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PRIVATE BANK BRIEFING

LATHAM & WATKINS

Issues Impacting the Private Bank Sector

Welcome to our quarterly round-up of legal and compliance issues impacting private banks and their clients.

In This Edition

Brexit: Latest Updates

On 22 July 2020, HM Treasury published a policy statement setting out the UK government's rationale and proposed approach for extending the transitional period for third country benchmarks under the UK Benchmarks Regulation (UK BMR) from 31 December 2022 to 31 December 2025.

HM Treasury has decided to depart from the timing of the end of the third country transitional period under the EU BMR by extending the third country transitional period under the UK BMR by three years, to 31 December 2025.

Under both the EU BMR and the UK BMR, regulated entities in either the EU or the UK respectively are not permitted to use third country benchmarks from 1 January 2023, the end of the third country transitional period, unless such benchmarks are subject to an equivalence determination or have been recognised or endorsed.

HM Treasury has decided to depart from the timing of the end of the third country transitional period under the EU BMR by extending the third country transitional period under the UK BMR by three years, to 31 December 2025. This measure will allow UK regulated entities to continue to access third country benchmarks for an extended period of time with the intention of resolving concerns about market fragmentation and the current lack of take-up of the EU BMR third country regime.

Separately, the revised compromise text of the European Commission's proposal for a regulation amending the EU BMR as regards the exemption of certain third country foreign exchange benchmarks and the designation of replacement benchmarks for certain benchmarks in cessation also suggests extending the transitional provisions for third country benchmarks until 2025. ISDA is strongly in support of this proposal.

Temporary Permissions Regime

Ahead of the end of the transition period, regulators are emphasising the need for firms to ensure that they are ready to comply with their "Day 1" obligations in this regard. This includes firms entering the Temporary Permissions Regime (TPR) that will need to consider their obligations under UK law once their temporary permission takes effect, as they will come within full scope of the UK regulators' supervisory powers.

On 1 September 2020, the PRA published a Dear CEO letter which emphasises that firms need to take all appropriate actions to ensure that they are operationally prepared for the end of the transition period on 31 December 2020 at 11 p.m., when the TPR will take immediate effect.

The PRA has also created a new webpage summarising its approach to the TPR and highlighting the key requirements of the TPR for branches.

Sustainable Finance: AFME White Paper "Governance, Conduct and Compliance in the Transition to Sustainable Finance"

Latham & Watkins has collaborated with the Association for Financial Markets in Europe (AFME) to produce Governance, Conduct and Compliance in the Transition to Sustainable Finance, a first-of-its-kind roadmap to assist financial services firms with establishing and furthering their corporate purpose, objectives, and strategy in relation to sustainable finance.

Focused on the European regulatory framework, the paper sets out 15 key principles for boards and leaders at financial institutions as they develop their transition to sustainable finance.

Focused on the European regulatory framework, the paper sets out 15 key principles that boards and leaders at financial institutions may wish to consider in order to assist in the development of their approach to the transition to sustainable finance. The principles cover:

Objectives and governance

Ensuring that a central corporate purpose is established and that there is collective understanding, oversight, and accountability in relation to sustainable finance-related risks amongst internal and external stakeholders.

Risk management

Considering whether and how sustainable finance-related risks impact existing financial and non-financial risk factors — and whether they create new risk factors— as well as determining how these sustainable finance-related risk factors can be integrated into existing risk management frameworks, strategically and in line with the defined risk appetite.

Compliance and monitoring

Considering how to measure, monitor, and mitigate the key risks arising from the transition to sustainable finance, including the tools and metrics that may be necessary to achieve this as well as the existing processes that can be leveraged.

Impact measurement

Considering how to assess the progress and effectiveness of existing strategies deployed against established sustainable finance goals; determining what adjustments, if any, are required; and identifying opportunities for further development and innovation.

MiFID II: European Commission Adopts Legislative Proposals on Amendments to MiFID II

The European Commission has adopted a legislative proposal for a directive amending MiFID II as part of a capital markets recovery package designed to facilitate an economic recovery following the COVID-19 pandemic. The proposed text amending MiFID II was published on 24 July 2020, along with proposals to amend securitisation rules, the CRR, and the Prospectus Regulation.

Private banks should note that the European Commission is proposing targeted amendments to MiFID II requirements in order to reduce some of the administrative burdens that experienced investors face in their business-to-business relationships. The amendments refer to a number of requirements that were identified during the European Commission's MiFID/MiFIR public consultation as being overly burdensome or hindering the development of European markets. The COVID-19 crisis makes alleviating unnecessary burdens and providing opportunities to growing markets even more important. The European Commission is also proposing to amend the MiFID rules affecting energy derivatives markets.

At the same time, the European Commission has opened a public consultation on amendments to the MiFID II Delegated Directive to increase the regime for research on small- and mid-cap issuers and on fixed-income instruments to help the recovery from the COVID-19 pandemic. In particular, small- and mid-cap issuers need a good level of investment research to give them enough visibility to attract new investors. Notably, the European Commission is consulting on a "research unbundling" exception under this proposed new alleviated regime.

The amendments refer to a number of requirements that were identified during the European Commission's MiFID/MiFIR public consultation as being overly burdensome or hindering the development of European markets.

Legislative proposal amending MiFID II

The European Commission's proposals cover the following areas:

Amendments to information and disclosure requirements

- Phasing out paper as the default method for communication
- Introducing an exemption for eligible counterparties and professional clients from the cost and charges disclosure requirements
- Allowing for a delayed transmission of cost information when using distant communication channels
- Relaxing rules requiring ex-post statements to eligible counterparties and professional clients concerning the services they have received
- Allowing professional clients to opt in to cost-benefit analysis in case of switching investments
- Suspending the requirement to publish best execution reports

In its draft proposal, the European Commission exempts investment firms from providing the disclosure of costs and charges to professional clients and eligible counterparties for certain MiFID services other than investment advice and portfolio management. The ECON Committee's draft report of 18 September 2020 on the European Commission's proposal recommends that investment advice and portfolio management should also be excluded from cost and charges disclosure for professional clients (with an opt-in clause) as those clients should be generally familiar with the cost structure of these services.

The ECON Committee's draft report also proposes to delete the limitation that information on cost and charges must always be transmitted in "electronic format" to accommodate the needs of older and less computer literate clients.

With regards to suspending the requirement to publish best execution reports, the ECON Committee is proposing to extend this to best execution reports for retail clients, as well as for venues.

Amendments to product governance

- Exempting bonds with make-whole clauses from the MiFID II product governance regime
- Complementing the exemption by introducing a clear rule that such non-complex bonds with make-whole clauses would not be considered a PRIIP

The ECON Committee's draft report states that the exemption from product governance requirements should also be extended to other simple products such as other "plain vanilla bonds", UCITS, and shares traded on regulated markets.

Energy derivatives markets

The proposed amendments in relation to energy derivatives markets recalibrate the position limit regime and the scope of the hedging exemption in order to ensure that growing euro-denominated markets are able to foster and allow producers and manufacturers to hedge their risks whilst safeguarding the integrity of commodity markets.

Consultation on amendments to MiFID II Delegated Directive

The European Commission is consulting on:

An alternative alleviated research regime

- Introducing an alternative alleviated regime for investment firms when the research is provided exclusively on small- and mid-cap issuers or fixed-income instruments

A "research unbundling" exception

- Introducing a narrowly defined "research unbundling" exception under which investment firms would be allowed to pay jointly for the provision of research and for the provision of execution services on small- and mid-cap issuers or fixed-income instruments

The ECON Committee proposes that providing a different treatment of research for small- and mid-cap issuers should be moved into the Level 1 text to make sure that it is an exemption mandated by the legislator and not the start to the unravelling of the unbundling regime. This would also give the legislator a better say in determining the type of financial instrument covered by an exception, as well as the conditions under which the exemption applies.

Next steps

The proposed amendments to MiFID II still need to be approved by the European Parliament and Council and then transposed into national law by each Member State. Therefore, the timing for the implementation of these proposed changes remains uncertain. In the context of Brexit, it is unclear if, and how, these changes will be implemented in the UK.

The closing date for the consultation on amendments to the MiFID II Delegated Directive was 4 September 2020.

For more details, see Latham's *Client Alert* European Commission Proposes Changes to MiFID II Due to COVID-19.

FCA Market Watch Issue 64: Brexit and MiFID II Transaction Reporting Issues

On 27 August 2020, the FCA published issue 64 of its Market Watch newsletter, which provides information to help MiFID II firms prepare for the end of the Brexit transition period on 31 December 2020.

Private banks are reminded that the FCA's temporary transitional power — which allows firms time to adapt to new requirements that apply as a result of Brexit — does not apply to the transaction reporting rules under MiFID II. Firms and Approved Reporting Mechanisms (ARMs) must therefore ensure that they comply with the changes to their regulatory obligations by the end of the transition period. Private banks that are unable to comply fully with the transaction reporting regime immediately following the end of the transition period will need to be able to back-report missing, incomplete, or inaccurate transaction reports as soon as possible.

Private banks are reminded that the FCA's temporary transitional power — which allows firms time to adapt to new requirements that apply as a result of Brexit — does not apply to the transaction reporting rules under MiFID II.

The FCA also confirms that, as part of the development of a post-exit MiFID regime, industry testing for its Financial Instruments Transparency System (FCA FITRS) opened on 5 October 2020. The FCA's Financial Instruments Reference Data System (FCA FIRDS) is still available for testing.

CRD V: UK Implementation

HM Treasury has published a consultation paper on updating the UK's prudential regime before the end of the Brexit transition period, focusing on the UK implementation of the CRD V Directive.

The UK is required to transpose the CRD V Directive by 28 December 2020.

HM Treasury has stated that it will use secondary legislation to amend the UK legislation that implemented the CRD IV Directive to reflect amendments to that Directive made by the CRD V Directive. This legislation will give the PRA new or updated powers to implement CRD V, ensuring that it can update its rulebook as necessary.

In the consultation, HM Treasury seeks views on issues requiring secondary legislation including:

- Macro-prudential tools
- Holding companies
- Equal pay framework and enforcement

HM Treasury has also confirmed that it intends to exempt FCA-authorised investment firms from the scope of UK measures implementing CRD V.

The deadline for responses was 19 August 2020. The UK is required to transpose the CRD V Directive by 28 December 2020.

PRA consultation on implementation of the CRD V Directive

On 31 July 2020, the PRA published a consultation paper (CP12/20) on the implementation of the CRD V Directive.

The PRA proposes not to implement the requirements of CRD V that do not need to be complied with by firms until after the end of the transition period, particularly some of the requirements for EU intermediate parent undertakings (IPUs) and Pillar 2 requirements for the leverage ratio.

The PRA considers that some of its proposals will need to be amended to ensure that they are legally operational following the end of the transition period.

Remuneration

The PRA's approach to implementing the CRD V reforms relating to remuneration, include:

- Identification of material risk takers (MRTs)
- Minimum deferral period
- Payment in instruments
- Proportionate application of remuneration requirements

The PRA intends to amend the Remuneration Part of the PRA Rulebook and its supervisory statement on remuneration (SS2/17).

The PRA's proposals are based on the final draft regulatory technical standards (RTS) on the identification of MRTs published by the EBA in June 2020. The PRA may need to re-consult on these proposals if the version of the RTS enacted as EU law substantively differs from that draft version.

Governance

The PRA's approach to implementing the CRD V reforms relating to governance, include:

- Operational risk from outsourcing
- Loans to board members
- Verification of fitness and propriety

The deadline for responses to the consultation paper was 30 September 2020.

The PRA intends to publish a second consultation in autumn 2020 on the remaining elements of the CRD V not covered in CP12/20 and changes introduced by the CRR II.

FCA consultation paper on updating the Dual-regulated firms Remuneration Code to reflect the CRD V

On 3 August 2020, the FCA published a consultation paper on updating its Dual-regulated firms Remuneration Code to reflect the CRD V (CP20/14).

The FCA intends to update the Dual-regulated firms Remuneration Code set out in SYSC 19D to reflect the remuneration requirements introduced by the CRD V and the PRA's proposals for implementing these requirements set out in its July 2020 consultation paper.

The FCA will not apply the CRD V remuneration requirements to solo-regulated investment firms. Instead, these firms should continue to apply the FCA's existing remuneration regime until the new UK prudential regime for investment firms is in place.

The deadline for responses was 30 September 2020. The FCA intends to publish a policy statement before the CRD V transposition deadline.

Market Abuse: ESMA's Outcome of the MAR Review

As part of the European Commission's review of the workings of the Market Abuse Regulation (EU) 596/2014 (MAR), ESMA launched a consultation paper on 3 October 2019 and has now published its feedback in a Final Report, which is being made available to the market and the European Commission.

Private banks should be aware that ESMA is proposing amendments in the following key areas:

Pre-hedging / front running: ESMA proposes developing detailed guidance on acceptable practice, but identifies a number of factors such as trade-by-trade transparency that may be disruptive to some existing practices.

Market soundings: ESMA has maintained its stance that the market soundings regime is compulsory, and is unmoved by arguments driven by conflicts of laws and extraterritorial effect.

Insider lists: ESMA has provided some flexibility on the question of who should be included on an insider list, and how large a permanent insider list should be, without changing the thrust of its overall position that deal lists should capture only those who have accessed inside information.

Spot FX contracts: ESMA's conclusion is not to include spot FX contracts within the ambit of MAR, and instead take into account progress with the embedding of the FX Global Code.

The process now reverts to the European Commission, which will consider various submissions, including the Final Report, and then contemplate legislative proposals to amend MAR.

For more details, see Latham's *Client Alert* The MAR Review — ESMA's Final Report.

SMCR: FCA Publishes Consultation Paper on Extending Implementation Deadlines for the Certification Regime and Conduct Rules

HM Treasury has agreed to delay the deadline by which FCA solo-regulated firms must have first assessed the fitness and propriety of their Certified Staff until 31 March 2021. This delay will give firms significantly affected by COVID-19 time to make the changes they need.

The FCA proposes in CP20/10 to amend its rules to effect this change. The FCA also proposes to make a corresponding extension to the deadline for training staff in the Conduct Rules and reporting Directory Person data from 9 December 2020 to 31 March 2021. The FCA believes that extending these deadlines will ensure that these targets remain consistent and will provide extra time for firms that need it to deliver effective training on the Conduct Rules.

The FCA is focused on ensuring that the SMCR continues to deliver significant improvements in conduct and governance. However, the FCA wants to give firms whose business has been impacted by the COVID-19 pandemic more time to implement and fully embed the Conduct Rules within their organisation.

Firms should continue with their programmes of work in these areas. If they are able to certify staff earlier than March 2021, they should do so. Firms should also not wait to remove staff who are not fit and proper from certified roles.

The FCA will still publish details of certified employees of solo firms on the Financial Services Register starting from 9 December 2020. The FCA encourages firms that are able to do so to provide this information before March 2021.

The deadline for responses to the consultation paper was 14 August 2020.

COVID-19: ESMA Proposes to Further Postpone CSDR Settlement Discipline

On 28 August 2020, ESMA published a final report on draft RTS postponing the date of entry into force of the European Commission Delegated Regulation (EU) 2018/1229 (RTS on settlement discipline) until 1 February 2022. This postponement is due to the impact of the COVID-19 pandemic on the implementation of regulatory projects and IT deliveries by CSDs and a wide range of market participants and follows a request from the European Commission.

The measure is additional to the European Commission Delegated Regulation (EU) 2020/1212, based on ESMA's proposal to amend the RTS on settlement discipline to postpone its date of entry into force from 13 September 2020 to 1 February 2021.

The RTS on settlement discipline cover measures to prevent and address settlement fails, including:

- Rules for the trade allocation and confirmation process
- Cash penalties on failed transactions
- Mandatory buy-ins
- Monitoring and reporting settlement fails

The UK has said it will not implement the settlement discipline regime. However, ICMA has previously noted that "UK trading entities, along with all third country trading entities, are still likely to be brought into scope of the EU CSDR, as it applies at EU settlement level and requires trading parties to put enforceable contractual arrangements in place importing the mandatory buy-in regime". Therefore, UK firms still need to think about the settlement discipline regime, as it will impact firms when trading instruments settled in EU CSDs.

Following the endorsement of the RTS by the European Commission, the Delegated Regulation will then be subject to the non-objection of the European Parliament and Council.

PRIIPs: HM Treasury Policy Statement on Amendments to Retained EU Law Version of PRIIPs Regulation

On 30 July 2020, HM Treasury published a policy statement on amendments to the PRIIPs Regulation. The policy statement provides an update on HM Treasury's previously announced intention to bring forward amendments to the onshored PRIIPs Regulation to improve the functioning of the UK PRIIPs regime.

Industry has widely condemned the PRIIPs standardised disclosure document (the KID) as being potentially misleading to ordinary consumers with regards to the products it is intended to describe. The European Supervisory Authorities carried out a recent review of the KID but failed to agree on proposals to amend it following the outcome of the review, which was published on 20 July 2020.

HM Treasury's proposed amendments target only what it believes are the most critical concerns with the PRIIPs Regulation and aim to ensure that UK retail investors are provided with more appropriate PRIIPs disclosures.

Brexit gives the UK an opportunity to amend and improve the KID. The UK government's proposed amendments will enable the FCA, once the UK is no longer bound by the EU regime, to make supplementary provisions and amendments to the RTS that supplement the PRIIPs Regulation (PRIIPs RTS) with the aim of avoiding consumer harm, addressing distortions of competition, and providing greater certainty to industry. The FCA also intends to explore possible solutions to rectify current issues with the PRIIPs Regulation.

HM Treasury's proposed amendments target only what it believes are the most critical concerns with the PRIIPs Regulation and aim to ensure that UK retail investors are provided with more appropriate PRIIPs disclosures. In the longer term, the government intends to conduct a more wholesale review of the disclosure regime for UK retail investors, including, for example, how to harmonise the UK PRIIPs regime with requirements set out in MiFID II.

Of interest to private banks, HM Treasury has proposed the following amendments to the onshored PRIIPs Regulation:

FCA to clarify the scope of the PRIIPs Regulation through its rules

Whilst the definition of a PRIIP will remain unchanged, the government has proposed an amendment that delegates a power to the FCA to clarify the scope of PRIIPs through its rules. The government has said there is "currently significant uncertainty in industry as to the precise scope of PRIIIPs, such as with respect to corporate bonds".

"Performance scenario" to be replaced with "appropriate information on performance" in the PRIIPs Regulation

The PRIIPs Regulation requires PRIIPs manufacturers to include performance scenarios in the KID. The methodology for calculating these scenarios is set out in the PRIIPs RTS, and according to the government "has been criticised for producing misleading performance scenarios across a wide range of products". The policy statement explains that "this is believed to be due, at least in part, to the prescribed methodology in the PRIIPs RTS relying on past performance to project future performance in a way that generates procyclicality". The government has therefore proposed an amendment to replace the term "performance scenario" with "appropriate information on performance" in the PRIIPs Regulation. The FCA will then be able to amend the PRIIPs RTS to clarify what information on performance should be provided in the KID.

Further extension of the exemption currently in place for UCITS funds

Until 31 December 2021, undertakings for the collective investment in transferable securities (UCITS) funds are exempted from the requirements of the PRIIPs Regulation. Until that date, UCITS funds must produce a Key Investor Information Document (KIID) as set out in the UCITS Directive, instead of a KID. Since the government currently considers that the existing rules for UCITS disclosure are satisfactory, it has proposed an amendment delegating a power to HM Treasury to further extend the exemption for UCITS for a maximum of five years.

HM Treasury indicated in the policy statement that it intends to legislate for these proposed amendments to the onshored PRIIPs Regulation when parliamentary time allows.

For more details, see Latham's blog post HM Treasury Policy Statement Addresses Pressing Concerns With PRIIPs Regulation.

Outsourcing: AFME Paper "Outsourcing — Guidance on the Legal and Regulatory Framework"

In light of the increasing regulatory focus on outsourcing in financial services, AFME, in collaboration with Latham & Watkins, has published a reference paper titled Outsourcing — Guidance on the Legal and Regulatory Framework. The paper is aimed at compliance, legal, and risk teams within regulated firms, and is designed to provide a single reference point for the key legislation, rules, and guidance in relation to outsourcing. It also provides an overview of all relevant European legal and regulatory requirements for arrangements with group entities and third parties and outlines jurisdiction-specific considerations required by financial services regulators in France, Germany, Ireland, Italy, Luxembourg, Spain, and the UK.

As a result of Brexit, as well as regulators' increased focus on outsourcing, there is now a significant emphasis on the need for intra-group outsourcing arrangements (where a firm enters into an outsourcing arrangement with a separate legal entity within the same group) and intra-entity outsourcings (where a firm enters into an outsourcing arrangement within the same legal entity, such as outsourcings between two branches of the same legal entity) to meet the same requirements as outsourcings to external third parties. Accordingly, the paper identifies the application of the relevant outsourcing requirements in both an intra-group and intra-entity context in order to help firms navigate their obligations in this respect.

Ahead of the end of the Brexit transition period, the paper also identifies some of the key Brexit implications relevant to the outsourcing requirements as well as the specific considerations for UK branches of EEA firms in this context.

HM Treasury Consults on Proposed Reforms to Regulatory Framework for Financial Promotion Approvals

On 20 July 2020, HM Treasury published a consultation paper on a regulatory framework for approval of financial promotions. The consultation proposes to establish a regulatory "gateway" that a firm must pass through before it is able to approve the financial promotions of unauthorised firms.

The aim of the proposal is to provide better protections against misleading and inadequate promotions for consumers of financial products.

The UK government considers that the current requirement for an authorised firm to approve the financial promotion of an unauthorised firm may not operate as a strong enough safeguard to ensure that promotions comply with FCA rules that such promotions are fair, clear, and not misleading. Any authorised firm is able to approve any financial promotion of an unauthorised firm, as set out in section 21(2)(b) of FSMA, without any restriction. Legislation does not currently provide a specific regime for the FCA to assess the suitability of an authorised firm before it begins approving such promotions.

The consultation proposes to establish a regulatory "gateway" that a firm must pass through before it is able to approve the financial promotions of unauthorised firms.

In order to strengthen the FCA's ability to ensure that the approval of financial promotions operates effectively, the government proposes to amend FSMA so that the general ability of authorised firms to approve the financial promotions of unauthorised firms is removed. Instead, unauthorised persons would only be able to communicate financial promotions that were approved by a firm that had obtained the FCA's consent to provide such approval. This would enable the FCA to operate a specific gateway that a firm is required to pass through before it could approve the financial promotions of unauthorised persons.

The proposed change would, in the government's view, lead to several improvements in the regulatory regime for financial promotions communicated by unauthorised persons, including:

- More effective FCA oversight and supervision
- More effective prevention and intervention
- Ensuring that approver firms have the relevant expertise
- Improved due diligence

The government has proposed two options to introduce the new "gateway":

- Amend section 21(2)(b) of FSMA so that unauthorised persons are only able to communicate their own financial promotions if they have been approved by a firm that has obtained the FCA's consent to provide such approval
- Specify the approval of financial promotions communicated by unauthorised persons as a "regulated activity" under FSMA, which would involve amending the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO), to make the approval of financial promotions of unauthorised persons a regulated activity with firms requiring a Part 4A permission from the FCA, and amend section 21(2)(b) of FSMA to provide that only financial promotions of unauthorised persons approved by a firm with the relevant Part 4A permission can be lawfully communicated

The government clearly states that the proposal will not affect the way authorised firms currently communicate their own financial promotions, approve their own promotions for communication by unauthorised persons, or approve the promotions of unauthorised persons within the same corporate group.

The deadline for responses is 25 October 2020. For more details, see Latham's blog post UK Government Proposes to Strengthen Protections Around Promotion of Financial Products and Cryptoassets.

UK Government Publishes Revised Draft Debt Respite Scheme Regulations

On 10 September 2020, the UK government published a revised draft version of the Debt Respite Scheme (Breathing Space Moratorium and Mental Health Crisis Moratorium) (England and Wales) Regulations 2020 (the Breathing Space Regulations).

The Breathing Space Regulations establish the first part of a debt respite scheme for individuals in problem debt and supersede the draft version that was published on 15 July 2020. They give eligible people in problem debt who receive professional debt advice access to a 60-day period in which interest, fees, and charges are frozen and enforcement action is paused.

For people receiving mental health crisis treatment, the Breathing Space Regulations establish an alternate route by which the protections of a moratorium may be accessed and ensure that the protections are in place for the duration of their crisis treatment.

The Breathing Space Regulations confirm that the first part of the debt respite scheme will come into force on 4 May 2021, other than for certain limited provisions. Private banks should act now to ensure they can implement these regulations in time.

LIBOR: Update on Transition

Private banks should take note of the recent developments in relation to LIBOR transition and factor them into their LIBOR transition plans. A summary of key developments follows. The FCA has introduced a dedicated LIBOR webpage that may be useful to private banks when carrying out their LIBOR transition exercises.

European Commission proposes to amend the EU BMR to address LIBOR cessation risks

On 24 July 2020, the European Commission adopted a legislative proposal amending the EU Benchmarks Regulation (EU BMR) to introduce:

- An exemption from the EU BMR requirements for certain third country foreign exchange benchmarks
- The designation of replacement fallback benchmarks for certain benchmarks

The European Commission proposes an exemption from the EU BMR for foreign currency spot exchange rates due to the concerns raised by market participants regarding the unavailability of such rates after the third country transitional period under the EU BMR ends on 1 January 2022. The unavailability of such rates would then impact the ability of market participants to hedge against exposure to foreign exchange rate volatility in currencies that are not readily convertible or subject to exchange controls, by entering into non-deliverable currency forwards and swaps. This exemption would apply to FX benchmarks specifically designated by the European Commission where certain listed criteria are fulfilled.

The proposal provides the European Commission with the power to designate a fallback rate in relation to the cessation of LIBOR — which may be of use in the case of tough legacy contracts.

The European Commission has introduced its second proposal to ensure that when a widely used benchmark is ceasing, and where the cessation of publication of that benchmark may result in significant disruption in the functioning of financial markets in the EU, the European Commission can designate a replacement rate if certain criteria are satisfied. The proposal provides that a replacement benchmark will by operation of law replace all existing references to the benchmark under cessation where:

- Financial instruments, contracts, and performance measures reference the original benchmark when the European Commission formally designates the replacement rate
- Those financial instruments, contracts, or performance measures contain no suitable fallback provisions

The proposal therefore provides the European Commission with the power to designate a fallback rate in relation to the cessation of LIBOR — which may be of use in the case of tough legacy contracts. The European Commission will take into account the recommendations made by dedicated working groups on replacement rates.

Private banks should note that how this proposal will work in practice remains uncertain — including, for example, when a financial instrument will not be considered to contain a suitable fallback provision. It is also uncertain how this proposal fits with the UK legislative proposal, which gives the FCA the power to create a synthetic LIBOR if the FCA announces that LIBOR is no longer representative.

The four to six months ahead are arguably the most critical period in the transition away from LIBOR. The time to act is now. The need to act on LIBOR transition has not been pushed back by the impact of COVID-19.

FCA speech on critical tasks ahead of LIBOR transition

On 3 August 2020, the FCA published a 15 July 2020 speech by Edwin Schooling Latter, FCA Director of Markets and Wholesale Policy, on "LIBOR transition – the critical tasks ahead of us in the second half of 2020".

Key points in the speech include:

- The four to six months ahead are arguably the most critical period in the transition away from LIBOR. The time to act is now. The need to act on LIBOR transition has not been pushed back by the impact of COVID-19
- ISDA is close to finalising the protocol and other documentation through which outstanding derivatives contracts that reference LIBOR can transform, more or less seamlessly, to work on the new risk-free rates (RFRs). Firms will need to sign the protocol within the four-month adherence period that ISDA will offer after the protocol is published this summer
- The FCA welcomes the legislation put forward to give it additional powers to enhance its ability to manage the LIBOR end-game. However, these powers are not an alternative to transition. Firms still need to be ready for life without LIBOR. The FCA will only use its powers in respect of legacy transactions if doing so is necessary to protect consumers or market integrity. And even if doing so would be desirable, the FCA may not always be able to use the powers in all circumstances
- The existence of the powers does not mean that firms do not need the protocol. The FCA may not be comfortable using the powers unless the protocol has been widely taken up because the FCA does not view a synthetic LIBOR as a suitable foundation for derivatives markets, but rather, as a tool to help tackle difficult legacy issues

IBOR Fallbacks Protocol and IBOR Fallbacks Supplement

On 22 September 2020, ISDA published a letter that it sent to the Co-Chairs of the Financial Stability Board (FSB) Official Sector Steering Group (OSSG) regarding the timing of the IBOR Fallbacks Protocol and IBOR Fallbacks Supplement.

ISDA is ready to launch the Protocol and Supplement to implement the new fallbacks for legacy and new derivative contracts.

ISDA is ready to launch the Protocol and Supplement to implement the new fallbacks for legacy and new derivative contracts, respectively. However, ISDA is waiting for the green light from a number of national competition authorities.

ISDA will give market participants approximately two weeks' notice of the official launch date and later effective date, and will during this interim period permit regulated entities and other key market

participants to adhere to the IBOR Fallback Protocol "in escrow" (where they will be complying during the escrow period and their names will be made public upon the effective date). Due to market feedback, ISDA will not provide an effective date in December, and because ISDA has provided for a minimum of three months between the launch and effective date, the effective date will not be before the second half of January 2021.

To the extent that private banks have any derivatives exposure to LIBOR, they should consider their approach to adhering to the ISDA IBOR Fallbacks Protocol and IBOR Fallbacks Supplement.

To the extent that private banks have any derivatives exposure to LIBOR, they should consider their approach to adhering to the ISDA IBOR Fallbacks Protocol and IBOR Fallbacks Supplement and should monitor the date for their publication and entry into force.

FCA Letter on Findings From 2019/20 Review of Firms' Remuneration Policies and Practices

On 22 July 2020, the FCA published a letter, sent to firms' remuneration committee chairs, setting out its findings and observations from the 2019/20 remuneration round and specifying how the FCA plans to assess firms' remuneration policies and practices throughout 2020/21.

During 2019/20, the FCA saw firms continuing to embed conduct in their remuneration policies and practices through performance assessment measures, including outlining conduct objectives and responding to misconduct by adjusting variable remuneration. The FCA also engaged with firms on how remuneration policies can positively influence approaches to diversity and inclusion. The FCA found that firms understand the benefits of a diverse workforce and are moving towards long-term goals.

Private banks are advised that the FCA expects firms to make material progress in achieving those goals to tackle inequalities and create an inclusive environment, including through the actions of the remuneration committee chair.

During 2019/20, the FCA saw firms continuing to embed conduct in their remuneration policies and practices through performance assessment measures, including outlining conduct objectives and responding to misconduct by adjusting variable remuneration.

The FCA letter comments on the following topics:

Accountability: Firms are expected to ensure that their remuneration policies and practices remain aligned with their long-term business plans. The FCA will continue to assess how firms' policies may have evolved in response to the COVID-19 pandemic. Firms will continue to be asked how they have ensured that their remuneration policies reinforce healthy cultures and promote the right behaviours. Firms are expected to consider how their remuneration policies promote equality of opportunity and to ensure that diversity and inclusion is embedded within their approaches to rewarding individuals, avoiding unconscious bias.

Firms should be aware of the risks that may have a negative impact on diverse and inclusive cultures.

Ex-post risk adjustments: The 2019/20 review focused on how firms had responded to major risk and performance issues, including adjustments made to bonus pools and individual remuneration outcomes. The FCA found that some firms were slow in concluding investigations and failed to demonstrate how they aligned levels of adjustment with what they knew about individuals' conduct. Remuneration committee chairs are expected to oversee how their firms make consistent and timely judgments on the level of adjustments made.

Diversity and inclusion: Firms should be aware of the risks that may have a negative impact on diverse and inclusive cultures. Firms should proactively recognise issues that some people may face and aim to can be made by firms proactively recognising issues that some people may face and aiming to take action where possible.
This is the time for firms to push forward with their diversity agenda. Gender and Black, Asian and Minority Ethnic (BAME) pay gaps provide a quantitative window into inequalities, and firms are expected to consider the analysis from those reports and use them to address any inequalities.

Private banks are reminded that FCA supervisors will continue to assess how firms' remuneration policies drive good conduct outcomes and the remuneration committee chair's role in delivering those outcomes.

FCA Dear CEO Letters on Inappropriate Use of Title Transfer Collateral Arrangements and Client Money

On 24 July 2020, the FCA published a Dear CEO letter on "inappropriate use of title transfer collateral arrangements (TTCAs) and regulatory permissions for financing transactions" to firms acting as brokers in wholesale financial markets that currently, or may in the future, offer services (including clearing broker and prime broker services) that involve holding clients' cash or securities as collateral.

The FCA recently identified examples of inappropriate use of TTCAs by firms, amounting to failures of CASS compliance.

The FCA notes that it is common market practice to enter into TTCAs with clients over that collateral, allowing firms to use the cash or securities to secure obligations owed to them by their clients. Outside of such arrangements, cash and securities given to the firm when providing investment services to a client are likely to be client money or custody assets under CASS. In all cases, firms must ensure compliance with any applicable CASS rules, including obligations relating to the use of TTCAs and the correct application of the exclusions in CASS for TTCAs.

The FCA recently identified examples of inappropriate use of TTCAs by firms, amounting to failures of CASS compliance. Additionally, the FCA has seen examples of the same types of firms incorrectly classifying financial transactions as falling within the prudential matched principal exemption and therefore holding lower financial resources than may be required and also acting outside the limitations of their regulatory permissions.

The protection of client money and custody assets is a long-standing priority for the FCA. It is particularly important during the COVID-19 pandemic, given the increased risk of client defaults and firm failures.

Private banks with business models that use TTCAs to hold collateral for leveraged client trading should remember that it is their responsibility to ensure that they have the correct regulatory permissions for the activities they undertake. This includes private banks that are considering whether they can genuinely rely on the matched principal exemption for prudential categorisation purposes.

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Firms were asked to review the use of TTCAs in their business and confirm to the FCA, by 14 August 2020, that the Senior Manager with responsibility for client assets, or alternatively the Senior Manager responsible for compliance, has considered the issues in the appendix to the letter and will bring any issues to the attention of its board. If any rule breaches are identified in relation to a private bank's use of TTCAs or regulatory permissions, they should take immediate steps to rectify those breaches, and the FCA should be notified accordingly.

Dear CEO letter on increased client money balances

On 12 August 2020, the FCA published a Dear CEO letter to firms that provide a non-discretionary investment service. In the letter, the FCA states that it is aware that clients may have rebalanced their portfolios to mitigate volatility during the COVID-19 pandemic. As a result, a number of firms that hold client money have reported an increase in client money balances, and in some cases significantly so, in their reporting from January to June 2020.

The FCA advises that each firm's relevant Senior Manager should consider whether the firm needs to hold client money balances that are unlikely to be reinvested, or whether it would be in its clients' better interests to place those balances directly with their own current or savings account providers.

In the FCA's view, it is good practice at this time for firms to communicate with their clients about increased client money balances to determine whether these should be returned to the clients or whether the firm should hold on to them to facilitate further investment in the short term. If it is in clients' better interests during this time, firms should return client money balances if they are unlikely to be reinvested in the short term. The FCA will continue to review client money balances and follow up with firms that report significantly increased balances.

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The FCA clarified that its letter does not apply to client money balances held within a tax efficient wrapper or under a collateral arrangement for margined transactions.

Conduct: FCA "Messages From the Engine Room"

On 4 September 2020, the FCA published its annual Industry Feedback for 2019/20 in relation to its 5 Conduct Questions Programme.

In 2019, the FCA hosted conduct roundtables with 18 wholesale banks, each of which was represented by a group of staff at the vice president level or equivalent — termed the "Engine Room". The roundtables culminated in the FCA's latest report on the 5 Conduct Questions Programme, "Messages From the Engine Room", which reflects the FCA's findings and perspectives.

The FCA highlights that "Improving clarity [of a firm's purpose] is essential, as these concepts often feature in important conversations both internally and externally with clients and other stakeholders".

The FCA found that identification of conduct risk remains weak, and advised that "an active approach to identifying conduct risk is an essential first step for firms, given that a risk that has not been identified cannot be managed or reduced". However, the FCA applauded the efforts of firms to "raise the profile of non-financial misconduct".

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Previous feedback reports have focused on the importance of "tone from the top" and, more recently, "tone from above". This latest report introduces the notion of "tone from within", calling it "an important new operative phrase to consider when issues of conduct arise". The FCA elaborates: "This represents one's individual mindset, preferences, beliefs, habits and pre-dispositions. It is one thing to have an idea about how your CEO or line manager might respond in a situation, it is another to be clear about how you might respond on your own and why. Whether stated directly or not, the development of Tone from Within via training, self-reflection and self-challenge is a pre-cursor to wider corporate change".

While the FCA observed a "generally positive impact of training rolled out over the past few years … the depth of understanding and the ability to identify conduct risk in day-to-day working life remains unacceptably weak".

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Other findings of interest to private banks include:

- There is a "worrying lack of awareness or depth in the wide range of conduct issues" (beyond the well-understood topics, such as conflicts of interest, inside information, customer fairness, diversity and inclusion, and non-financial misconduct)
- Deeper, wider conduct topics might include: enabling client misbehaviour, failure to train or be trained, glossing over "Know Your Client" gaps, new automation risks (e.g., through use of robots), and remote working risks
- Firms can take further steps to improve employees' ability to identify new sources of conduct risk as they emerge.
- Firms have taken good steps to make conduct risk training engaging through face-to-face delivery and use of real-life scenarios. However, there is often little (if any) meaningful subsequent engagement on the topic
- With regards to remuneration and performance assessments, firms have taken steps to ensure that the contribution of personal conduct and behaviour (the "how") in achieving objectives is a prominent factor alongside "what" is achieved. However, some firms have taken "insufficient steps to ensure substantive feedback discussions with staff, keep future-oriented records, analyse trends and develop a governance feedback loop"
- There is a "persistent and significant lack of psychological safety in day-to-day speak up and challenge" that firms need to address

The FCA also identified some emerging best practices, including:

- Encouraging the active participation of CEOs and other business heads in conduct and culture initiatives
- Offering training sessions, including time for self-reflection
- Providing upfront training to new arrivals before they assume their line roles
- Establishing conduct as a standing agenda item at regular team meetings

For more details, see Latham's *Client Alert* Conduct and Culture Update From the FCA.

Call for Input: Consumer Investments

Reducing harm in the consumer investment market was identified as a business priority in the FCA's 2020/21 Business Plan. On 15 September 2020, the FCA issued a Call for Input to look across the whole market and consider whether there are systemic issues that need to be fixed. The FCA highlights that "a well-functioning market channels money to companies looking to grow and innovate, supporting the UK economy which will be even more important as the UK recovers from the economic effects of the COVID-19 pandemic". The Call for Input applies to a wide range of consumers, firms, and other interested parties, including private banks.

Private banks should note that while much of the consumer investment market meets the goals of retail investors, the FCA thinks that there are some areas of the market that are not working well enough for consumers. Regulating this market will need to balance a consumer's freedom to choose with the need to protect consumers from harm, and to foster the innovation and competition that new entrants bring with the need to stop "bad actors" from thriving.

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The Call for Input focuses on the following key areas:

Making the mass market work well

The FCA asks what it can do to help the market offer a range of products and services that meet straightforward investment needs. In particular, the FCA seeks views on the barriers to firms providing simple investment advice models and simple investment products for consumers.

Higher-risk investments

The FCA asks how it can better ensure that those who have the financial resources to accept higher investment risk can do so if they choose, while understanding the risks they are taking. The FCA also seeks views on the role of the exemptions in the financial promotions regime, in particular how the high-net-worth and self-certified sophisticated investor exemptions are working in practice and the level they are set at.

Regulatory protections

The FCA asks how it can make it easier for people to understand the risks of investment and the level of regulatory protection afforded to them when they invest.

Fair compensation

The FCA asks what more it can do to ensure appropriate compensation for consumers who lose money because of an act or omission of a regulated firm. The FCA is considering how firms that cause harm can pay more redress before recourse is needed to the Financial Services Compensation Scheme (FSCS). It does not intend to conduct another review of the funding of the FSCS. The FCA also seeks views on how the appointed representative regime is operating in practice.

Tackling scams

The FCA asks how people can be better protected from scams.

Competition and innovation

The FCA asks what more it can do to facilitate effective competition and encourage firms to develop innovative products and services that help consumers to invest.

The deadline for responses to the Call for Input is 15 December 2020. The FCA will use the feedback to shape its work over the next three years, and will share with the UK government any views or insights on relevant matters.

Enforcement: FCA Publishes Final Notice Against Former WorldSpreads CEO for Market Misconduct

On 9 September 2020, the FCA published a Final Notice in respect of Conor Foley, the former CEO of WorldSpreads, imposing a public censure pursuant to section 123(3) of FSMA for engaging in market abuse (dissemination, manipulating transactions, and false or misleading impressions). The FCA replaced the financial penalty of £658,900 proposed in the Decision Notice, because the former CEO had provided verifiable evidence that the imposition of a financial penalty of any amount would cause him serious financial hardship. The FCA also made a prohibition order, pursuant to section 56 of FSMA, as proposed in the Decision Notice, banning Mr Foley from performing any function in relation to any regulated activities carried on by an authorised or exempt person, or exempt professional firm. The Final Notice outlines the reasons for the FCA's actions.

Mr Foley, the former CEO of WorldSpreads Limited (WSL) and its holding company WorldSpreads Group plc (WSG), was involved in drafting admission documentation ahead of WSG's flotation on AIM in August 2007. These documents contained misleading information and omitted key information that investors would have needed to make an informed decision about the company. In particular, the documentation did not mention that some WSG executives had made significant loans to WSG and its subsidiaries. This fact was also never disclosed in the annual company accounts. Nor did the documentation mention an internal hedging strategy by which some WSG subsidiaries hedged considerable trading exposures internally with company executives. This fact was not disclosed in the annual accounts until at least 2009.

Between January 2010 and March 2012, large spread bets were placed on the shares of WSG on the trading accounts of WSL clients on terms that made statements in WSG's annual accounts as to its credit policy false and misleading. In addition, large spread bets were carried out on two clients' accounts by Mr Foley himself without the knowledge of the clients. This had the effect of giving the appearance of greater demand for WSG shares than in fact existed.

Mr Foley is the third and last executive of WSL against whom the FCA has taken action following its collapse in March 2012. The FCA fined and banned WSL's CFO, Niall O'Kelly, and its Financial Controller, Lukhvir Thind, in April 2017 for falsifying critical financial information concerning WSL's client liabilities and cash position, which was passed to the company's auditors. By 31 March 2011, these misstatements amounted to £15.9 million. WSL was unable to meet this client money liability, which ultimately led to its collapse.

BEIS Response Paper to the Smart Data Consultation

On 9 September 2020, the Department for Business, Energy and Industrial Strategy (BEIS) published its response to the consultation on proposals following its Smart Data Review in June 2019.

BEIS confirmed in its response that respondents were in favour of extending Smart Data to other sectors beyond banking, including the technology, energy, communications, and financial sectors as well as charities and academia. Respondents also:

- Supported a new Open Communications initiative (adding to the initiatives developing in energy, finance, and pensions). Some advocated for Smart Data in education, retail, transport, and health. Since the Smart Data Review, Ofcom has launched work on the Open Communications initiative, with a consultation due to close in November 2020
- Favoured legislation to mandate industry involvement in Smart Data initiatives (though some respondents wanted to allow more time for voluntary involvement)
- Agreed the UK government should increase coordination across sectors. Respondents said coordination should be flexible to sector-specific needs and clear on the role of sector regulators, any cross-sector bodies (such as the Smart Data Function proposed in the Smart Data Review), and organisations (such as the Information European Commissioner's Office)
- Raised detailed points about oversight and regulation of Smart Data initiatives and the firms involved, including comments on how schemes should be funded
- Welcomed the Smart Data Review's emphasis on making sure that Smart Data benefits vulnerable consumers

BEIS confirmed in its response that respondents were in favour of extending Smart Data to other sectors beyond banking, including the technology, energy, communications, and financial sectors as well as charities and academia.

Additionally, BEIS announced the next steps on cross-sector smart data work, including:

- Primary legislation, when parliamentary time allows, that extends the government's powers to mandate participation in smart data initiatives
- A cross-sector smart data working group to coordinate and accelerate existing smart data initiatives across regulators and government, focusing initially on communications, energy and finance to inform the development of high-quality standards, and to include detailed consideration of how schemes should be coordinated and regulated in the long term, as well as how they can best benefit vulnerable consumers

BEIS also published terms of reference for the smart data working group and an impact assessment for the proposed legislation.

ESMA's Recommendations on the AIFMD Review

ESMA has written a letter to the European Commission highlighting areas ESMA would like considering during the forthcoming review of the AIFMD. Annex I to the letter sets out the key issues in the legislative framework for which ESMA recommends revisions, and Annex II sets out the key reporting issues that could be improved. Many of the recommendations also require consideration of changes to the UCITS legislative framework. ESMA's letter includes recommendations for changes in 19 areas of the AIFMD, including:

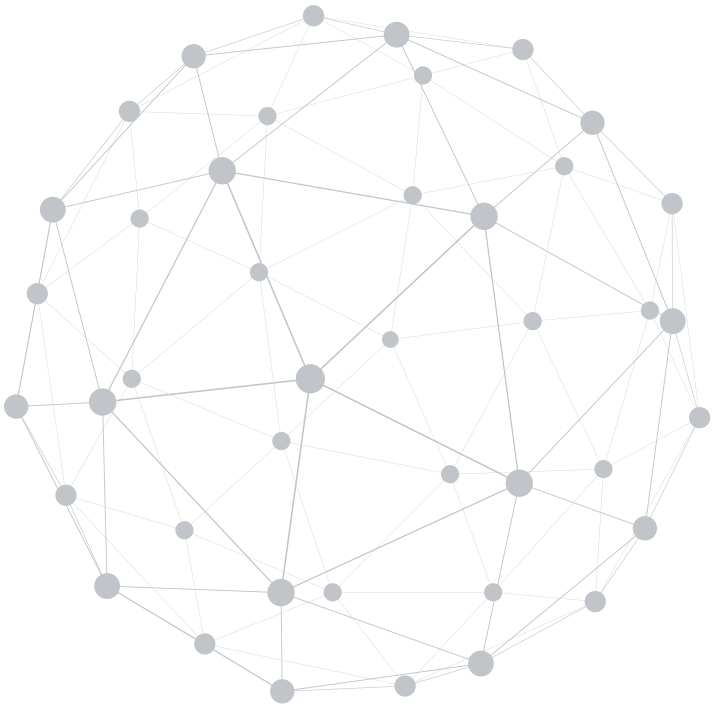
- Harmonising the AIFMD and UCITS regimes, in particular with regards to risk management and liquidity management requirements and in the field of reporting
- Clarifying the scope of additional MiFID services and the application of the rules, including the provision of greater regulatory consistency between AIFMD/UCITS and MiFID, in order to ensure that entities providing similar types of services are subject to similar regulatory standards
- Clarifying the delegation and substance requirements, including on the maximum extent of delegation
- Providing further detail on reverse solicitation
- Making available all additional liquidity management tools in all jurisdictions in a consistent manner
- Amending the current reporting of the gross method calculation for assessing leverage in investment funds to ensure alignment with the IOSCO framework
- Addressing issues regarding the AIFMD reporting regime and data use
- Harmonising the supervision of cross-border entities, including clarifying the supervision of cross-border activities and branches

The letter gives the impression that ESMA is of the view that a number of the areas of the AIFMD permit arrangements (such as delegation and secondments) allowing market participants to avoid the application of certain rules. Further, especially with Brexit in mind, the letter seems to suggest that these areas should be tightened up to bring more of those people and entities that currently sit outside the scope of the AIFMD within its reach.

The review of the AIFMD provides the EU with an opportunity to improve many areas of the existing framework based on national competent authorities' practical experience in supervising firms in accordance with the rules since the AIFMD was published.

We expect the European Commission to publish its review in the middle of 2021, with any legislative proposals for changes to the AIFMD to follow.

TechTrends: European Commission Publishes Comprehensive Proposal for a Markets in Cryptoassets Regulation



The European Commission has published a proposal for a wide-ranging EU regulation covering cryptoassets and e-money tokens, both of which are currently largely unaddressed in EU financial services legislation.

MiCA creates a new EU-wide licensing regime for cryptoasset issuers and service providers along with substantive conduct of business and consumer protection requirements.

The draft Markets in Cryptoassets Regulation (MiCA) has been designed to:

- Increase legal certainty in the area of cryptoassets
- Support innovation and promote the development of cryptoassets and the wider use of distributed ledger technology (DLT)
- Instil appropriate levels of consumer and investor protection and market integrity in an area that presents many of the same risks as traditional financial instruments
- Ensure financial stability

MiCA creates a new EU-wide licensing regime for cryptoasset issuers and service providers along with substantive conduct of business and consumer protection requirements. MiCA also introduces a new EU-wide passport that is available to market participants who become licensed under the MiCA regime in their home member state. While the details on how MiCA will be applied have not yet been published and may take one to two years, it is clear that the European Commission has drafted an ambitious, full-scope regulatory regime for cryptoassets that should create a significant amount of certainty for issuers and service providers of cryptoassets.

The proposal is part of the EU Digital Finance package, a set of measures designed to make the EU fit for the digital age and to further enable and support the potential of digital finance in terms of innovation and competition while mitigating the risks involved. In addition to the proposal for MiCA, the package also includes a proposal for a pilot regime on DLT market infrastructures, a proposal for digital operational resilience, and a proposal to clarify or amend certain related EU financial services rules. These complementary proposals are intended to address clear obstacles to the use of DLT in the financial sector and to allow for experimentation for market infrastructures within a safe environment with the aim of exploring the need for possible further developments in this area.

The European Commission is concerned that the legal framework applying to issuers of cryptoassets and cryptoasset service providers has become fragmented across the EU.

The European Commission is concerned that the legal framework applying to issuers of cryptoassets and cryptoasset service providers has become fragmented across the EU, noting that key objectives such as ensuring investor protection, market integrity, and financial stability cannot be sufficiently achieved by EU member states acting alone. The European Commission writes in its proposal that these objectives can be better achieved by creating a framework on which a larger cross-border market for cryptoassets and cryptoasset service providers could develop.

Given that a lack of legal certainty has been a significant anchor on the development of the cryptocurrency market in the EU and globally, MiCA should foster growth of the EU markets in cryptoassets, paving the way for newly regulated businesses to achieve legitimacy within the arena of financial services providers, thereby encouraging greater institutional investment and participation in this space.

MiCA has been designed to interplay with existing EU financial services legislation and authorisation requirements meaning that many of the requirements it imposes on cryptoasset issuers and service providers will be familiar to legal and compliance professionals in traditional financial services, although adapted to meet the idiosyncracies of this new technology.

For more details, see Latham's blog post MiCA: EU Commission Publishes Comprehensive Cryptoasset Market Regulation Proposal.

Global Insights — US

SEC Flags Deficiencies in Private Fund Adviser Compliance

On 23 June 2020, the Securities and Exchange Commission's (SEC's) Office of Compliance Inspections and Examinations (OCIE) published a Risk Alert describing various compliance deficiencies observed in recent examinations of registered investment advisers that manage private equity funds or hedge funds. OCIE highlighted compliance deficiencies in three areas, aligned with the areas of concern for private funds previously noted by OCIE in its 2020 Examination Priorities: (1) conflicts of interest; (2) fees and expenses; and (3) controls related to material non-public information (MNPI).

The Risk Alert, although not exhaustive, is a timely reminder to private fund advisers regarding common areas of supervisory deficiency. It reinforces the need to address certain compliance fundamentals, such as implementation of adequate written policies and procedures. Private fund advisers should use the findings in the Risk Alert, in conjunction with self-audits and internal compliance reviews, to gauge the strength of their risk management programs and their overall alignment with regulatory expectations.

Notably, the issues highlighted in the Risk Alert are not unique to US advisers. Regulators in other jurisdictions, such as the FCA, might be concerned to observe any such issues involving advisers or managers falling within their jurisdiction.

The Risk Alert provides a useful framework against which all private fund managers and advisers can self-assess and benchmark against good industry practice.

For more details, see Latham's *Client Alert* SEC Flags Deficiencies in Private Fund Adviser Compliance.

What to Look Out for in Q4 2020

- Onshoring – End of the Brexit transition period on 31 December 2020
- Policy statement due on extension of the SMCR implementation period
- Planned second PRA consultation on the transposition of CRD V
- ESMA expected to report on various aspects of the MiFID II review
- HM Treasury to publish more information on the UK BMR and PRIIPs regime in the UK
- Consultation closes on the regulatory framework for approval of financial promotions

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