



LATHAM & WATKINS

8 February 2023

# Financial Regulation Monthly Breakfast Seminar

# Overview



A blue-toned background featuring a financial line chart with multiple data series and a grid. The chart shows various trends, including a sharp decline followed by a recovery and another decline. The overall aesthetic is professional and data-driven.

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Consumer Duty: latest FCA developments and  
market colour  
Becky Critchley and Ella McGinn

# Consumer Duty: timing recap



# Consumer Duty: latest from the FCA

- [Dear CEO letters](#) - 3 February 2023
- [FCA Multi-firm review findings](#) - 25 January 2023
- Podcasts:
  - [Explaining the Consumer Duty consumer understanding outcome](#) – 27 January 2023
  - [Understanding the Consumer Duty products and services outcome](#) – 17 January 2023
  - [What is the price and value outcome?](#) – 06 January 2023



# Dear CEO letters

<b>PUBLISHED 3 FEBRUARY 2023</b>	<b>TO BE PUBLISHED 'SHORTLY'</b>
Asset Management, Custody & Fund Services and Alternatives	Credit Unions
Consumer investments	Debt advice firms
Credit reference agencies and providers of credit information services	Debt purchasers, debt collectors and debt administrators
General Insurance and pure protection firms	Mortgage Intermediaries
Life insurance	Motor Finance providers
Mainstream consumer credit lenders	Payments Services and E-Money
Mortgage lenders and administrators	Retail Finance providers
Retail banks and building societies	Credit brokers

# Dear CEO letters - thematic

- Senior management to consider the contents of the letter (could be several!)
- The areas highlighted in the letters are likely to be the primary focus of future FCA supervisory work
- Consumer Duty as not simply a change to governance and processes
- Not enough to avoid bad outcomes
- Firms will need to pay as much attention to good consumer outcomes as they would to any other significant aspects of their business

# Dear CEO letters - thematic

- Cost of living crisis
- Enabling consumers to make informed, effective decisions, act in their interests and pursue their financial objectives
- *“A key part of the Duty is that firms are able to define, monitor, evidence and stand behind the outcomes their customers are experiencing”*
- Consumer Duty is not retrospective
- Employee remuneration structures



# Dear CEO Letters – consumer investments

- Four areas where particular focus is needed:
  - Mainstream investments
  - Higher risk investments
  - Scams and fraud
  - Consumer redress
- Appointed Representatives
- Scoping of services as well as products

# Dear CEO Letters – consumer investments

## Consumer Duty doesn't:

Protect insistent customers from making poor decisions or acting in away that a firm might consider to be against their interests

Mean consumers can or will be protected from all harm

Create a fiduciary relationship where one doesn't already exist

Go beyond the scope of a firm's regulatory requirements (e.g. require a firm to provide advice without permission to do so)

Apply retrospectively to actions by firms before the Duty came into force

## Consumer Duty does require firms to:

Pro-actively act to deliver good outcomes for customers generally and put customers' interests at the heart of their activities

Focus on the outcomes customers get, and act in a way that reflects how consumers actually behave and transact in the real world

Ensure they have sufficient understanding of customer behaviour and how products and services function

Where they identify that good outcomes are not being achieved, act to address this

Consistently and regularly challenge themselves to ensure their actions are compatible with delivering good outcomes for customers

# Dear CEO Letters – Asset Management, Custody & Fund Services and Alternatives

- For each portfolio type the FCA will have a different Consumer Duty ‘strategy’
- Interaction with the Asset Management Market Study
- Concept of being able to ‘determine or materially influence retail customer outcomes’ is particularly relevant:
  - Can the firm ‘make or influence decisions’?
  - Is there discretion over customer outcomes?
  - Shared responsibility, how to apportion which firm does what?
- Application to high net worth and sophisticated customers
- 2024 review of this sector to assess the embeddedness of the Consumer Duty

# FCA Multi-firm review: Consumer Duty Implementation Plans

- On 25 January 2023, the FCA published feedback on firms' current implementation progress via its **Multi-firm review: Consumer Duty Implementation Plans**
- Some positive observations, but overall impression is that firms need to do more and quickly to meet the implementation deadline
- FCA has separately commented that the plans of some larger firms are overly simplistic and optimistic about their ability to comply with the Consumer Duty by the deadline
- Firms should expect the FCA to ask to see documented implementation plans and the results of scoping exercises

# FCA Multi-firm review: Consumer Duty Implementation Plans

- Three key areas of focus:
  - **Effective prioritisation:** to reduce the risk of poor consumer outcomes
  - **Embedding the substantive requirements:** consider Duty requirements in sufficient depth to meet the new standards – not only “superficially”
  - **Working with other firms:** working together with and sharing information with other firms in the distribution chain
- FCA also noted several examples of “good” and “poor” practice

# FCA Multi-firm review: Consumer Duty Implementation Plans

- Key observations in relation to the following areas:
  - **Governance and Oversight:** Senior leaders in firms need to drive the changes
  - **Culture and People:** Staff engagement and training to ensure understanding of their responsibilities
  - **Deliverability:** Clear workstreams, resource planning, and sensible prioritisation
  - **Third-party providers:** Identify and work together with third-party distributors and providers
  - **Four outcomes:** Avoid “high-level” approach and address substantive Duty rules/guidance
  - **Data strategies:** Monitoring, assessing, testing, understanding, and evidencing the outcomes customers are receiving
- FCA announced it will soon be sending a survey to a sample of firms, and has already issued a suite of letters to firms in particular sectors



# Consumer Duty: scoping points

- Benchmark Administrators
- Investment Trusts
- Secondary equity trading
- Assessing 'material influence'
- Portfolio acquisitions and structured finance

# Consumer Duty: further clarity needed?

- What is 'good' and how to demonstrate it?
- Vulnerability – industry led approach?
- MI
- PROD 3 compliance – additional qualitative considerations?



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Whistleblowing: insights  
David Berman

# Backdrop

- Strong regulatory focus on the cultural significance of “speak-up culture” combined with movements such as #MeToo, BLM
- Recent and steady increase in whistleblowing cases throughout financial services sector
- Whistleblowers increasingly inclined to share their concerns with the Regulator or with the media – predominantly, as they feel that their issues were not adequately addressed internally

# Actual or perceived impropriety

- Misperceptions can arise, most obviously, from one or both of: (a) a lack of perceptual awareness (as to how one's words or actions might be construed by others); and (b) poor or weak communication or transparency
  - Practical importance of combining: (a) pervasive perceptual awareness at organisational and individual levels; with (b) consistent, clear communication and transparency
- Marked increase in behavioural training sessions, particularly at managerial level - commonly covering areas such as, self-awareness, perceptual awareness, and demonstrable empathy

# Actual or perceived unfairness, inequality or inconsistency

- Espoused corporate values will invariably include a commitment to fairness, equality, and consistency
- Preferential, unfair, unequal, or inconsistent treatment represents one of the most common whistleblower drivers
- For example, (perceived or actual) differential treatment of senior versus junior staff whereby the firm imposes a lower sanction on a more senior staff compared with a junior staff (for an identical or very similar transgression)



# Actual or perceived unfairness, inequality or inconsistency

- The FCA will often take a particular interest in the fairness of treatment between senior and junior ranks. Indeed, any suggestion that a senior employee has, by virtue of their seniority, received unduly favourable treatment will likely be viewed as a cultural “red flag”
- Therefore, any organisation proposing to impose a lower sanction on a more senior employee compared with a junior colleague for an identical or ostensibly similar transgression would be well-advised to ensure that it has a **cogent and credible justification** in case this stance is ever challenged

# Failure to listen to, and meaningfully address, concerns raised informally

- The vast majority of organisations encourage a “speak-up” culture for employees to be able to raise concerns, make constructive challenges without fearing adverse consequences
- Regulators continue to emphasise the importance of a “psychologically safe” culture
- In many of these cases, the whistleblower will first have raised their concern(s) within their organisation, but to no avail, seeing no other alternative but to pursue a formal (and, increasingly, of late, public) route.
- For example, numerous recent ESG whistleblow cases have attracted high-profile media coverage - with each whistleblower having first raised their concerns informally within the organisation

# Failure to listen to, and meaningfully address, concerns raised informally

- **Demonstrable responsiveness, clear communication and transparency** are key in addressing concerns informally raised within organisations
- Concerns that are voiced — even on an informal basis — should be taken seriously, not least since they tend to escalate into formal whistleblows (and, possibly, attract enhanced sanctions from the Regulator) if unaddressed

# Poor (and tolerated) behaviour of influential managers

- A significant proportion of whistleblows will reference **perceived poor or inappropriate behaviour of influential managers** - often characterised, as intimidation, lack of self-awareness and empathy, resistance to challenge, bullying, harassment, victimisation, arrogance, snobbery, or favouritism
- Junior employees tend to take their behavioural cues from their direct (middle) managers, who play a key role in promoting values and in setting the “tone from above”

# Poor (and tolerated) behaviour of influential managers

- Many organisations are taking an increasingly dim view of such conduct — including more severe disciplinary and compensation consequences
- In practice, **behavioural skills training** is a key form of control for firms in this context

# Actual or perceived management hypocrisy

- This is often characterised by whistleblowers as management failure to “walk the talk”, “practise what they preach”, or “set a good example”.
- Such sentiments commonly result in significant resentment and disaffection within firms, with an adverse consequential impact on productivity, creativity, and workplace morale
- As such, management hypocrisy is a commonly cited feature of whistleblows
- Engagement surveys, pulse checks, and exit interviews are customary ways in which employee sentiment is routinely gauged. Ideally, these mechanisms would incorporate specific questions relating to the perception of management — in particular, whether management is regarded as setting a strong and positive example and “living by” espoused corporate values
  - Importance of **critical and objective analysis of results**



# Actual or perceived “tick box” culture

- “Tick box” culture is a commonly referenced feature of many public whistleblowers
- Perception that form overrides substance.
- In practice, it may be the case that some whistleblowers may have misconstrued a lack of visible action as inauthenticity, or disinterest
- Importance of clear, transparent, and consistent communication together with embedded (institutional and individual) perceptual awareness
- For example, many organisations will routinely convey substantive “all-firm” feedback on key points arising from a recent engagement survey and any responsive actions being taken (ideally, including timelines and accountabilities)

# Failure to keep pace with a changing environment

- Behavioural expectations and norms continue to evolve rapidly.
- For example, in several recent whistleblower cases, younger-generation employees have taken offence at words or conduct of more senior (and, typically, older) colleagues - more often than not, with the latter not having intended to cause offence or even having realised that they had done so
  - Real-life examples include: sexual innuendos made in front of others; use of inappropriate terms in the workplace; and inappropriate practical jokes
- “Harmless banter”. While the words may have been intended as such, the risk is that they can — and do — cause offence to others in proximity. In other words, it is the effect , not the intent that matters in this context

# Weak retaliation monitoring controls

- A material number of whistleblows derive from a perception formed by the complainant that they have suffered retaliation of sorts from speaking up / out
- In effect, a complainant who alleges retaliation is making a fresh whistleblower — that they have been retaliated against by virtue of speaking up
- Retaliation can occur in different forms – for example, exclusion (for no legitimate reason) from meetings
- The FCA takes a notoriously dim view of actual retaliation – which could call into question the fitness and propriety of the firm or relevant members of its staff
- While there is no prescriptive formula per se, all organisations are expected to take meaningful and proportionate measures to mitigate against the (potentially existential) risk of whistleblower detriment

# Inadequate governance and oversight

- In practice, inadequate governance and oversight is inextricably linked to several of the above drivers. In practice, this will often be exhibited via:
  - Insufficient focus on whistleblower drivers within the firm's governance framework
  - An apparent failure to “join the dots” for example through the absence of routine and systematic trend identification
  - Weak metrics, inadequate management information resulting in poor visibility of underlying whistleblower drivers/themes
  - A reluctance/failure to investigate underlying root causes of incidents, leading to missed opportunities to identify potentially troubling themes/trends

A blue-toned background image featuring a financial line chart with multiple data series and a grid. The chart shows various peaks and troughs, with some lines appearing more prominent than others. The overall aesthetic is professional and data-oriented.

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Financial promotions: FCA publishes data and  
insights from 2022  
Jonathan Ritson-Candler

# FCA publishes 2022 data on actions taken in relation to financial promotions

- FCA has published insights and data relating to its financial promotions supervisory and enforcement action throughout 2022, which is focussed on:
  - Authorised firms failing to comply with financial promotions rules; and
  - Unauthorised firms making unlawful financial promotions
- FCA has materially increased its surveillance and intervention activity:
  - *Authorised firms:* 8,582 promotions amended or withdrawn, an increase of 1398% compared to 2021
  - *Unauthorised firms:* 1,882 alerts, an increase of 34% compared to 2021 (and despite the number of reports / complaints of unlawful finproms received by the FCA decreasing by 24%)



# Priority areas for FCA supervision and enforcement

- FCA is concerned that the cost of living crisis is increasing the prevalence of scams, often as a result of unfair, unclear and misleading or unauthorised financial promotions
  - “It is more important than ever that financial promotions are responsible and clear so consumers can commit to appropriate financial products”*
- Fin-fluencers, bloggers and social media:
  - Confluence of younger investors / students potentially being encouraged into risky products and/or high cost credit products plus non-traditional communication channels via which unauthorised persons are making unlawful financial promotions
  - FCA has increased surveillance capabilities across all social media channels to detect harmful content and ask companies to remove it
  - Working with search engine providers to get commitments that they will not permit unauthorised firms to market financial services

# Priority areas for FCA supervision and enforcement

- Policing the perimeter
  - FCA has issued alerts to, and requested content be taken down by, influencers promoting unauthorised traders to their followers and those providing trading signals to 70k potentially vulnerable followers
  - FCA has used banning power under FSMA to require an online retail broker with 1.1m UK retail customers to cease its marketing campaign as it was targeting vulnerable customers with significant debt
  - Took action against an unregistered cryptocurrency exchange that was offering derivative cryptocurrency products to UK customers and had its website taken down
  - Actively checking if de-authorized firms were still making promotions or otherwise representing that they are regulated and taking action

# Priority areas for FCA supervision and enforcement

- Strengthening rules
  - FCA comments on its ongoing work to strengthen the financial promotions rules, including the consolidation and updates to the rules relating to marketing high risk investments to retail clients
  - Certain of those rules entered into force on 1 December 2022 and the FCA did not provide implementation forbearance, instead reviewing 67 crowd funding and peer to peer lending firms shortly after the implementation date to assess compliance
  - 60% were found to have failed to comply
- Takeaways for firms:
  - A generally more assertive regulator
  - Keep on top of the various changes to the financial promotions regime and update processes accordingly (and be ready from day 1)
  - Consider non-traditional media and if they are being used to make finproms



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ESMA Trading Venue Perimeter: Final Guidance  
Nicola Higgs

# ESMA Trading Venue Perimeter

- 2 February 2023: ESMA published final guidance on the trading venue perimeter
  - Explains when systems should be considered as multilateral systems and seek authorisation as a trading venue
  - ESMA's goal is to enhance supervisory convergence in the Union, ensure that firms operating multilateral systems swiftly apply for authorisation as a trading venue with their respective national competent authority (NCA) and thereby contribute to a level-playing field in the EU

# New points

- **Primary / secondary markets**
  - The guidance intends to capture secondary markets trading and not primary market activities
- **SFTs**
  - An entity operating a system in which multiple third-party buying and selling interests in SFT relating to financial instruments are able to interact, should seek authorisation to operate a trading venue

# New points

- **RTO**

- ESMA: *“In relation to the potential guidance on what is the service of RTO and the respondents’ feedback that more guidance may be needed, ESMA will reflect whether further clarifications need to be published in the future”*
  - RTO = the receipt and transmission from one provider to another, on behalf of a client, of orders relating to financial instruments
  - OTF = operating a multilateral system with discretionary functionality to match, arrange and/or negotiate a transaction between participants
  - How will the pre-arranging guidance impact RTO analysis?



# Types of trading venue

<b>Regulated market</b>	<ol style="list-style-type: none"> <li>1. Multilateral system</li> <li>2. Brings together (or facilitates bringing together)</li> <li>3. Multiple third-party buying and selling interests in financial instruments</li> <li>4. In the system and in accordance with <b>non-discretionary</b> rules</li> <li>5. In a way that results in a contract</li> </ol>	<ol style="list-style-type: none"> <li>1. Operated by a <b>market operator</b></li> <li>2. In respect of the <b>financial instruments admitted to trading under its rules and/or systems</b></li> </ol>
<b>Multilateral trading systems (MTF)</b>	<ol style="list-style-type: none"> <li>1. Multilateral system</li> <li>2. Brings together</li> <li>3. Multiple third-party buying and selling interests in financial instruments</li> <li>4. In the system and in accordance with <b>non-discretionary</b> rules</li> <li>5. In a way that results in a contract</li> </ol>	<ol style="list-style-type: none"> <li>1. Operated by an <b>investment firm / market operator</b></li> </ol>
<b>Organised trading facilities (OTF)</b>	<ol style="list-style-type: none"> <li>1. Multilateral system</li> <li>2. Multiple third-party buying and selling interests</li> <li>3. Are able to interact in the system using <b>discretion</b> to match orders</li> <li>4. In a way that results in a contract</li> </ol>	<ol style="list-style-type: none"> <li>1. Neither a regulated market or MTF</li> <li>2. In: <ul style="list-style-type: none"> <li>• Bonds</li> <li>• Structured finance products</li> <li>• Emission allowances</li> <li>• Derivatives</li> </ul> </li> </ol>



# Multilateral system

**Multilateral system** = Any system or facility in which multiple third-party buying and selling trading interests in financial instruments are able to interact in the system (*Article 4(1)(19) MiFID II*)

Multilateral system	✓	✗
1. It is a system or facility	A set of <b>rules</b> that governs how third-party interests interact	<b>Rules ≠</b>
2. There are multiple third party buying and selling interests	<p><b>Rules =</b></p> <ul style="list-style-type: none"> <li>▪ contain elements that concern the matching, arranging and/or negotiation of trading interests</li> <li>▪ do not need to ensure that trades executed in the system are contractually binding</li> </ul>	<ul style="list-style-type: none"> <li>▪ technical standard of message construction (e.g. XML)</li> <li>▪ the protocol which governs the technical exchange of messages</li> </ul> <p>Software providers: Not in scope if it is the investment firm user that sets the rules of interaction</p>
3. Those trading interests need to be able to interact	<p><b>Interaction =</b></p> <ul style="list-style-type: none"> <li>▪ advertising trading interests +</li> <li>▪ facilitate reaction by providing the means to match, arrange and/or negotiate a transaction between participants (i.e. the <b>intention to enter into a transaction</b> can be confirmed in the system)</li> </ul>	<b>Interaction ≠</b>
4. Trading interests need to be in financial instruments		<ul style="list-style-type: none"> <li>▪ simple provision of pricing data or other tools used to make trading decisions / aggregate and broadcast indications of interest (e.g. bulletin boards)</li> <li>▪ simple connectivity between the bulletin board and an execution venue would not bring the system into scope</li> <li>▪ system that only displays third party trading interests which are routed to, and subject to execution under the rules of the relevant trading venue, should not be considered as a multilateral system</li> </ul>

# Guidance on specific systems

## **Order management system (OMS)**

OMSs that are designed to automate the order submission system, to structure the order flow, and work as an inward-looking tool that helps companies to easily follow up the lifecycle of orders are not intended and should not be considered multilateral systems

## **Execution management system (EMS)**

EMSs that manage orders across multiple execution venues, offering traders real time information on market data and analytics and facilitate order execution by offering an overview of liquidity and prices on various venues, subsequently sending orders to the preferred trading venue or trading venues for execution should not be considered multilateral systems

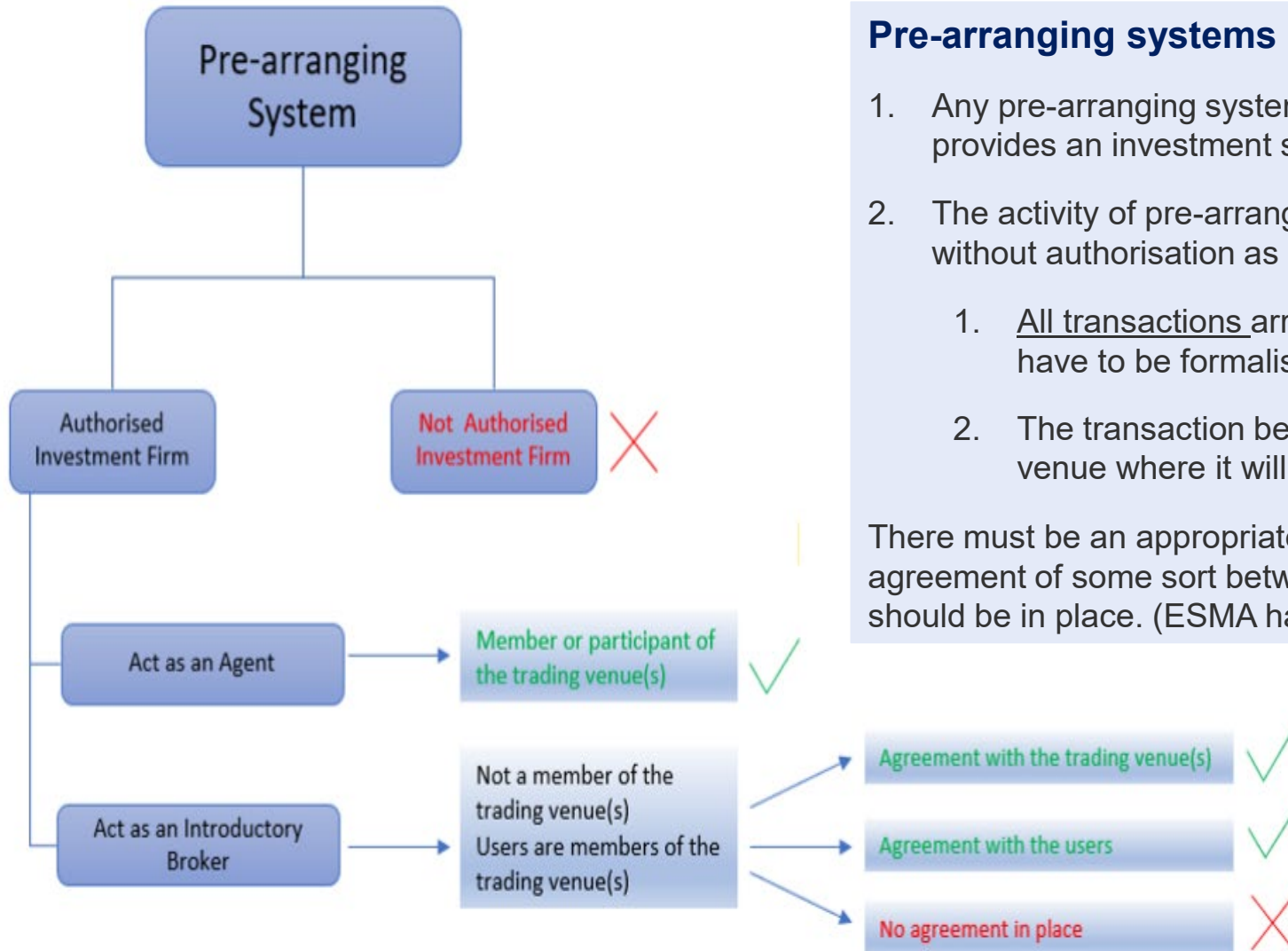
## **Request for quote (RfQ)**

Multilateral system = systems in which the operator is independent from the (buy and sell-side) participants on the system, should be considered as multilateral

- multiple members have the possibility to interact with multiple liquidity providers
  - even if only bilateral interaction happens in practice
  - even with only one liquidity provider

As distinguished from SIs – where the investment firm allows its (multiple) clients to initiate RFQs for which the firm is the sole counterparty. I.e. the liquidity provider governs how the trading interests interact and sets the rules of the platform.

# Guidance on specific systems



## Pre-arranging systems

1. Any pre-arranging system should be authorised as a MiFID II investment firm as it provides an investment service to clients
2. The activity of pre-arranging transaction in a multilateral way is only possible without authorisation as a trading venue when:
  1. All transactions arranged through the investment firm's system or facility have to be formalised on a (regulated) trading venue (i.e. not OTC)
  2. The transaction benefits from a pre-trade transparency waiver in the trading venue where it will be formalised

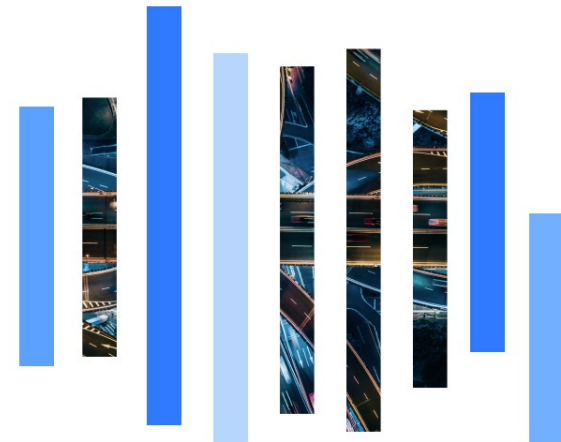
There must be an appropriate oversight of this pre-arranging system and therefore, an agreement of some sort between the pre-arranging system and the trading venue should be in place. (ESMA has provided examples of these agreements)

# 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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## [Consumer Duty Update: FCA Issues Dear CEO/Director Letters Setting Priorities for Sectors](#)

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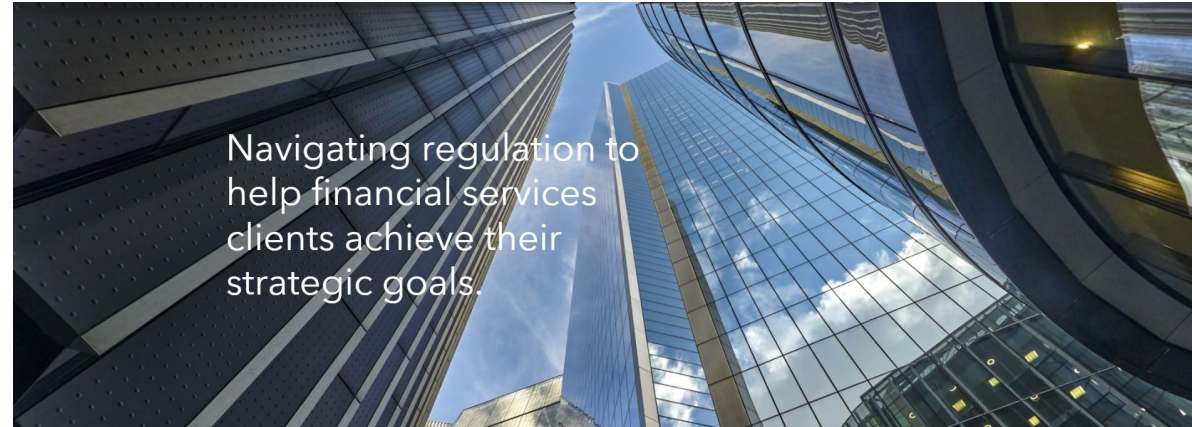
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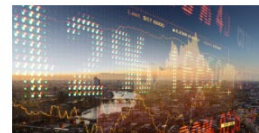
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