctioning powers

On 30 January 2017, the European Securities and Markets Authority (ESMA) published the text of a letter it has written to the European Commission to ask it to consider a number of issues relating to its supervisory and sanctioning powers under the Regulation on over-the-counter derivatives, central counterparties and trade repositories (known as EMIR) in the context of the ongoing review, and also similar issues related to credit rating agencies (CRAs) under the CRA Regulation.

The letter follows up on the Commission's recent report on the EMIR review, for which ESMA had submitted four reports in August 2015, and also ESMA's technical advice on the functioning of the CRA market which it submitted to the Commission in October 2015.

5.9 EMIR: ESMA announces details of 2017 stress test for CCPs

On 1 February 2017, the European Securities and Markets Authority (ESMA) published the methodological framework for its 2017 pan-EU stress test exercise on central counterparties (CCPs). The exercise covers 17 EU CCPs including all products currently cleared by these CCPs and will assess the resilience and safety of the EU's CCPs from a systemic risk viewpoint. ESMA is required to carry out the stress test under Article 21(6) of the Regulation on over-the-counter derivatives, central counterparties and trade repositories (known as EMIR)

The results of the exercise will provide supervisors, CCPs and other market participants with useful information on the resilience of the EU's CCPs to different market shocks. The exercise will also help identify any potential shortcomings in the CCPs' resilience, and if required ESMA will issue recommendations for further action.

The stress test will complement the stress tests CCPs already run on a daily basis. As CCPs' stress tests focus on their own environment, such as their participants, cleared products and business activity, the ESMA stress test will look at the entire system of EU CCPs by considering possible spill-over effects resulting from CCPs' interconnectedness. CCPs' resilience will be assessed against a combination of multiple participant defaults and simultaneous market price shocks.

The process for running the 2017 EU-wide CCP stress test involves close cooperation between ESMA, national competent authorities (NCAs), the 17 CCPs and the European Systemic Risk Board, which has provided the common market stress scenarios.

ESMA has launched the data request and has provided detailed instructions on how CCPs are expected to calculate and report the data. In March 2017, CCPs will have to provide the data for the stress test, which will then be validated by NCAs and ESMA in the second quarter of 2017. ESMA will finalise the data analysis by the third quarter of 2017 with the results of the exercise being published in the fourth quarter of 2017.

5.10 EMIR: ESMA updates Q&As on implementation

On 2 February 2017, the European Securities and Markets Authority (ESMA) published an updated version of its questions and answers (Q&As) on implementation of the Regulation on over-the-counter derivatives, central counterparties and trade repositories (known as EMIR).

The updated Q&As include a new Q&A (see question 44 in the section on trade repository (TR) questions) in relation to transition to the revised technical standards on reporting, which will become applicable on 1 November 2017. The Q&A clarifies that the reporting entities are not obliged to update all the outstanding trades upon the application date of the revised technical standards and that they are required to submit the reports related to the old outstanding trades only when a reportable event takes place (for example, when the trade is modified). Furthermore, the Q&A explains how those reports will be validated by TRs.

The table of questions on pages 7 to 9 of the document indicates when questions were last updated. The date each question was last amended is also included after each question for ease of reference and new items are highlighted in red.

The purpose of the Q&As document is to promote common supervisory approaches and practices in the application of EMIR. The content of the document is aimed at competent authorities under EMIR to ensure that in their supervisory activities their actions are converging along the lines of the responses adopted by ESMA.

5.11 MAR: ESMA updates Q&As

On 27 January 2017, the European Securities and Markets Authority (ESMA) published an updated version of its document containing questions and answers (Q&As) in relation to the implementation of the Market Abuse Regulation (MAR) to include new Q&As on:

- the notification managers' transactions (see section 2, question 6); and
- how to handle investment recommendations (see section 3, questions 9, 10 and 11).

The content of the document is aimed at competent authorities to ensure that in their supervisory activities and their actions are converging along the lines of the responses adopted by ESMA and at helping issuers, investors and other market participants by providing clarity on the content of the market abuse rules, rather than creating an extra layer of requirements.

The document may be updated where relevant as and when new questions or issues arise. The date on which each question was last amended is included after each question for ease of

reference and new questions are marked in red. ESMA will review the questions and answers in the document to identify if, in a certain area, there is a need to convert some of the material into ESMA guidelines and recommendations.

5.12 MiFID II: ESMA updates Q&As on market structures topics

On 31 January 2017, the European Securities and Markets Authority (ESMA) published an updated version of its document containing questions and answers (Q&As) regarding implementation issues relating to market structures topics under the MiFID II Directive and the Markets in Financial Instruments Regulation (together known as MiFID II).

ESMA has added three new questions The questions clarify:

- when a multilateral trading facility (MTF) operator can also be a member of its own MTF;
- that trading venues locating electronic systems on a third party data centre must comply with the co-location provisions; and
- how the reference to market makers should be understood under Article 2(1)(d) of MiFID II, which provides an exemption, under very specific conditions, from the obligation to be authorised as an investment firm.

The purpose of the Q&A document is to promote common supervisory approaches and practices in the application of MiFID II. ESMA will continue to develop the Q&As in the coming months, both by adding questions and answers to the topics already covered and introducing new sections not yet addressed. The date on which each section was last amended is included for ease of reference.

5.13 MiFID II: ESMA updates Q&As on transparency topics

On 31 January 2017, the European Securities and Markets Authority (ESMA) published an updated version of its document containing questions and answers (Q&As) regarding implementation issues relating to transparency topics under the MiFID II Directive and the Markets in Financial Instruments Regulation (together known as MiFID II).

MiFID II extends the systematic internaliser (SI) regime to other equity-like instruments, in addition to shares, and to non-equity instruments. It also introduces the requirement for investment firms to perform a quantitative calculation to assess whether they are of a size which requires them to be an SI.

The Q&As include four new questions and answers which clarify issues on the new SI regime, including;

- the level at which the firm must perform the calculation where it is part of a group or operates EU branches;
- which transactions should be exempted from, and included in, the calculation;
- at which level of asset class the calculation should be performed for derivatives, bonds and structured finance products; and
- how SIs in non-equity instruments can comply with some of their quoting obligations.

The purpose of the Q&A document is to promote common supervisory approaches and practices in the application of MiFID II. ESMA will continue to develop the Q&As in the coming months, both by adding questions and answers to the topics already covered and introducing new sections not yet addressed. The date on which each section was last amended is included for ease of reference.

5.14 MiFIR: ESMA updates Q&As on data reporting

On 2 February 2017, the European Securities and Markets Authority (ESMA) published an updated version of its document containing questions and answers (Q&As) regarding the implementation of regulatory data reporting

topics under the Markets in Financial Instruments Regulation (MIFIR).

The document provides responses to questions posed by the general public and market participants in relation to the practical application MiFIR on:

- date and time of the request of admission and admission (see section 3 Q&As 4 and 5);
- instrument identification code and Underlying instrument code (see new section 4);
- maturity date (see new section 5);
- classification of financial instruments and financial instrument short name (see new section 6);
- request for admission to trading by issuer (see new section 7); and
- base point spread of the index/benchmark of a floating rate bond (see new section 8);

The document is intended to be continually edited and updated as and when new questions are received. The date on which each section was last amended is included for ease of reference.

5.15 Alternative performance measures: new ESMA Q&As document

On 27 January 2017, the European Securities and Markets Authority (ESMA) published a new questions and answers (Q&As) document containing questions on the implementation of its guidelines on the alternative performance measures for listed issuers.

An alternative performance measure is a financial measure of historical or future financial performance, financial position, or cash flows, other than a financial measure defined or specified in the applicable financial reporting framework. The guidelines apply to alternative performance measures disclosed by issuers or persons responsible for drawing up a prospectus (see ESMA's one page summary).

The purpose of the document is to promote common supervisory approaches and practices in the implementation of these guidelines. It is intended to be continually edited and updated as and when new questions are received. The date each question was last amended is included after each question for ease of reference. Where questions relate to the interaction of the guidelines with the prospectus regime, these are also included in ESMA's Q&As on prospectuses.

ESMA welcomes feedback from market participants on these or other questions with a view to updating the document, where necessary.

5.16 UCITS share classes: ESMA opinion

On 30 January 2017, the European Securities and Markets Authority (ESMA) published an opinion on the extent to which different types of units or shares (share classes) of the same UCITS fund can differ from one another, having found diverging approaches in different EU countries.

UCITS can be sold to retail investors throughout the EU. However, there is currently no common EU framework for share classes, with some countries prohibiting the set-up of different share classes within a single fund and others permitting it with varying degrees of flexibility. While all investors in a UCITS fund invest in a common pool of assets, share classes attribute different rights or features to sub-sets of investors although there is no legal segregation of assets between the share classes.

In the opinion, which is addressed to national regulators, ESMA sets out four high-level principles which UCITS must follow when setting up different share classes in order to ensure a harmonised approach across the EU:

- **common investment objective**: share classes of the same fund should have a common investment objective reflected by a common pool of assets. ESMA considers that hedging arrangements at share class level, with the exception of currency risk hedging, are not compatible with the

requirement for a fund to have a common investment objective;

- **non-contagion**: UCITS management companies should implement appropriate procedures to minimise the risk that features specific to one share class could have a potentially adverse impact on other share classes of the same fund;
- **pre-determination**: all features of the share class should be pre-determined before the fund is set up; and
- **transparency**: differences between share classes of the same fund should be disclosed to investors when they have a choice between two or more classes.

ESMA says that it is aware that these principles will have an impact on investment fund markets in countries where share classes can currently be set up which do not comply with them. Therefore, to mitigate the impact on investors in share classes established prior to this opinion which do not comply with these principles, ESMA is of the view that they should be allowed to continue. However, such share classes should be closed for investment by new investors within six months of publication of the opinion, and for additional investment by existing investors within 18 months of publication.

6. Financial regulation

6.1 Bank of England and Financial Services (Consequential Amendments) Regulations 2017

The above Regulations, SI 2017/80, were made on 31 January 2017 and come into force on 1 March 2017. A related explanatory memorandum has also been published.

The Bank of England and Financial Services Act 2016 (the 2016 Act) ends the status of the Prudential Regulation Authority (PRA) as a subsidiary of the Bank of England (the Bank) by making the Bank the PRA. The 2016 Act also creates the Prudential Regulation Committee, through which the Bank must exercise its functions as the PRA. References to the PRA in the 2016 Act or any other enactment are now treated as references to the Bank acting as the PRA through its Prudential Regulation Committee.

The Regulations make consequential amendments to references to the Bank and the PRA in various enactments to account for the change in status of the PRA. These include the Building Societies Act 1986, the Freedom of Information Act 2000 and the Proceeds of Crime Act 2002, to account for the change in status of the PRA. In some cases, references to the Bank are clarified so that they are interpreted to exclude the Bank when it is acting as the PRA, to reflect an existing difference in the way that the enactment is intended to apply to the Bank and the PRA. In other cases, references to the PRA are removed and references to the Bank are expressly confirmed to include the Bank when it is acting as the PRA to reflect that the enactment should now apply to the Bank, including its new functions as the PRA as a whole.. Other amendments are included to remove ambiguity over how a reference to the Bank should be interpreted.

Paragraphs 7, 9 and 14 of Part 1 of the Schedule to the Regulations make amendments in consequence of the Financial Services Act 2012 (the 2012 Act) or in consequence of both the 2012 Act and the 2016 Act. The 2012 Act replaced the Financial Services Authority with the Financial Conduct Authority and the PRA and introduced new enforcement functions for the Bank, it also made amendments to the Financial Services and Markets Act 2000 (FSMA). The amendments made by the Regulations in consequence of the 2012 Act replace out-of-date references to the Financial Services Authority and update references to certain provisions of FSMA which the 2012 Act amended.

6.2 Financial Services Act 2012 Part 5 reviews: House of Commons Treasury Select Committee letter to Chancellor of the Exchequer

On 30 January 2017, the House of Commons Treasury Select Committee published the text of a letter sent by its Chairman, Andrew Tyrie, to the Chancellor of the Exchequer, Philip Hammond, on HM Treasury's powers to block public reviews under Part 5 of the Financial Services Act 2012.

In the letter, which is dated 24 January 2017, Mr Tyrie says that the Select Committee disagrees with the Government's view that it is appropriate for HM Treasury to have such extensive powers of direction over financial reviews. The Financial Services Act 2012 provides HM Treasury with powers to block reviews instigated by the regulator (that is the Financial Conduct Authority, the Prudential Regulation Authority or the Payment Systems Regulator). These can be exercised even when the regulators, the Treasury Select Committee and the public may consider a review essential. Mr Tyrie says that the power could prevent legitimate scrutiny of government executive action and it could also be seen to be used to cover up the Government's own mistakes.

Mr Tyrie says that it is all the more important that this obstacle to legitimate scrutiny be removed given HM Treasury's exclusive role in crisis-management and its wider influence on financial regulation. The clear conflict of interest between these functions and HM

Treasury's powers of direction over Part 5 reviews should not be left unaddressed. The Financial Services Act 2012 should be amended.

7. Securities markets

7.1 CCP resolution and resolution planning: FSB consults on draft guidance

On 1 February 2017, the Financial Stability Board (FSB) published a consultation paper containing draft guidance on central counterparty (CCP) resolution and resolution planning.

In August 2016, the FSB published a discussion note on essential aspects of CCP resolution planning and the draft guidance has been informed by responses to the discussion note. The draft guidance builds on the FSB's key attributes of effective resolution regimes for financial institutions which set out a framework for resolution of financial market infrastructures.

The guidance covers a number of aspects which authorities should consider when developing frameworks for resolving failing CCPs, including:

- policy objectives for CCP resolution to maintain financial stability;
- the powers that resolution authorities should have to maintain the continuity of critical CCP functions, return the CCP to a matched book and address default and non-default losses, including potential indicators for considering when a CCP should enter resolution;
- use of loss allocation tools in resolution and provisions necessary to protect creditor rights so the triggering of resolution by authorities does not leave creditors worse off than if the authorities had not stepped in; and
- steps authorities should take to establish crisis management groups for CCPs that are systemically important in more than one jurisdiction, develop resolution plans and conduct resolvability assessments.

Comments are requested by 13 March 2017. The guidance will be finalised in June 2017 in advance of the G20 leaders' summit.

The FSB will undertake further work on financial resources for CCP resolution and, based on further analysis and experience gained in resolution planning, determine by the end of 2018 whether it should develop further guidance on this issue.

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