

A blue-toned background image 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.

LATHAM & WATKINS^{LLP}

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Financial Regulation Monthly Breakfast Seminar

Overview



The background of the slide is a blue-tinted financial chart. It features a grid of dashed lines and several data series represented by thick, glowing blue lines. The lines show various trends, including a sharp decline followed by a recovery, and a more volatile, jagged line. At the bottom of the chart, there are some faint, partially visible labels like '12h' and ':30'.

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MiFID Research

Rob Moulton

MiFID research – extra territoriality

- The basic problem
 - EU-based firms need to pay
 - US-based firms are not allowed to receive payments without becoming an Investment Advisor
- The Commission and the FCA's approach to extra territoriality issue
- US / SEC's (potential) approach to extra territoriality issue
- Watch this space

MiFID research – the future of RPAs

- Clear and significant recent swing towards paying by P&L
 - In particular, large long-only buy side firms
- Clear and significant recent swing towards utilising ESMA's guidance on freely available research
- Will this be acceptable to the FCA?
- What is the future for RPAs?

MiFID research – legal documentation

- Termination of CSA and transfer arrangements for legacy balances
 - Pay into RPA?
 - Pay back to manager?
 - Pay to underlying funds?
 - Keep as pre-payment on 2018 research coverage?
 - Keep full stop?
- Research Payment Agreement
- Research Charge Collection Agreement
- Is there any documentation requirement at all?

MiFID research – other points

- Trial periods
- Can payment arrangements be entirely after the event?
- Pre-IPO and corporate sponsored research
- (i) Research: (ii) non-monetary benefit: (iii) minor-non-monetary benefit
 - “If macro-economic analysis is not considered as research, it does not automatically classify as a minor non-monetary benefit”
- Client money status of pre-RPA research charges

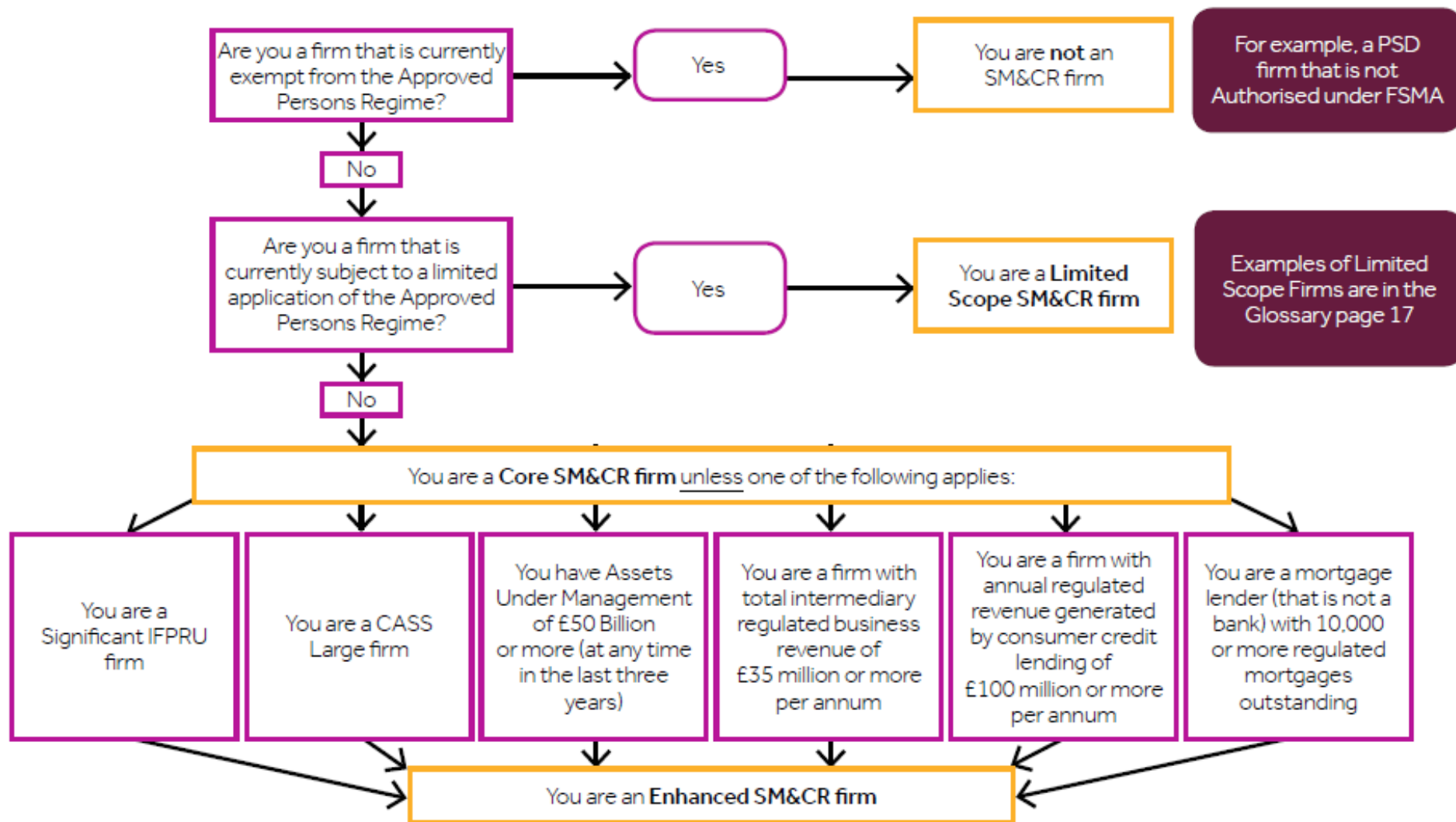


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Senior Managers & Certification Regime – Extension

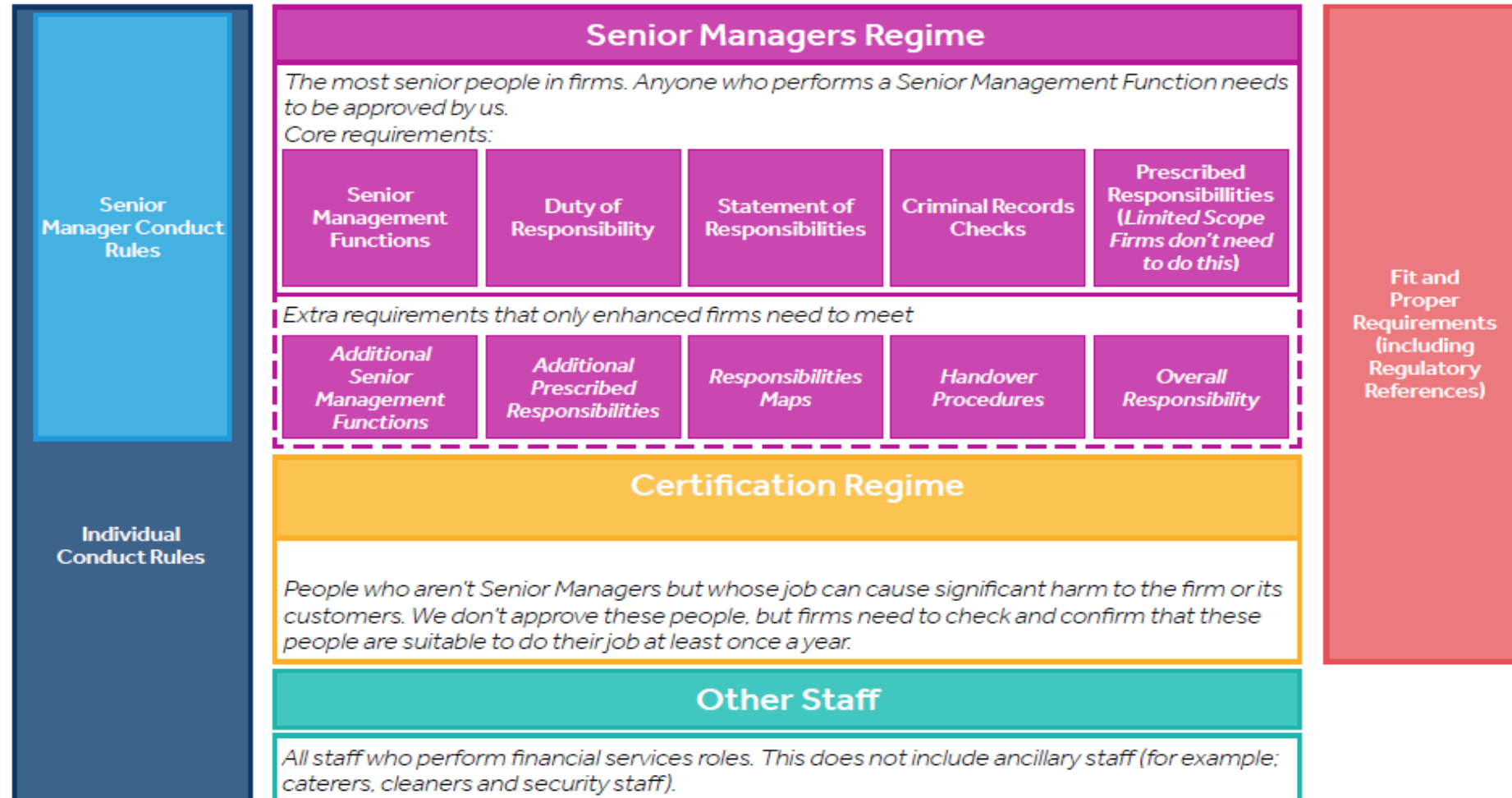
David Berman

What does 'proportionality' look like for both firms and individuals?



Summary diagram

Summary Diagram – The Senior Managers & Certification Regime



Key features of SMCR (1)

- Categories of individual
 - Senior Managers: role involving risk of serious consequences for firm, or for business
 - Certified Staff: role involves risk of significant harm to firm or its customers
 - Conduct Employees: broadly everyone else (save for purely administrative personnel)
- Senior Management Functions
 - Core: chief executive; executive director, partner; chair; compliance oversight, MLRO
 - Enhanced: all of the above PLUS: chief finance function; chief risk function; senior independent director; chairs of the remuneration; risk audit and (if there is one) nominations committee; group entity senior manager; chief operations function; other overall responsibility

Key features of SMCR (2)

Prescribed responsibilities

Anticipated PRs		Application
1.	Performance by the firm of its obligations under the Senior Managers Regime, including implementation and oversight	Core
2.	Performance by the firm of its obligations under the Certification Regime	Core
3.	Performance by the firm of its obligations in respect of notifications and training of the Conduct Rules	Core
4.	Responsibility for the firm's policies and procedures for countering the risk that the firm might be used to further financial crime	Core
5.	Responsibility for the firm's compliance with CASS (if applicable)	Core
6.	Responsibility for ensuring the governing body is informed of its legal and regulatory obligations	Core
7.	Responsibility for an AFM's value for money assessments, independent director representation and acting in investors' best interests	Core
8.	Compliance with the rules relating to the firm's Responsibilities Map	Enhanced
9.	Safeguarding and overseeing the independence and performance of the internal audit function (in accordance with SYSC 6.2)	Enhanced
10.	Safeguarding and overseeing the independence and performance of the compliance function (in accordance with SYSC 6.1)	Enhanced
11.	Safeguarding and overseeing the independence and performance of the risk function (in accordance with SYSC 7.1.21R and SYSC 7.1.22R)	Enhanced
12.	If the firm outsources its internal audit function, taking reasonable steps to ensure that every person involved in the performance of the service is independent from the persons who perform external audit, including: <ul style="list-style-type: none">• supervision and management of the work of outsourced internal auditors• management of potential conflicts of interest between the provision of external audit and internal audit services	Enhanced
13.	Developing and maintaining the firm's business model	Enhanced
14.	Managing the firm's internal stress-tests and ensuring the accuracy and timeliness of information provided to the FCA for the purposes of stress-testing	Enhanced

Key features of SMCR (3)

Conduct rules

First Tier – Individual Conduct Rules

- 1 You must act with integrity
- 2 You must act with due care, skill and diligence
- 3 You must be open and cooperative with the FCA, the PRA and other regulators
- 4 You must pay due regard to the interest of customers and treat them fairly
- 5 You must observe proper standards of market conduct

Second Tier – Senior Manager Conduct Rules

- SC1. You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively
- SC2. 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
- SC3. You must take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person and that you oversee the discharge of the delegated responsibility effectively
- SC4. You must disclose appropriately any information of which the FCA or PRA would reasonably expect notice

Key features of SMCR (4)

- Statements of Responsibilities (for Senior Managers)
- Fitness and Proprietary => Certification
- Responsibilities Maps (enhanced only)
- Handover Procedures (enhanced only)
- Training for all
- Non-executive directors

Some open questions / issues (1)

- Can the regime extend to individuals based abroad or elsewhere within a group?
 - Example of a clerical employee based off-shore having infrequent contact within UK clients
 - Delegation of portfolio management
- Does the regime capture 'de facto' directors or partners?
- Why is there no CIO function?
- Which SMFs should be allocated to non-executives?
 - What if we have no non-executives?

Some open questions / issues (2)

- What are likely to be the most significant implementation workstreams?
- Will the absence of an 'overall responsibility' obligation for core firms effectively result in the CEO shouldering even more responsibility?
- What does the Duty of Responsibility add over and above Senior Manager Conduct Rule 2?
- Where is a Senior Manager most vulnerable?
- What enforcement routes can the FCA pursue against a Senior Manager?
- What do 'reasonable steps' look like?

The background of the slide is a blue-tinted financial line chart. It features a grid of horizontal and vertical dashed lines. Two primary data series are visible: a thick, solid blue line and a thinner, dotted blue line. The thick line starts at the top left, dips, rises to a peak, dips again, and then rises to a higher peak before trending downwards. The dotted line starts at the top center, dips, and then trends downwards. At the bottom of the chart, there are some faint, partially visible labels: '12h' and ':30'.

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MLD4 – Update

Anne Mainwaring

Overview

- The Fourth Money Laundering Directive (MLD4) is designed to strengthen the EU's defences against money laundering and terrorist financing
- MLD4 has repealed and replaced the Third Money Laundering Directive (MLD3) and the MLD3 Implementing Directive
- MLD4 was implemented in the UK through the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017, which amended and replaced the Money Laundering Regulations 2007 on 26 June 2017
- The JMLSG guidance has been updated to align it with the 2017 Regulations

Key changes – documented risk assessment

- Firms are required to undertake a risk assessment to identify and assess the risks of ML and TF to which their business is subject taking into account at least the following risk factors
 - Who their customer is
 - The countries or geographical areas they operate in
 - The particular products, services and transactions the customer requires
 - The channels the firm uses to deliver these products, services and transactions
- This risk assessment must be documented, kept up to date and made available to the FCA on request

Key changes – customer due diligence

- No automatic reliance on simplified due diligence
- A risk based assessment must be undertaken to determine whether simplified due diligence is appropriate
- Firms may apply SDD measures in situations where the ML and TF risk associated with a business relationship has been assessed as low
- ESAs have published Final Guidelines on customer due diligence and the factors firms should consider when assessing money laundering and terrorist financing risk
- Introduction of a blacklist of high-risk third countries which make EDD compulsory if any business relationship/transaction is with a person established in that country

Key changes – PEPs

- MLD4 extends the scope of persons who are included within the PEP definition
- The requirements that previously only applied to foreign PEPs have been extended to cover UK PEPs
- This extends the range of persons that fall within the PEP definition and that therefore must be subject to enhanced due diligence
- PEPs must be subject to EDD for at least a year after they have left office. However family members of PEPs no longer need to be subject to EDD immediately upon the PEP leaving office (previously family members and close associates were subject to EDD for a year after the PEP in question left office)

FCA FG 17/5 the treatment of PEPs for AML purposes

- Provides useful guidance in relation to proportionality
 - The definition of a ‘prominent public function’ will vary according to the nature of the function held by a person. The FCA would expect firms to understand the nature of the position held and whether the function gives rise to the risk of large-scale abuse of position. If a position is held in a country assessed as being at a lower risk of large-scale corruption (because of the system and checks and balances in place that reduce the threat) then only those with true executive power should be considered to hold a prominent public function. In the UK, it will not normally be necessary to treat public servants below Permanent or Deputy Permanent Secretary as having a prominent public function

MLD5

- Will amend MLD4 with the aim of better countering the financing of terrorism and to ensure increased transparency of financial transactions and of corporate entities.
- The amendments under MLD5 target areas such as:
 - Designating virtual currency exchange platforms as obliged entities
 - Setting lower maximum transaction limits for certain pre-paid instruments
 - Enabling competent authorities to identify holders of bank and payment accounts



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Questions?