



LATHAM & WATKINS

14 October 2020

# Financial Regulation Monthly Breakfast Webcast

# Overview



The latest Brexit developments, including the FCA's use of the Temporary Transitional Power and updated guidance for firms on the end of the transition period

ESMA's proposals in its final MAR Review report (including market soundings, insider lists and pre-hedging/front running)

FCA Decision Notice relating to market manipulation using CFDs

The new EU Markets in Cryptoassets Regulation – key issues and the impact on the UK market



LATHAM & WATKINS

The latest Brexit developments, including the FCA's use of the Temporary Transitional Power and updated guidance for firms on the end of the transition period

Anne Mainwaring

# Dear CEO letter: Final preparations for the end of the transition period

- Sets out expectations from the PRA and the FCA in relation to the final preparations for the end of the transition period
- Key message

***It is imperative that firms continue to build on their preparatory work to ensure that they, and to the extent possible their clients, are ready for a range of scenarios at the end of the transition period***

- It is important that firms continue to engage with clients and customers to minimize any disruption



# Continuity of wholesale banking business and contracts

- Firms should continue to take steps to facilitate the continuity of business and contracts:
  - Proactively engage with affected clients to complete repapering and on-boarding
  - Novate existing trades where necessary to ensure clients can manage risks related to lifecycle events
  - Where you plan to use national licensing regimes and exemptions in EU Member States, ensure that you will have everything in place by the end of the transition period to comply with requirements in those Member States
- Ensure that you have fully considered the impact on each client and whether the proposed changes, including any transfer of business, are in each **client's best interests**

# Data

- Consider whether contracts involving the transfer of personal data to your firm from the EEA need to be updated to comply with EU requirements or to consider other appropriate measures for personal data transfers from the EEA into the UK
- In the absence of a decision by the European Commission on UK data protection adequacy, the use of standard contractual clauses in relevant contracts is one of the available ways that EEA firms can comply with the EU's cross-border personal data transfer laws after the expiry of the transition period

# Trading venues

- If you are currently subject to the share and/or derivatives trading obligation consider:
  - How you will continue to meet your trading obligations in both the EU and UK under a range of scenarios at the end of the transition period
  - The implications for your clients of this analysis

# Payments

- Currently banks and payment service providers do not need to provide the name and address of the debtor when making payments between the UK and the EEA
- This information will however be required for payments between the UK and the EEA after the transition period ends



# Payments (cont.)

- Impacted firms should continue to take all reasonable steps to avoid disruption to payments, including ensuring that:
  - They are ready to provide the relevant customer information when making payments, including in relation to direct debit transactions
  - Customers are aware of the need to provide the information
- In the event any payments are disrupted, firms should ensure they are ready to communicate promptly with impacted customers to alert them to this and to give them the opportunity to make the payment in an alternative way

# Provision of retail banking services (noting wider read across)

- Firms with customers in the EEA should have plans in place in relation to their approach to servicing existing contracts
  - These plans should ensure the firm acts in accordance with local law and national regulators' expectations
  - Firms should be guided by what is the right outcome for their customers
  - Timely communications should be made to customers to enable them to make appropriate decisions and take necessary steps
- The regulators note that in many cases it would be a poor outcome for the customer for a firm to suddenly stop servicing them
- Firms that will be reducing or ceasing services should ensure that impacted customers are treated fairly and provide them with sufficient notice to seek alternative arrangements in an orderly manner
- Firms also need to consider and manage all remaining operational risks

# Other areas of focus for firms

- The regulators are not providing an exhaustive list of all the issues that may arise – firms need to consider the risks specific to their firm
- *E.g.* changes to reporting requirements, operational continuity of services including when provided by a third-party supplier, safeguarding of client money and custody assets and communications to customers

# FCA publishes rules that will apply at the end of the transition period

- The FCA has re-confirmed that it intends to apply temporary transitional relief on a broad basis from the end of the transition period until 31 March 2022
- This means that, where temporary transitional relief applies, firms can continue to comply with their existing obligations and can phase in the onshoring changes
- However, temporary transitional relief will not apply across the board

# FCA publishes rules that will apply at the end of the transition period (cont.)

- The FCA has called out the following areas where relief will not apply:
  - MIFID II transaction reporting
  - EMIR reporting obligations
  - SFTR reporting obligations
  - Certain requirements under MAR
  - Issuer rules
  - Contractual recognition of bail-in
  - Client Assets Sourcebook requirements (CASS)
  - Market-making exemption under the Short Selling Regulation
  - Use of credit ratings for regulatory purposes
  - Securitisation
  - Electronic commerce EEA firms
  - Mortgage lending after the transition period against land in the EEA
  - Payment Services – strong customer authentication and secure communication

# FCA publishes rules that will apply at the end of the transition period (cont.)

- In these areas compliance will be required for 1 January 2021 subject to regulatory forbearance
- The FCA has also published an updated version of the FCA Handbook to show the rules that will apply at the end of the transition period



# Dear CEO letter: Temporary permissions regime – operational readiness

- The PRA has also published a Dear CEO letter for firms entering the TPR
- Reminds TPR firms of the need to ensure that they are operationally prepared to enter the TPR and are able to meet the regulatory requirements once in it
- Sets out the obligations relevant to TPR firms at the different TPR lifecycle points
- Reminds firms in the TPR that they will come within the full scope of the supervision and rule-making powers of the UK regulators



LATHAM & WATKINS

ESMA's proposals in its final MAR Review report  
(including market soundings, insider lists and pre-  
hedging/front running)

Rob Moulton

# MAR / ESMA's Final Report - spot FX

- Detailed ESMA analysis on the spot FX market
- ESMA open minded on potential for future change / expansion
- But on balance, ESMA makes no proposals (in light of FX Global Code)

# MAR / ESMA - buy backs

- ESMA proposes a number of simplifications
  - Report only to the most liquid market
  - Simplification of data to be submitted
  - Broadly welcomed by industry so far

# MAR / ESMA - front running and pre-hedging

- ESMA proposes future guidance, and hints at content
  - Traceable benefit to client (pass it on?)
  - Clear mandate from client (ex-ante and trade-by-trade)
  - Minimise market impact
  - Ex-post provision of information to client on actual impact
- Front running restriction extended beyond those executing orders (*e.g.* issuer, investors)

# MAR / ESMA - market soundings

- ESMA reiterates its view – market soundings regime compulsory, not a safe harbour
  - ESMA asks European Commission to introduce pan-European sanctions regime for violations
- No change to the definition of a market sounding
  - But helpful proposal to say repeat wall-crossings need not all be treated as market soundings
- ESMA unmoved by arguments based upon geographical scope of MAR



# MAR / ESMA - insider lists

- Focus remains on including only persons who have actually accessed information
  - ESMA “*considers the inclusion of persons who could potentially have accessed a piece of inside information...as acceptable*”

# MAR / ESMA - PDMRs

- Exemption for corporate actions (provided that PDMRs are not treated advantageously compared to other parties)
- ESMA does not propose extending ban to parties acting on behalf of the company (inside information restrictions would still apply)

# MAR / ESMA - definition of inside information

- ESMA persuaded by industry feedback not to try to change the definition
- ESMA asks the European Commission to be permitted to provide further guidance, *e.g.* commodity derivatives, M&A

# MAR / ESMA - next steps

- European Commission to consider the guidance
- European Commission likely to make formal proposals in next few months
- Unlikely to be legislative change prior to 2022
- UK focus on updating UK legislation in light of Brexit



LATHAM & WATKINS

FCA Decision Notice relating to market manipulation  
using CFDs  
Jon Holland

# Abbattista Decision Notice

- Decision notice
- FCA findings
  - Corrado Abbatista (CA) - founding partner and CIO of Fenician Capital Management (dissolved in April 2019)
  - Fenician managed two offshore long / short equity funds and received management and performance fees
  - No performance fee was paid in FY2016/17 because Fenician failed to hit its targets and so no distribution was made to Fenician's members, including CA



# Abbattista Decision Notice (cont.)

- FCA findings (cont.)
  - Investment decisions “*followed a structured and considered process*”, although minutes of Investment Committee meetings were not consistently maintained
  - CA “*had the final say*” on investment decisions
  - CA received external compliance training, including on MAR
  - CA mainly placed orders and executed trades using a direct market access system, which looked for liquidity first in a dark pool, then in four “lit” trading venues

# Abbattista Decision Notice (cont.)

- FCA findings (cont.)
  - CA typically traded CFDs
  - Fenician's involvement would not typically be apparent to counterparties, even on settlement of a trade
  - CA's misconduct consisted of placing misleading orders opposite genuine iceberg orders

# Abbattista Decision Notice (cont.)

- FCA findings (cont.)
  - For example, in January 2017, Fenician wanted to increase a short position in M&S shares, which it held until May 2017
    - CA placed a genuine **sell** order as an iceberg order at the best offer - that was (unsurprisingly) filled, mostly after . . .
    - CA placed a fully visible **buy** order - that was (also unsurprisingly) not filled, because it was
      - Much larger (10x) than the prevailing volumes for trades in M&S shares
      - Priced away from the existing best bid and cancelled within one second after the sell order was filled and nine seconds after the buy order was placed

# Abbattista Decision Notice (cont.)

- FCA findings (cont.)
  - CA repeated this pattern of trades on the same day, increasing Fenician's short position by 43,000 shares
  - Between January and May 2017, CA carried out similar trades involving M&S, Diageo, Istock, Thomas Cook and Redrow
  - In the meantime, CA was warned by a colleague not to trade in this way, but continued to trade until the colleague eventually instructed him to stop

# Abbattista Decision Notice (cont.)

- FCA findings (cont.)
  - CA's actions breached Articles 15 (*placing an order . . . which gives, or is likely to give, a false or misleading signal as to the supply of or demand for a UK listed share*) and 12 (*placing an order . . . or any other behaviour which . . . gives, or is likely to give, false or misleading signals as to the supply of, demand for, or price of, a financial instrument . . . [without] legitimate reasons . . . [or in conformity with] an accepted market practice*)

# Abbattista Decision Notice (cont.)

- Penalty
  - Financial penalty of GBP100,000 based on level 4 seriousness (a) because CA's conduct was reckless and repeated and (b) despite:
    - The absence of any personal benefit
    - CA's earnings in the relevant period being GBP5,250
  - Prohibition from performing any function in relation to any regulated activity



# Abbattista Decision Notice (cont.)

- CA's arguments (which the FCA rejected) included:
  - The cancelled orders were a form of "*liquidity testing*" and were cancelled so quickly because CA was worried about algo traders executing against them
  - The orders were open (albeit for a short period), not complicated, unlike the trades in *Coscia*, and not expressly prohibited by FCA guidance at the time
- CA has referred the decision to the Upper Tribunal

## In other (MAR) news . . .

- Julia Hoggett (Director, Market Oversight, at the FCA) spoke at the City Financial Global event on 12 October 2020
- Key points:
  - *“At a time where capital raising activity is vital to fuel much needed economic activity, we must be crystal clear that behaviours that risk disrupting that activity will not be tolerated”*
  - The FCA has placed *“the market abuse risk assessment at the heart of how [it] encourages firms and venues to think about all the activities they need to undertake to surveil for market abuse”*

# In other (MAR) news . . . (cont.)

- Key points (cont.):
  - The FCA's review of typologies of market abuse suggests that the pandemic has not given rise to new forms of market abuse, but it may mean that market abuse is more prevalent and may manifest itself differently
  - For example:
    - The scale of new issuances in the UK since Spring 2020 generated significant inside information that needed to be managed appropriately
    - Inside information has changed as a result of the pandemic (e.g., knowledge that a businesses' operations are about to close down, the pace of cashflow burn etc.)
    - Controlling inside information within the home presents new challenges
    - Increased M&A activity will exacerbate these risks

# In other (MAR) news . . . (cont.)

- Key points (cont.):
  - Dynamic risk assessment is therefore even more crucial as is appropriate recalibration of surveillance systems to deal with greatly increased alert volumes triggered by increased levels of activity
  - If firms have a “backlog” of STORs built up during the pandemic, they need to tell the STOR Supervision team
  - Firms have generally overcome the challenges of remote recording and surveillance – and the FCA’s *“expectation is that, going forward, office and working from home arrangements should be equivalent – this is not a market for information that we wish to see be arbitrated”*

# In other (MAR) news . . . (cont.)

- Key points (cont.):
  - The FCA expects firms to have updated policies, refreshed training and put “*rigorous oversight*” in place – “*particularly regarding the risk of use of privately owned devices*”
  - These steps need to be demonstrable to internal audit and the FCA
  - Good culture is even more important where colleagues may not overhear – and report - inappropriate behaviour in the office
  - The FCA is “*exceptionally focused*” on single stock events (*i.e.*, individuals using inside information for personal trades) and is watching closely

## In other (MAR) news . . . (cont.)

- Key points (cont.):
  - The FCA has excellent data from reporting by firms which suggests that “*discipline in UK markets is overall strong and effective*”, although potentially anomalous trading increased slightly in 2019, demonstrating the need for continued vigilance
  - Where firms conduct an internal investigation, that needs to be discrete in order to avoid tipping off, especially where the investigation is prompted by an FCA information requirement



LATHAM & WATKINS

The new EU Markets in Cryptoassets Regulation –  
key issues and the impact on the UK market

Stuart Davis

# MiCA proposal - background

- Part of the EU Digital Finance package which seeks to:
  - Tackle EU fragmentation
  - Facilitate digital innovation
  - Create EU financial data space
  - Address challenges and risks, promote resilience, data protection and prudential supervision
- Published alongside a proposal for a pilot regime on DLT market infrastructures
- European Commission particularly concerned about fragmentation in the cryptoassets space across the EU – core objectives “*cannot [currently] be achieved*”
- Harmonisation should lead to growth and increased innovation



# MiCA - who is covered?

## Covers:

- **Issuers:** any legal person who offers to the public any type of cryptoassets or seeks the admission of such cryptoassets to a trading platform
- **Cryptoasset service providers:** firms providing a range of specified services relating to cryptoassets
- Definition of **cryptoassets:** “*a digital representation of value or rights that may be transferred and stored electronically, using distributed ledger technology or similar technology*”

# MiCA - tokens

3 types of relevant tokens:

- **Asset-referenced tokens:** cryptoassets that purport to maintain a stable value by referring to the value of several fiat currencies that are legal tender, one or several commodities or one of several cryptoassets, or a combination of such assets
- **E-money tokens:** cryptoassets to be used as a means of exchange and that purport to maintain a stable value by referring to the value of a fiat currency that is legal tender
- Cryptoassets that are **neither of the above**

# MiCA - what is not covered?

- Cryptoassets which are:
  - MiFID II financial instruments or structured deposits
  - Electronic money, except where they qualify as e-money tokens
  - Bank deposits
  - Securitisations under the Securitisation Regulation
- Insurance/re-insurance/retrocession activities under Solvency II
- Exclusively intra-group services

## **Issuers of asset-referenced tokens**

- Must be authorised by their NCA
- Must publish a whitepaper which is approved by their NCA
- Subject to MiFID-like prudential, conduct and governance regulation
- Must maintain a reserve backing the tokens which must be safeguarded
- EBA can designate “significant asset-referenced tokens” and issuers of these tokens will be subject to enhanced regulation through a supervisory college – designed to mitigate financial stability risks
- Compliant issuers can issue tokens throughout EU

# MiCA – issuers (cont.)

## Issuers of e-money tokens

- Must be authorised by NCA as credit institutions or e-money institutions
- Must submit whitepaper to NCA at least 20 working days before publication
- Must ensure that:
  - Holders have a claim on the issuer
  - Tokens are issued at par value on receipt of funds
  - Tokens are redeemable immediately on demand
  - Conditions of redemption are clearly stated
  - No interest is payable on the tokens
- EBA can also designate “significant e-money tokens”
- Compliant issuers can issue tokens throughout EU

# MiCA – issuers (cont.)

## Other issuers

- No authorisation requirement
- Must submit whitepaper to NCA at least 20 working days before publication
- Must confirm why the token is not a financial instrument, deposit etc.
- Must ensure marketing communications comply with form and content requirements
- Compliant issuers can issue tokens throughout EU
- Broad range of powers for NCAs to suspend or prohibit offers to the public
- Prospectus Regulation-style public offer exemptions available

# MiCA - Market Abuse Regime

- Prohibitions on:
  - Insider dealing
  - Unlawful disclosure of inside information
  - Market manipulation
- Inside information defined to mean “*any information of a precise nature that has not been made public, relating, directly or indirectly, to one or more issuers of cryptoassets or to one or more cryptoassets, and that, if made public, would likely have a significant effect on the prices of those cryptoassets*”

# MiCA - cryptoasset services and activities

<b>MiCA Services and Activities</b>	<b>MiFID II Investment Services and Activities</b>
Custody and administration of cryptoassets on behalf of third parties	Safekeeping and administration of financial instruments
Operation of a trading platform for cryptoassets	Operation of an MTF; operation of an OTF
Exchange of cryptoassets for fiat currency that is legal tender	Dealing on own account
Exchange of cryptoassets for other cryptoassets	N/A
Execution of orders for cryptoassets on behalf of third parties	Execution of orders on behalf of clients
Placing of cryptoassets	Underwriting of financial instruments; placing of financial instruments on a firm commitment basis
Reception and transmission of orders for cryptoassets on behalf of third parties	Reception and transmission of orders in relation to one or more financial instruments
Providing advice on cryptoassets	Investment advice



# MiCA - cryptoasset service providers

- Must be authorised by NCA
- Credit institutions and MiFID investment firms do not need to be re-authorised
- Cryptoasset service providers are subject to:
  - Client best interest rule
  - Prudential requirements
  - Organisational requirements
  - Conflicts of interests
  - Outsourcing rules
  - Complaints-handling
  - Additional obligations for particular services (e.g. trading platforms)

# MiCA - transitional arrangements (from in force date)

- Cryptoasset service providers will have 18 months to comply
- Grandfathering provisions for tokens offered prior to in-force date
- No grandfathering for asset-referenced tokens and e-money tokens

# MiCA - next steps

- First reading for European Parliament (EP) and then European Council (EC) (no time limit)
- If not agreed, second reading (maximum 5 month time limit)
- If still not agreed, third reading (maximum 10 week time limit)

# Global Financial Regulatory Blog

LATHAM & WATKINS LLP



## Global Financial Regulatory Blog

Insights and commentary on financial regulatory issues and developments impacting business and innovation in the US, Europe, Asia, and across the world.

Home

About Us

Contact

Subscribe

Search



### About

Welcome to the Latham & Watkins Global Financial Regulatory Blog.

Here, you will find our views and short updates on the most important financial regulatory developments impacting business and innovation across the world.



<https://www.globalfinregblog.com/>

LATHAM & WATKINS

### Topics

Benchmark Regulations

Conduct of Business

Derivatives

Financial Crime

Fintech and Cryptocurrency

# London Financial Regulatory Portal

Home | London Financial Regulatory Portal

London Financial Regulatory Home

The Practice

Markets ▼

Retail ▼

Culture & Governance ▼

FinTech

Brexit

Guides

Events ▼

Monthly Breakfast Seminar  
Materials

Thought Leadership



Markets



more >

Retail



more >

Culture & Governance



more >

FinTech



more >

Brexit



more >



# Recent Thought Leadership

Home | London Financial Regulatory Portal | E

London Financial Regulatory Home

The Practice

Markets ▼

Retail ▼

Culture & Governance ▼

FinTech

Brexit

Guides

Events ▼

Monthly Breakfast Seminar  
Materials

Thought Leadership

[MiCA: EU Commission Publishes Comprehensive Cryptoasset Market Regulation Proposal](#)

[Latham Launches 2nd Edition of Innovative Culture Assessment Framework](#)

[The MAR Review — ESMA's Final Report](#)

[Cyber and Payments Are Priority Areas for Policy Changes](#)

[Sustainable Finance and Climate Change Risk in Financial Services For Insurers 2020](#)

[MAR and Sustainable Investing / ESG](#)

[BoE Governor Speaks: Payments Firms Should Expect Regulatory Change](#)

