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19 April 2023

Financial Regulation Monthly Breakfast Seminar

Overview

-
- FCA's Business Plan 2023/24
 - Edinburgh Reforms - the SMCR Review
 - The PRA's latest Senior Manager enforcement case
 - Investment Research – International Developments
 - HM Treasury's proposals to regulate ESG ratings providers
 - Other recent ESG developments



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FCA's Business Plan 2023/24
Rob Moulton

Strategic themes

- Three key strategic themes
 - Protecting consumers
 - Enhancing market integrity
 - Promoting competition in the interests of consumers
- New secondary objective to facilitate the international competitiveness of the UK economy and its growth in the medium to long term – FCA will “fully embrace this secondary objective as already significantly in line with our approach”
- Past years have seen record levels of volatility
 - Expect economic and geopolitical environment to remain highly uncertain
 - Reference to recent bank collapses and rescues

FCA's focus for 2023/24

- Our people
 - Head count expanded by approximately 500 in 2022
 - Authorisations Division
 - Enforcement and Market Oversight Division
 - Further increases in 2023 focused on Future Regulatory Framework (“a very significant programme of work”) and data analytics
- Our locations
- Only sectoral focuses highlighted are:
 - Crypto assets
 - BNPL

Setting and testing higher standards

- Major initiative in “putting consumers’ needs first” is the Consumer Duty
 - Follow-on sector-specific supervisory work
 - Linked to other topics in progress, such as vulnerability, BNPL, fair value
- Helping consumers to help themselves
 - Crypto assets
 - Gateway for firms that want to approve financial promotions
 - Initiative relating to “influencers”

Fin-fluencing? Get it right.

Got an opportunity to promote a financial product to your followers?



Did you know that the Financial Conduct Authority (FCA) polices the promotion of MOST financial products and services?

You could be on the wrong side of the law if you promote without cluing yourself up first.

Could you be providing financial product advice or arranging for your followers to deal in a financial product?

Making an unlawful financial promotion is a criminal offence that carries a maximum sentence of 2 years imprisonment and an unlimited fine.



3 Are you aware that the Advertising Standards Authority (ASA) regulates the promotion of other financial products, including cryptocurrency, fan tokens and NFTs, and ensures that all ads are responsible? If your post breaks the rules, the ASA will take action.

Are your posts responsible?

4 Are you the right person to be promoting financial services and products? You have an obligation to your followers and they rely on what you post. Don't assume that they fully understand what you are promoting or that it's in their best interests to follow your guidance.

5 Do you know that the FCA does not currently regulate firms offering direct investments in cryptocurrency or NFTs? If anything goes wrong with these products your followers could lose all their money. The FCA will soon start policing the promotion of cryptocurrencies too – watch this space.

6 Is the company whose services you are promoting legitimate? Investment scams are on the rise and you may be unknowingly introducing your followers to criminals. If you are unsure, search 'ScamSmart'.



Is it clear which of your posts are ads?

You must label your content as an ad upfront if you get any form of payment (not just financial) from the brand, including affiliate links. Make sure you're working with a brand that knows the rules.

Get it right – The checklist for responsible financial promotions

The FCA and ASA monitor content online and will take action against those not following the rules. This checklist will help you get it right.

- Are you providing advice about a financial product?
- Are you authorised by the FCA or has your post been approved by an FCA authorised person?
Seek legal advice if you are unsure.
- Have you or your agent done your due diligence?
- Does your post follow the ASA rules?
Is it legal, truthful, responsible and correctly labelled as an ad?
- Promoting crypto? You must make it clear to your followers:
 - that cryptocurrency is unregulated;
 - profits may be subject to tax; and
 - the value of any investment could fall.
- Don't suggest to your followers that cryptoassets would be an easy investment decision or create any sense of urgency or FOMO.

If in doubt, don't promote.

Disclaimer – This publication provides a summary of basic information. It does not cover all of the relevant law and is not a substitute for professional legal advice.



Strategy for positive change: ESG priorities

- Continues to be a major initiative, including working with the newly formed ESG Advisory Committee to the Board of FCA
 - Changes to listing rules to reference final ISSB standards once IOSCO has endorsed them
 - Feedback Statement to ESG governance Discussion Paper
 - Final rules on Sustainability Disclosure Requirements and investment labels
 - Published FCA's own net-zero transition plan
 - Actively monitor how effectively firms and listed companies are implementing disclosure rules
 - Be a thought-leader internationally
 - Further work to improve D&I transparency

Promoting competition

- Future Regulatory Framework
 - Orderly replacement of retained EU law, becoming Handbook rules but tailored to UK markets
- Updating Regulatory Framework
 - Conclude Listing Regime Review
 - New rules on transparency for equity markets, tick sizes, waivers and trade reporting
 - New guidance on trading venue perimeter
 - Consultation on consolidated tape
 - Consultation on commodity position limits regime
 - Amendments to UK EMIR reporting
 - Complete Wholesale Data Market Study on pricing and competition in supply of benchmarks and credit ratings



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Edinburgh Reforms - the SMCR Review
Jonathan Ritson-Candler

The Edinburgh Reforms – reform of SMCR?

- Under the banner of one of The Edinburgh Reforms’ stated goals – to ensure the UK is a “*competitive marketplace promoting effective use of capital*” – the government stated it was “*commencing a review into **reforming** the SMCR in Q1 2023*”
- Led to speculation that the SMCR could be substantively reformed or material aspects rolled back
- On 30 March 2023 the following papers were published seeking feedback on the SMCR:
 - the PRA and the FCA published a joint [Discussion Paper](#) (FCA DP23/3 and PRA DP1/23); and
 - HM Treasury published a [Call for Evidence](#)
- Deadline for responses to both papers is 1 June 2023

An information gathering process

- Both papers read as the first step in an information gathering process and are both written from the perspective that in the main, the feedback received from industry and other regulators to date is that SMCR is functioning well and is not having material unintended consequences (albeit the regulators are interested to know if that's not the case)
- The tone of the papers suggests that the government is not minded to fundamentally change or row back on SMCR
- The regulators and the government consider that the SMCR has driven positive behavioural changes in the financial services sector. This is interesting given that one of the key aims of the regime was to increase individual accountability when things go wrong within a firm, but this has not led to much successful enforcement action

Review (and possibly some minor tweaks) rather than reform

- The papers do not, at present, consult on specific proposals or changes. However, common to both papers is a suggestion that the following are aspects they imagine stakeholders will have views on:
 1. Delays in getting senior managers approved (albeit both papers refer to timelines having recently significantly improved, with particular efforts having been made by the FCA to reduce the backlog of applications)
 2. Challenges faced by firms when:
 - a) completing regulatory references; and
 - b) submitting conduct rule notifications,
 3. How SMCR applies to different types of firm
 4. The growth in new expectations on senior managers in respect of new and emerging risks
 5. The frequency with which firms must submit SMCR-related information to the regulator(s)

Review (and possibly some minor tweaks) rather than reform

- Interestingly, the papers also focus on how the SMCR affects the UK's international competitiveness — a nod to the regulators' new secondary objective of competitiveness and growth that has been included in the Financial Services and Markets Bill
- Overall, it seems that the review may be less fundamental than firms might have expected
- While firms do generally agree with the SMCR's overarching aims, day-to-day compliance can be challenging and firms will doubtless have various aspects of the Regime that they would like improved. It will be interesting to see how the regulators and the government choose to address the feedback they receive



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The PRA's latest Senior Manager enforcement case
Neil Perks

Background

- PRA fined the former CIO of TSB (and holder of SMF18 responsibility) £81,620
- Breach of PRA SM Conduct Rule 2 - *You must take reasonable steps to ensure that the business of the firm for which you are responsible complies with the relevant requirements and standards of the regulatory system*
- Failed to take reasonable steps to ensure that TSB adequately managed and supervised its outsourcing arrangement in relation to its 2018 IT migration programme

Statement of Responsibilities

- Responsibility for TSB's IT function and IT Business Continuity Planning
 - Providing leadership and strategic direction to IT function
 - Designing and managing Migration Programme
 - Accountable for IT to deliver TSB's strategic goals
- Migration Programme
 - Accountable for building and effective implementation
 - Responsible for relationship with SABIS (PRA's Outsourcing Rules)
 - Accountable for migration governance, communication, and decision-making process
 - Owner of material risk of operational resilience issues and poor customer outcomes caused by the migration

Failings

- Failed to take reasonable steps to ensure that TSB complied with the PRA's Outsourcing Rules
 - Did not obtain sufficient assurance from SABIS, particularly regarding fourth parties
 - Did not annex SABIS' letter of confirmation to CIO attestation
 - Over-reliant on the SABIS confirmation
 - Did not ensure that TSB reassessed SABIS' capabilities on an ongoing basis
 - Did not take a holistic view of the risks of the outsourcing arrangement
- Undermined operational resilience and contributed to significant disruption

Points to note

- No consideration of personal culpability
- Intragroup services and outsourcing arrangements must comply with PRA's Outsourcing Rules
- Attestations/Assurances must be appropriately supported by the material on which they are based
- Reasonable steps may involve senior managers further investigating and challenging the information on which they rely
- Engaged and proactive approach required for oversight of service provider's management of fourth parties



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Investment Research – International Developments
Rob Moulton

Research - UK

- Review launched 9 March 2023, due to report by 13 June 2023
- Focus on whether research unbundling rules damage levels of research and UK competitiveness
- Comparison against rules in other “major international financial services centres”
- Consider level of demand, as well as supply
- Reconsider UK 2022 rule revisions
- All options are on the table

Research - EU

- Ongoing MiFID quick fix amendments
 - Focus on size of company involved – above €10 billion
 - Also potential action to permit research to be provided if bundling required by overseas jurisdictions
- Further Swedish presidency-led proposals, including
 - Scrapping the regime entirely
 - Providing further clarity for non-research content
- All options appear to be on the table

Research - US

- No Action Letter expiry 3 July 2023
- No indication of movement from SEC

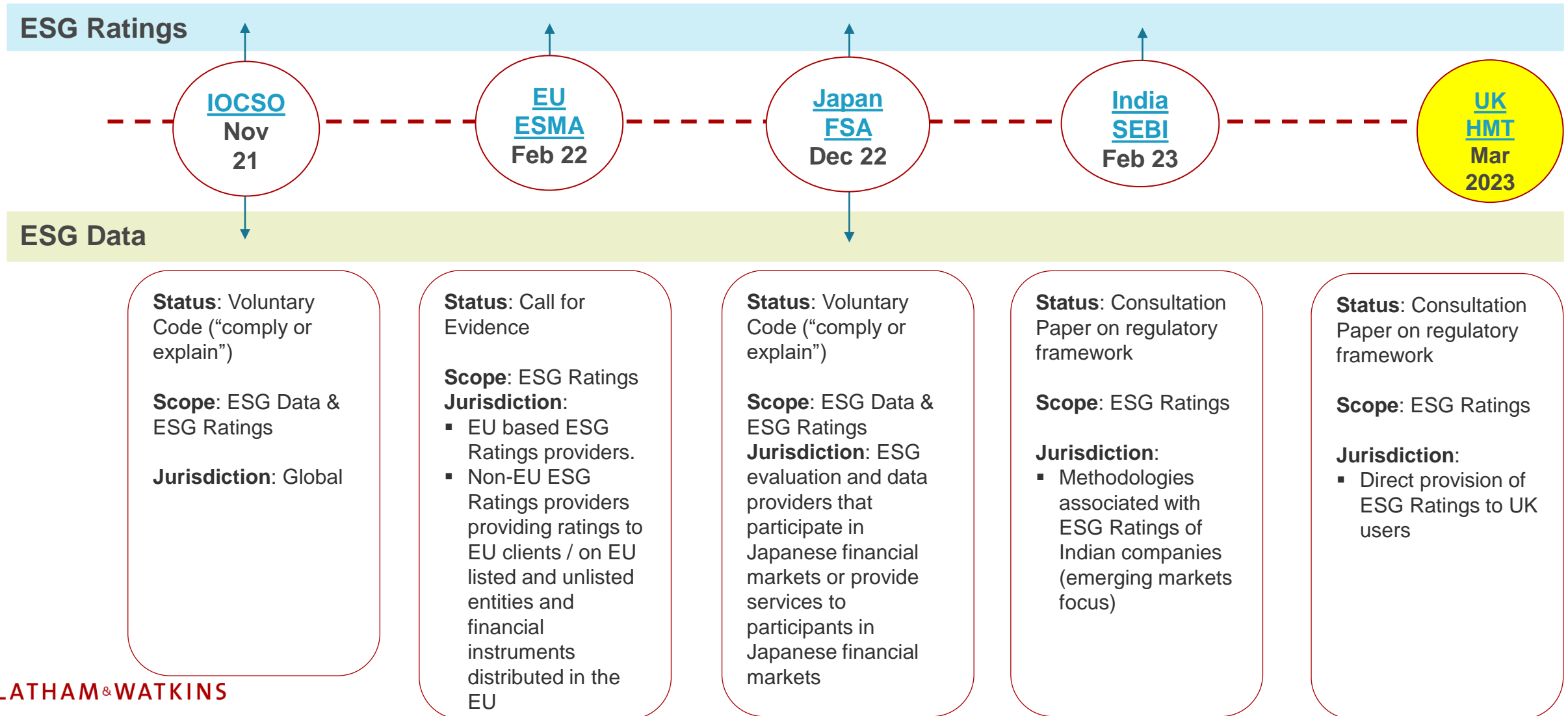


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HM Treasury's proposals to regulate ESG ratings
providers
Nicola Higgs

Global Perspective: ESG Ratings & Data

International momentum to regulate ESG ratings / data



UK HMT Consultation

Future regulatory regime for ESG ratings providers

- 30 March 2023: HMT consultation published
 - Consultation closes 30 June 2023
 - Final legislation before Parliament later this year
- Will be a further FCA consultation
- What is an ESG rating?
 - Assessment of the ESG characteristics of entities, sovereigns or products
 - Assessment = evaluation or value judgement
 - Includes ESG assessments directly produced by analysts in addition to algorithms
 - Different to ESG data which is ESG data on entities, sovereigns or products, with no final assessment or value judgement

Future regulatory regime for ESG ratings providers

- Purpose of the consultation
 - To bring ESG ratings providers inside the scope of the UK regulatory perimeter through amendments to FSMA / RAO
 - Once in scope, it is anticipated FCA will separately consult on the appropriate conduct regime with respect to ratings methodologies (but stopping short of harmonising the varying methodologies and objectives of ESG ratings)
 - Assumption is that IOSCO voluntary code will be baked into FCA rules
 - HMT is also considering overlap with BMR

Future regulatory regime for ESG ratings providers

- Proposed scope
 - The direct provision of an assessment of E, S or G factors to a user in the UK in relation to a RAO specified investment
 - The concept is tied to use in financial markets – does the rating influence capital allocation? (e.g. rating a pre-IPO company)
 - Extraterritorial impact where ESG ratings are provided directly to UK users
 - Direct provision = where an ESG rating is provided to a UK user (e.g. in return for a fee or bundled with other products / services)
 - ESG ratings made freely available which UK users can access (without direct provision) would not be caught

Future regulatory regime for ESG ratings providers

- Out of scope:
 - ESG ratings produced by charities / non-profits (does not satisfy the “by way of business” test)
 - ESG ratings produced purely for internal purposes (e.g. asset managers running proprietary ESG ratings on companies to inform investment decisions)
 - Investment research products (e.g. equity research reports which incorporate ESG considerations but which are not standalone ratings)
 - External reviews (e.g. second party opinions, verifications and certifications of company ESG disclosures / green bond standards)
 - Proxy advisor services (e.g. voting or recommendations to shareholders with respect to company ESG performance)
 - Consulting services (e.g. ad hoc or bespoke reviews which do not systemically influence capital allocation)
 - Academic research or journalism

Regulatory Strategy: ESG Ratings & Data

Questions to consider...

- Which global reform will impact us?
- Do we have a clear understanding of “ESG Rating” and “ESG Data”?
- Do we need to enhance our disclosures in relation to certain products / services?
- What questions can we anticipate from stakeholders?
- Should we be asking questions of our ESG data providers?



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Other recent ESG developments
Nicola Higgs and Ella McGinn

Primary Markets Bulletin 44

Diversity and inclusion on company boards and executive management

- FCA has issued additional guidance on the new Listing Rules on disclosure of D&I data in Annual Reports.
- Companies in scope of the new Listing Rules =
 - Equity listings: UK and overseas issuers with equity shares, or certificates representing equity shares, admitted to the premium or standard segment of the FCA's Official List, excluding open-ended investment companies and shell companies, but including closed-ended investment funds and sovereign controlled companies
 - Not in scope: Issuers of listed debt and debt-like securities, securitised derivatives, or miscellaneous securities

Primary Markets Bulletin 44

Diversity and inclusion on company boards and executive management

- The first annual financial reports including disclosures subject to this rule will be published from April 2023. Failing to publish in the Annual Report will trigger a requirement to publish via RIS

WARNING: Non-compliance will be viewed seriously and will lead to action. In addition to considering LR and DTR compliance, FCA will consider disclosures identified as containing potentially false or misleading information, including the omission of material facts, likely to cause investor harm or which may breach other relevant FCA rules for ESG matters (see TN 801.2)

Update: UK ESG developments

- FCA Sustainability Disclosure Requirements (SDR)
 - Policy Statement now due in Q3 23
 - Proposed effective dates will be adjusted accordingly
- UK Government has published an updated Green Finance Strategy
 - UK Green Taxonomy due Autumn 2023
 - UK will also be reviewing the final ISSB Standards (due Jun 23) and TNFD (due Sep 23) to determine whether and how to align with UK policy
 - Call for Evidence on Scope 3 emissions in Q3 2023
 - FRC will review Stewardship Code in Q4 2023 (inc. reviewing fiduciary guidance)

ESG Benchmarks: FCA Dear CEO Letter

- On 20 March 2023 FCA issued a Dear CEO letter addressed to **benchmark administrators** following a preliminary review of a sample of **UK ESG benchmarks**
- FCA has expressed several concerns relating to:
 - The poor quality of benchmark administrators' ESG-related disclosures
 - Incorrect implementation of ESG benchmarks' methodologies
- Inadequate disclosures could lead to greenwashing and dilute trust in ESG labelling
- The FCA warned it **will use its supervisory and enforcement powers** against firms that do not address the areas of concern it raised

ESG Benchmarks: FCA Dear CEO Letter

- In particular, the FCA is concerned about:
 - Lack of details in benchmark statements on how ESG factors considered in benchmark methodologies
 - Insufficient explanation in benchmark statements on how ESG factors are reflected against each of the requirements in the UK Benchmarks Regulation
 - Lack of specific descriptions of the market or economic reality measured by benchmarks, particularly in benchmark statements for families that covered a broad range of benchmarks
 - Where additional information is made available in other documents, links to such materials are not clearly sign-posted or easily accessible to users
 - Lack of explanations on why broader ESG metrics factoring in social and governance factors are appropriate where the benchmark purports to have climate objectives only

ESG Benchmarks: FCA Dear CEO Letter

- In particular, the FCA is concerned about (cont.)
 - Underlying methodologies for ESG data and ratings products used in ESG benchmarks not being accessible, clearly presented and explained to users
 - Insufficient information on the data and standards used to calculate the weighted average scores for the ESG factors, such as descriptions of the data sources and the extent to which they are estimated or reported
 - Failure to disclose average weighted scores against all the mandatory ESG factors in Annex II of the UK Low Carbon Benchmarks Regulation
 - Failure to state which factors are being applied to which benchmarks, and whether used to select, exclude or weight constituents
 - Miscalculation in benchmarks due to the incorrect application of ESG factors
 - Lack of controls to verify that ESG factors or methodologies had been correctly applied in ESG benchmarks

ESG Benchmarks: FCA Dear CEO Letter

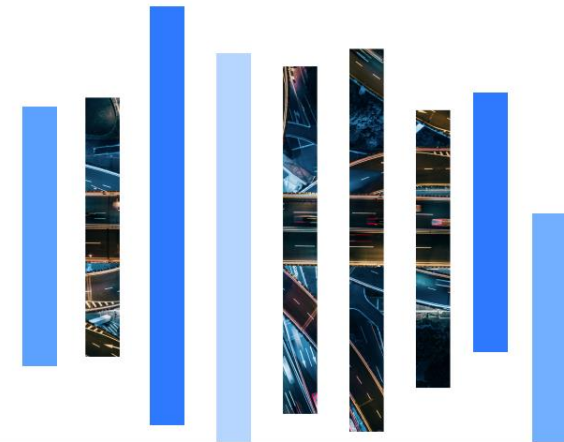
- The letter takes a **heavily critical tone** and may be seen as a **final warning** about the issues raised
- Firms should **engage senior leadership** to determine what strategies should be implemented to address the FCA's concerns and be prepared to explain these strategies to the FCA on request
- Proposed regulation of ESG ratings providers could change the current landscape significantly and presumably provide a more structured framework for benchmark administrators seeking data for their ESG benchmarks

Whistleblow Insights: Recurrent Themes and Common Drivers



With a marked recent increase in the number of whistleblows across the financial services sector, this guide highlights recurrent themes and common drivers, and poses gently provocative self-assessment questions against which firms can usefully benchmark themselves.

[Please click here to read the full publication.](#)



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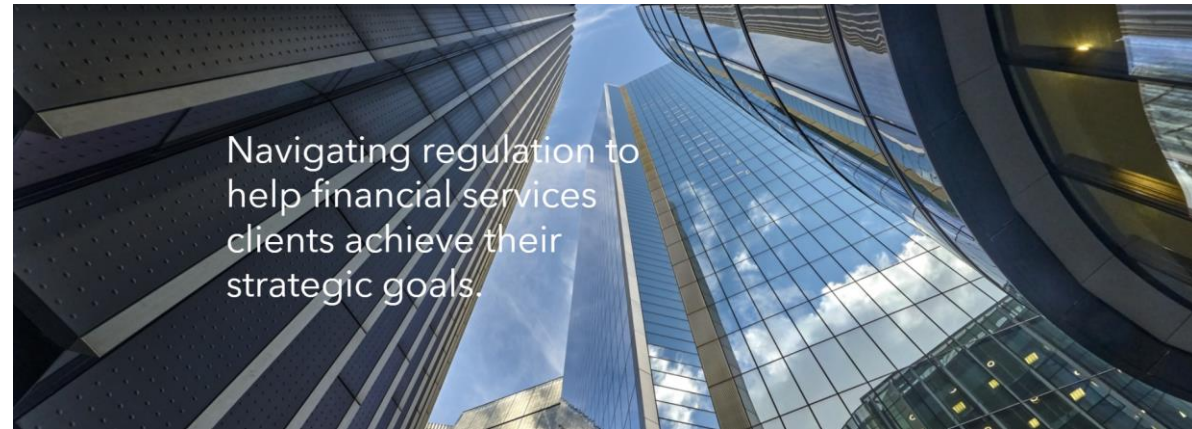
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[UK Government and Regulators Launch SMCR Review](#)

[UK Government Kicks Off Investment Research Review](#)

[Focus on Greenwashing: The Latest Regulatory Proposals in the EU and the UK](#)

[UK Government Consults on Regulation of ESG Ratings Providers](#)

[FCA Seeks Improvements to ESG Benchmarks](#)

[FCA to Unveil Blueprint for Reforms to the Listing Regime](#)

