BRIEFING

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New Year briefing

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After a tumultuous 2019, it's a new year, a new decade and a new UK Government pledged to "get Brexit done". The UK Parliamentary paralysis that characterised so much of the UK's approach to Brexit last year is over.

The UK will leave the EU on 31 January 2020. At the same time, it will enter into an 11-month implementation period where in practice nothing much will change for UK financial services firms – EU rules will still apply, passporting will continue.

However, the UK Government has said it will not seek an extension to this period. Quite soon, therefore, EU lead negotiator Michel Barnier's clock is likely to start ticking again and, depending on how negotiations between the UK and EU proceed (which may or may not focus on financial services), another type of "no deal" deadline may loom as we get closer to the end of the year. The numerous "Brexit SIs" that were made last year in preparation for a no deal exit day have been postponed, *en masse*, to 31 December 2020. It may all start to feel like groundhog day again.

Considerable uncertainty therefore remains. Many EU financial services legislative measures in the pipeline are not scheduled to come into effect until *after* the end of the transitional period on 31 December 2020. With no current legal mechanism in place that would mandate their transposition into UK law, mixed signals from the UK government as to whether and to what extent the UK will be seeking alignment with EU rules, and the intention on its part to introduce a domestic, post-Brexit Financial Services Bill, there is uncertainty as to whether the UK will track future EU legal developments in financial services.

But firms cannot afford to "wait and see"; they will need to start planning and preparing on the assumption that the EU pipeline measures *will* be implemented in the UK with little or no amendment (not least because many of them, to a greater or lesser extent, were driven by UK government policy).

In this briefing:

This means UK investment firms will need to start planning for the most significant legislation to hit them since the MiFID II regime, the new prudential regime established by the Investment Firms Regulation and Directive: for all it will mean having to make major adjustments to their processes and the way they calculate their prudential requirements; for some, it will mean having to hold a great deal more regulatory capital.

Climate change and sustainabilty increasingly dominate the political agenda around the world and incoming legislation and other regulatory initiatives reflect this with specific measures directed at the financial services sector and the making of investment decisions. These include EU regulations on sustainability-related disclosures and on a taxonomy for environmentally sustainable activities and a new European Green Deal which includes within its wide-ranging scope a focus on the private sector and strengthening the foundations for sustainable investment.

The cross-border distribution of funds legislation, which will apply to EU AIFMs, may or may not end up having a direct impact on UK AIFMs (who will lose their passporting rights after 31 December 2020). Even if it doesn't, some of its ideas may be adopted by individual EU member states in their national private placement regimes, impacting on the ability to market into those countries without a passport. Ongoing changes continue to be made to EU measures that are already in force, such as the Market Abuse Regulation, EMIR and the rules on PRIIPs. The European Commission is likely to publish the results of its review of AIFMD during 2020 – proposed legislative amendments will almost certainly follow.

The transition from LIBOR (which is due to expire at the end of 2021) to risk-free reference rates will not only impact on those banks and others which use the moribund benchmark in their products and investments – the FCA also expects asset managers which have LIBOR-reference instruments in their portfolios and funds to prepare and take proactive steps to mitigate the risks.

So, alongside their post-Brexit strategy, firms will need to start planning for, and dedicating resources to, a wide range of other significant measures.

You don't need to have 20/20 vision to see that the year ahead will be challenging…

PART A: PRUDENTIAL REGULATION

1 Investment Firms Regulation and Directive

WHAT IS THIS? New prudential regime including regulatory capital requirements, remuneration rules and internal governance and disclosure and reporting requirements. Includes stricter requirements for third-country firms seeking MiFID equivalence.

WHO DOES THIS APPLY TO? MiFID investment firms and (likely) AIFMs and UCITS management companies with "MiFID top-ups". In addition: MiFID third country firms (who will face tougher equivalence assessments) and all AIFMs and UCITS management companies (who will be subject to a revised own funds requirement).

WHEN DOES THIS APPLY? 26 June 2021, with some limited transitional phasing-in after this date.

INTRODUCTION

The new Regulation on prudential requirements for MiFID investment firms (**IFR**) and the accompanying Directive (**IFD**) came into force at the end of 2019 and will apply as of **26 June 2021**. We discussed the IFR/IFD in more detail in our briefing in May 2019 (here).

IFR/IFD introduces a bespoke prudential regime for most MiFID investment firms to replace the one that currently applies under the fourth Capital Requirements Directive and the Capital Requirements Regulation (**CRD IV and CRR**).

Given that the fifth Capital Requirements Directive and the second Capital Requirements Regulation (**CRD V and CRR II**) are due to come into force before IFR/IFD are effective, there is a theoretical risk that these firms could be required to step-up to CRD V before stepping back down to IFR/IFD. Representations have been made by certain member states and it is hoped that there will be some form of EU legislative "fix" to resolve this.

IFR/IFD will mean higher regulatory capital requirements for firms, subject to some transitional phasing-in in respect of own funds. IFR/IFD will also mean new, more onerous remuneration rules, based on those applicable to banks, as well as a raft of internal governance and disclosure and reporting requirements.

Investment firms should start their project planning now assuming that the IFR/IFD regime will be implemented in the UK with little or no change.

The rules are likely to be a significant step up for many firms, but the biggest impact is likely to be for adviser/arranger firms. These changes may result in a significant increase in their capital requirements and the application to them for the first time of both prudential consolidation and detailed remuneration rules.

The new regime will also introduce a stricter framework for third-country firms seeking to rely on the equivalence provisions in the Markets in Financial Instruments Regulation (**MiFIR**).

APPLICATION

IFR/IFD applies to MiFID investment firms other than those larger firms which deal on own account and/or carry out the activities of underwriting or placing on a firm commitment basis and which by virtue of their size and/or interconnectedness in the financial system are considered to be of systemic importance. Those large firms will be subject to CRD IV and CRR instead (and, in due course, CRD V and CRR II).

The majority of MiFID investment firms, including portfolio managers, brokers, corporate finance houses, trading venue operators and adviser/arrangers, will therefore be subject to IFR/IFD.

Where a MiFID investment firm meets the requirements to be a "small and non-interconnected investment firm" (**SNIF**), IFR/IFD applies, but on a limited basis. In particular, the remuneration requirements will not apply to such firms and they will not be required to make use of the K-factors metric when calculating own funds.

The criteria that a firm needs to meet to qualify as a SNIF mean that all but the smallest firms will be subject to the full scope of IFR/IFD (e.g. firms with an annual income in excess of EUR 30 million will not qualify as a SNIF).

For the most part, IFR/IFD does not affect collective investment fund managers directly. However:

- depending on future UK government policy, AIFMs with MiFID top-up permissions will - consistent with the approach the UK has previously adopted in respect of prudential matters - be caught;
- as summarised below, despite generally not applying to AIFMs directly, the new legislation will nonetheless make a specific amendment to AIFMD in terms of own funds; and
- IFR/IFD will clearly be relevant to fund management groups which have MiFID firms within their structures.

As with the EU cross-border distribution of funds package, the IFR/IFD regime will likely apply some time after the UK has left the EU. To a considerable extent, IFR/IFD reflects policy developed in the UK and, for the time being at least, the assumption is that the UK authorities will wish to impose similar domestic legislation. Whether there may be divergences in the detail (for instance, with regards to the imposition of remuneration requirements) depends on the UK's policy on the interrelationship between UK and EU regulation, such as the degree of 'equivalence' that will be sought. Firms should therefore look out for details of how H.M. Treasury and the Financial Conduct Authority (**FCA**) intend to 'onshore' the regime in the UK.

PRUDENTIAL GROUPS AND CONSOLIDATION

All investment firms subject to IFR/IFD must comply with the regime's requirements relating to own funds (regulatory capital) composition, the calculation of capital requirements, concentration risk, liquidity requirements, disclosure and reporting on a solo (individual firm) basis.

In general, a parent investment firm, parent investment holding company or parent mixed financial holding company in the EU (whether or not regulated) shall also be required to apply all of the above requirements on a consolidated (or group) basis. For most firms, this does not represent a change to existing group requirements, but it will be new for some, e.g. adviser/arrangers.

By way of derogation to the full prudential consolidation requirement described above, supervisors will have the discretion to apply a simpler and lighter-touch group capital test in the case of group structures which they deem to be

"sufficiently simple" and in respect of which no significant risks to clients or to the market will arise from not applying consolidated supervision.

If full prudential consolidation under the IFR applies, then the IFD's requirements relating to internal governance, transparency, treatment of risks and remuneration will also be applied to firms which are subject to the full application of the regime on a solo and consolidated basis (except in relation to certain third-country subsidiaries where it would be unlawful to do this).

REMUNERATION

The remuneration requirements apply in respect of staff, such as senior management and employees with comparable remuneration, whose professional activities have a material impact on the risk profile of the firm or the assets that it manages.

The requirements relating to remuneration include:

- A requirement to have a remuneration policy that is proportionate to the size, internal organisation and nature of the firm and the scope and complexity of its activities and which complies with a number of principles.
- A requirement to set - and publish - appropriate ratios of variable remuneration to fixed remuneration that may be paid to relevant staff, ensuring that the fixed component represents a "sufficiently high proportion" of the total remuneration to enable the operation of a fully flexible policy on variable remuneration components, which are likely to require firms to implement new processes and data capture arrangements so as to be able to calculate them correctly on an ongoing basis.
- A requirement for any variable remuneration to comply with a number of requirements, including as to payment in shares in the firm or other qualifying instruments and deferral as well as malus (i.e. restrictions on vesting) and clawback.
- A requirement to establish an independent and gender balanced remuneration committee.
- A requirement to make certain disclosures regarding the remuneration policy and practices as well as providing remuneration information to supervisors.

As stated above, none of the remuneration requirements apply to SNIFs. In addition, other firms which are below certain size criteria will not have to comply with the requirements governing the constitution of variable pay and the deferral of payment or the need to have a remuneration committee.

QUANTITATIVE CAPITAL REQUIREMENTS

Subject to transitional phasing-in, a firm will generally be required to have own funds at all times at least equal to the highest of its:

- *fixed overheads requirement* – at least one quarter of its fixed overheads for the preceding year;
- *permanent minimum requirement* – e.g. for a portfolio manager, corporate finance firm or adviser/arranger (which does not hold client money) it is likely to be EUR 75,000 and, for a firm with a principal dealing permission, EUR 750,000; and
- *"K-factor" requirement* – a new, activities-based capital requirement based on an aggregation of three risk factors applicable to the firm (each of which has a number of highly detailed components).

In addition to the own funds requirements, firms will be required to hold an amount of liquid assets equal to at least one third of their fixed overheads requirement, which, in practice, will equate to one month's fixed overheads.

Supervisors can also require firms to hold additional capital in certain circumstances such as where they consider that the firm is exposed to risks which are not adequately covered by the standard capital requirements.

DISCLOSURES AND PUBLIC REPORTING

Firms will also be subject to a wide range of disclosure and reporting requirements under IFR/IFD. These include (but are not limited to) the requirement to make public disclosures about their capital, capital requirements, risk management objectives and policies, internal governance arrangements and remuneration policies and practices.

Public country-by-country reporting rules will also apply as well as a requirement to report certain regulatory capital information to supervisors and for larger firms to disclose certain voting information.

IFD/IFR firms (other than SNIFs) will be subject to high earners reporting and will be required to provide supervisors with information on the number of natural persons per firm that are remunerated EUR 1 million or more per financial year.

THIRD COUNTRY FIRMS AND EQUIVALENCE ASSESSMENTS

IFR/IFD amends the rules on assessing third countries for equivalence in relation to the provision of cross-border services by third country firms under MiFIR to state that when carrying out any equivalence assessment in relation to a third country for those purposes, the Commission must take into account (amongst other factors):

- whether firms in that jurisdiction are subject to prudential, organisational and business conduct requirements which are equivalent to those which apply in MiFIR, CRD IV and IFR/IFD; and
- whether firms in that third country are subject to effective supervision and enforcement to ensure compliance with those requirements.

APPLICATION TO AIFM AND UCITS

The new regime does not directly impact upon collective investment fund managers acting as such. However, consistent with the current approach adopted here, it is likely that it will apply to AIFMs and UCITS management companies with "MiFID top-ups" in the UK. Elsewhere it will depend on national EU member state implementation. In addition, IFD makes specific amendments to both AIFMD and the UCITS Directive to provide that own funds of an alternative investment fund manager or UCITS management company can never be less than the fixed overheads requirement as specified in IFR – i.e. at least one quarter of the fixed overheads of the preceding year.

WHAT'S NEXT

The FCA is expected to publish a high-level discussion paper in the first quarter of 2020. This is likely to give the first clear steer as to how the UK will approach the implementation of a regime that will not become effective until after the end of the EU withdrawal transitional period (assuming that period is not extended).

PART B: INVESTMENT FUNDS

2 Cross-border Distribution of Funds

WHAT IS THIS? New rules on the marketing of funds.

WHO DOES THIS APPLY TO? EU AIFMs and UCITS management companies.

WHEN DOES THIS APPLY? Largely from 2 August 2021 (but some provisions apply earlier).

INTRODUCTION

The Regulation on cross-border fund distribution (**CBD Regulation**) and the Directive on the cross-border marketing of funds (**CBD Directive**) entered into force on 1 August 2019. The majority of the CBD Regulation applies as from **2 August 2021** and member states must also implement the CBD Directive as from that date.

Supervisors have the ability to require the prior notification of AIF marketing communications to retail investors as of 1 August 2019 but, as at the time of writing, the FCA has not yet applied this and we are not currently aware of any other EU member state doing so.

APPLICATION

The new regime will be directly applicable to EU AIFMs and UCITS management companies. It is now likely that, by August 2021, the UK will no longer be a member of the EU and that (unless extended) the EU withdrawal transitional period will have ended. It therefore remains to be seen to what extent UK fund managers will be affected, at least directly. To the extent that the regime amends the operation of the EU cross-border fund marketing passport regimes, the UK may simply decide to revoke the directly applicable CBD Regulation (which would have been the effect of the Cross-Border Distribution of Funds, Proxy Advisors, Prospectus and Gibraltar (Amendment) (EU Exit) Regulations 2019 had they come into force on 31 October 2019 on a "hard Brexit" then). It is possible, however, that even with such a

revocation and no implementation of the CBD Directive there may nonetheless be legislation 'onshoring' certain aspects of the regime into the UK. At the very least UK and other non-EU fund managers may find that they are affected by consequential amendments that individual EU member states may decide to make to their national private placement regimes. Firms which have established AIFMs or MiFID investment firms in a remaining EU member state are likely to need to prepare to comply with the rules under the CBD Regulation and CBD Directive as they apply in the EU and also the UK regime (assuming that elements of the new rules are "onshored").

We discussed the CBD Regulation and the CBD Directive in more detail in our briefing in May 2019 (here). We summarise below the main impacts of the CBD Regulation and the CBD Directive for AIFMs.

PRE-MARKETING BY AIFMS

The Alternative Investment Fund Managers Directive (**AIFMD**) marketing passport for alternative investment funds (**AIFs**) only applies to activities that fall within the AIFMD's definition of 'marketing'. Individual member states have taken divergent views about when 'marketing' is deemed to begin and the CBD Directive attempts to address this by introducing a new definition of 'pre-marketing'.

In essence, 'pre-marketing' is defined as: information or communication relating to investment strategies or investment in order to test investor interest in a fund which is not yet established, or is established but is not yet notified for marketing.

An AIFM will 'not be pre-marketing' where the information:

- is sufficient to allow investors to commit to the AIF;
- amounts to subscription documents in draft or final form; or
- amounts to final form constitutional or offering documents of a yet-to-be established AIF.

The AIFM will be required to send, within two weeks of the start of its pre-marketing, an 'informal letter' with details of the pre-marketing to its home member state regulator.

Any third parties which the AIFM uses to pre-market on its behalf will essentially have to be licensed as MiFID investment firms or EU banks and will be subject to same conditions which apply to the AIFM itself.

Any subscription by investors in units or shares of an AIF that takes place within 18 months of the pre-marketing will be considered to be the result of marketing and the applicable marketing notification procedures under AIFMD will be triggered. This closes down any possibility of arguing that subsequent investments can be considered to result from reverse solicitation.

MARKETING TO RETAIL INVESTORS

New requirements under AIFMD will apply when *any* AIFM (ie EU or non-EU) is marketing units or shares in an AIF to retail investors. The AIFM will be required to put in place certain 'facilities' in the relevant member state to perform certain defined tasks.

Where an AIFM proposes to market to retail investors in a particular EU member state, the regulator in that jurisdiction may require prior notification of the marketing communications which the AIFM intends to use. The relevant national regulator may request the AIFM to amend the marketing communication at any time within 10 working days of being notified.

The current AIFMD rules are unclear on when an AIFM can be considered to have ceased marketing in a member state. A new provision in AIFMD will clarify that an AIFM may only discontinue the marketing of units or shares of an EU AIF in a jurisdiction in which it has exercised the marketing passport if the following conditions are met:

- the AIFM has publicised its intention to cease its marketing activities in respect of some or all of its funds in that jurisdiction through a publicly available medium, including by electronic means, which is customary for marketing AIFs and suitable for a typical AIF investor;
- any contracts the AIFM has with financial intermediaries or delegates are modified or terminated with effect from the date of de-notification; and
- the AIFM has made a public offer to repurchase all the units or shares held by the investors in the relevant member state—this condition does not apply to closed-ended AIFs or European Long-term Investment Funds (ELTIFs).

For 36 months after such de-notification, the AIFM will not be able to engage in any further pre-marketing of the relevant units or shares or of any 'similar investment strategies or investment ideas' in the relevant member state.

Even after de-notification the AIFM must nonetheless continue to provide investor transparency information (e.g. periodic reports) on an ongoing basis to investors.

WHAT FUND MANAGERS SHOULD BE DOING

Fund managers should monitor the extent to which aspects of the EU regime are 'onshored' into the UK on or following Brexit. They should also look out for any amendments that individual EU member states may make to their national private placement regimes in consequence of some of the changes introduced by the CBD Regulation and Directive.

3 Liquidity stress testing

WHAT IS THIS? New guidelines for carrying out liquidity stress testing on funds.

WHO DOES THIS APPLY TO? AIFMs, UCITS management companies and depositaries.

WHEN DOES THIS APPLY? 30 September 2020.

The European Securities and Markets Authority (**ESMA**) published its final guidelines on liquidity stress testing (**Liquidity Guidelines**).

The Liquidity Guidelines will apply from **30 September 2020** and supplement the existing liquidity management requirements as set out in AIFMD and the UCITS Directive.

They are expressed as applying to AIFMs and UCITS management companies in respect of their UCITS and AIFs, including exchange-traded funds (**ETF**s) (whether the ETF is a UCITS or an AIF) and leveraged closed-ended AIFs. It is unclear from the text and the commentary whether they apply to non-leveraged closed-ended AIFs. A strict reading of the scope section of the Liquidity Guidelines might suggest that they do. However, we note that ESMA reiterated in its Questions and Answers on the application of the AIFMD from December 2019 that Article 16(1) AIFMD exempts closed-ended unleveraged AIFs from implementing liquidity risk management systems and from conducting liquidity stress tests and that therefore the liquidity stress testing reporting requirements are not relevant for AIFMs relying on this exemption. Therefore, it could be argued that, construed purposively in view of the nature of a non-leveraged closed-ended AIF and, based on the ESMA guidance, the Liquidity Guidelines are not relevant to most non-leveraged closed-ended AIFs.

The Liquidity Guidelines also apply on a more limited basis to money market funds (MMFs) and impose a verification obligation on depositaries.

Liquidity stress testing (**LST**) is a risk management tool, within the overall liquidity risk management framework of a manager, which simulates a range of conditions, including normal and stressed conditions, to assess their potential impact on the funding, assets and overall liquidity of a fund and any necessary follow-up actions.

The Liquidity Guidelines include obligations to design and build LST models and to produce an LST policy. They also impose governance principles which require LST to be properly integrated and embedded into a fund's risk management framework and subject to appropriate governance and oversight. LST should employ historical scenarios, hypothetical scenarios and, where appropriate, reverse stress testing. Where appropriate, managers should aggregate LST across funds under management to better ascertain the liquidation cost or time to liquidate each security.

Under the Liquidity Guidelines, LST should occur at least annually but quarterly or more frequent LST is recommended.

Depositaries must have appropriate verification procedures to check that fund managers have documented LST procedures in place.

4 PRIIPs Delegated Regulation

WHAT IS THIS? Consultation on possible changes to PRIIPs Key Information Document.

WHO DOES THIS APPLY TO? PRIIPs manufacturers including certain AIFMs and UCITS management companies.

WHEN DOES THIS APPLY? Not yet known; not likely in 2020.

The European Supervisory Authorities (**ESAs**) issued a joint consultation paper on proposed amendments to the Delegated Regulation for Packaged Retail and Insurance-based Investment Products (**PRIIPs**). The consultation closed on 13 January 2020 and the ESAs are expected to submit their final proposals to the European Commission during the **first half of 2020**.

The consultation follows the previous, more targeted, 2018 consultation by the ESAs. Following the 2018 consultation, it was decided to consult on more substantive changes to the Delegated Regulation for PRIIPs. This new consultation is intended to consider two main areas:

- the appropriate application of the Key information Document (**PRIIPs KID**) by UCITS and relevant non-UCITS funds; and
- the main regulatory issues identified since the implementation of the PRIIPs KID.

APPLICATION TO UCITS

The PRIIPs Regulation provides for a temporary exemption for UCITS management companies from the requirement to prepare a PRIIPs KID on the basis that the UCITS key investor information document (**UCITS KIID**) will be given to investors instead. This exemption, which would originally have expired on 31 December 2019, was recently extended until **31 December 2021**.

The consultation considers the potential scenario under which the UCITS KIID is brought within the scope of the PRIIPs regime and asks which UCITS KIID requirements under the UCITS Regulation would need to be included in the PRIIPs KID. Suggestions include the provisions relating to objectives and investment policy, the identification, explanation and presentation of risks and past performance information. The consultation also considers whether some of these provisions would need to be extended to other types of PRIIPs, such as retail AIFs, in order to ensure consistency and a level playing field. If so then this would effectively apply UCITS requirements to certain non-UCITS retail funds.

If the UCITS KIID were brought within the scope of the PRIIPs regime, there remains some uncertainty about how the requirement would apply to professional clients given that a UCITS KIID is required to be provided to both retail and professional clients but a PRIIPs KID is only required for retail clients. The consultation asks for views on whether, in those circumstances, the need for a professional client to receive a UCITS KIID should be reconsidered or whether professional investors in a UCITS should receive a PRIIPs KID.

AMENDMENTS TO THE PRIIPS KID

The consultation also considers some proposed amendments to the PRIIPs KID including the presentation of performance scenario information and whether to include illustrative performance scenarios and past performance information. In addition, the consultation seeks feedback on the calculation and presentation of costs including possible changes to the current costs tables and to the presentation of transaction costs. Finally, the consultation seeks views on the effectiveness of the current approach for multi-option products and, in particular, the option to make use of a generic PRIIPs KID.

5 New Swiss Distribution Regime

WHAT IS THIS? New rules on funds distribution in Switzerland.

WHO DOES THIS APPLY TO? Funds seeking to engage with Swiss investors.

WHEN DOES THIS APPLY? 1 January 2020.

A new set of laws regulating financial services and institutions in Switzerland came into force on 1 January 2020 and have implications for fund distribution in Switzerland. In very broad terms, the changes are likely to be positive for those looking to market their funds into Switzerland for the following reasons:

- if a foreign fund in Switzerland is exclusively offered to qualified investors, then the fund no longer needs to appoint a Swiss representative and a Swiss paying agent provided that the fund is not also offered to high net-worth individuals who have opted to be treated as qualified investors;
- the term "qualified investors" has been broadened;
- the previous concept of "distribution" has been abolished and replaced by the new, narrower concept of "offering".

We have a note setting out more details and which is available on request.

PART C: SUSTAINABILITY

The next few years will see an increased focus on the integration of sustainability and environmental factors into financial services, as regulatory measures are introduced at both at an EU and UK level. This is set against a wider backdrop of global initiatives relating to climate change generally.

In the context of financial services "sustainable finance" generally refers to the process of taking environmental, social and governance (ESG) considerations into account when making investment decisions. The three components break down as follows:

- *Environmental* considerations – these refer to climate change mitigation and adaptations – and to the environment more broadly and the associated risks (such as natural disasters);
- *Social* considerations – these refer to (among others) issues of inequality, inclusiveness, labour relations, investment in human capital and communities; and
- *Governance* considerations – these refer to management structures, employee relations and executive remuneration and their role in ensuring that environmental and social considerations are included in the investment decision-making process.

At an EU level, as part of the European Commission's Sustainable Finance Action Plan, the EU institutions have been working on a range of measures including a new taxonomy or classification system of environmentally sustainable activities, new disclosure requirements relating to sustainable investments and provisions designed to integrate sustainability risks and factors into the way that financial services firms do business and deal with clients.

Firms will need to adapt to having (and evidencing) an increased focus on sustainable finance and responsible investment over the next few years.

Not all these EU initiatives will be effective before the UK has left the EU and the transitional period under the EU Withdrawal Agreement has, as currently envisaged, expired. However, depending on UK policy with regards to implementing EU-derived legislation following Brexit, it is likely that the measures – or something very like them - will have a direct impact on UK firms; and, in any event, the UK is also pursuing its own domestic agenda on these issues.

6 EU Regulation on Sustainability-related Disclosures in the Financial Services Sector

WHAT IS THIS? New rules requiring firms to make disclosures in respect of sustainability.

WHO DOES THIS APPLY TO? Portfolio managers, investment advisers and AIFMs and UCITS management companies.

WHEN DOES THIS APPLY? Majority of the requirements apply from 10 March 2021.

The EU Regulation on sustainability-related disclosures in the financial services sector (**EU Disclosure Regulation**) has been published and is in force. The majority of its provisions are stated as applying from **10 March 2021.** This is despite a request from several trade associations in September 2019 asking for this date to be postponed by at least one year after the relevant Level 2 implementing legislation is published (see below) to allow firms time to prepare.

The EU Disclosure Regulation applies to portfolio managers, AIFMs, UCITS management companies, EuVECA managers and EuSEF managers as well as investment advisers.

The EU Disclosure Regulation is intended to complement the other work being carried out on sustainability including ESMA's work on the integration of sustainability risks and factors into firms' policies and procedures (see below).

The European Supervisory Authorities are required to develop regulatory and implementing technical standards in respect of many of the provisions of the EU Disclsoure Regulation which will, among other things, further specify the details of the presentation and content of the information on sustainability investment targets to be disclosed in pre-contractual documents, periodic reports and on websites.

Some of these technical standards are expected to be published later this year; others are expected to be published in 2021.

Broadly, under the EU Disclosure Regulation firms will be required to make a number of disclosures as follows:

- Disclosures on the firm's website, to include:
    - the firm's written policies about the integration of sustainability risks in its decision making process;
    - a statement on its due diligence policies with respect to the principal adverse impacts of investment decisions on sustainability (or, where the firm has not considered the adverse impacts of investment decisions on sustainabilty, clear reasons for not having done so);
    - for each financial product (e.g. AIF or UCITS) a description of its ESG characteristics – i.e. a description of its environmental or social characteristics or its sustainable investment objective; and
    - certain information required in respect of pre-contractual disclosures and in periodic reports (see below).
- Pre-contractual disclosures of:
    - how sustainability risks are integrated into its investment decisions;
    - the likely impact of sustainability risks on investment returns; and
    - how the firm's remuneration policies take the integration of sustainabilty risks and sustainable investments into account;
- Disclosures in periodic reports that are broadly designed to prevent firms from "greenwashing" (i.e. the holding out of a product as having green or sustainable characteristics where this is not, in fact, the case):
    - where a product seeks to promote environmental or social characteristics, a description of the extent to which these characteristics are obtained; and
    - where a product has certain sustainability objectives, a description of the overall sustainability-related impact of the product (for AIFMs this must be included in the AIFM annual report as required by Article 22 AIFMD).

7 EU - Integration of Sustainability Risks and Factors – MiFID II, AIFMD and UCITS Directive

WHAT IS THIS? Potential changes to MiFID II, AIFMD and the UCITS Directive requiring the integration of sustainability risks and factors into firms' policies and procedures.

WHO DOES THIS APPLY TO? MiFID investment firms (including portfolio managers and adviser/arrangers) and AIFMs and UCITS management companies.

WHEN DOES THIS APPLY? Not yet known; not likely in 2020.

In response to a request from the European Commission for technical advice on potential amendments to, or the introduction of, certain delegated legislation, ESMA consulted on potential amendments to Level 2 measures adopted under AIFMD and the UCITS Directive and also under MiFID II. In May 2019, ESMA issued its two final reports containing its technical advice in respect of potential legislation on the integration of sustainability risks and factors into firms' policies and procedures.

The proposals will apply to AIFMs and UCITS management companies and to MiFID investment firms (including portfolio managers and adviser/arrangers). In some cases, the proposed requirements in respect of the MiFID II Level 2 measures would also apply indirectly to the manufacturers of funds (including non-EEA funds), particularly where making use of an EU distributor which is subject to MIFID II.

Under the proposals, such firms would be required to take sustainability into account when complying with organisational requirements, including (where relevant) risk management, conflicts of interest and product governance requirements.

AIFMs and UCITS management companies would also need to integrate sustainability into the responsibilities of senior management and consider sustainability risks and factors when selecting and monitoring investments and when carrying out investment decisions.

Amendments to the relevant Level 2 measures under AIFMD, the UCITS Directive and MiFID II will follow.

8 EU Taxonomy Regulation

WHAT IS THIS? Rules on a framework to classify environmentally sustainable activities.

WHO DOES THIS APPLY TO? Financial market participants who offer financial products and companies falling under the Non-Financial Reporting Directive.

WHEN DOES THIS APPLY? Partially as from 31 December 2021 with the remainder as from 31 December 2022.

The European Parliament and the Council have reached agreement on the Regulation on the establishment of a framework to facilitate sustainable investment (**Taxonomy Regulation**). This will introduce an EU-wide taxonomy or classification system of environmentally sustainable activities. In other words, it will establish the *framework* criteria for determining whether and to what extent and economic activity can be considered environmentally sustainable.

The Taxonomy Regulation will apply to:

- financial market participants who offer financial products; and
- financial and non-financial undertakings which fall under the Non-Financial Reporting Directive (i.e. which are required to disclose how/to what extent their activities are associated with environmentally sustainable economic activities).

The six environmental objectives underpinning the criteria are as follows:

- climate change mitigation;
- climate change adapation;
- sustainable use and protection of water and marine resources;
- transition to a circular economy;
- pollution prevention and control; and
- protection and restoration of biodiversity and ecosystems.

On 16 December 2019, the European Council and the European Parliament reached political agreement on the Taxonomy Regulation which is now awaiting formal adoption. Parts of the Taxonomy Regulation are currently expected to take effect as from **31 December 2021** with the remainder coming into effect as from **31 December 2022**.

However, as stated above, the Regulation sets out framework criteria and details as to what specific types of economic activities or investments are objectively defined as being environmentally sustainable (the technical screening criteria) will appear in yet-to-be drafted delegated legislation (RTS/ITS). Therefore, the full impact of the Taxonomy Regulation

will only apply once the relevant delegated acts under the Regulation, which will set out the relevant technical screening criteria for each of the six environmental objectives, have been established.

9 UK Green Finance Strategy

WHAT IS THIS? UK government initiative to create a greener financial system.

WHO DOES THIS APPLY TO? Potentially all regulated firms but likely mainly to affect portfolio managers, investment advisers and AIFMs and UCITS management companies.

WHEN DOES THIS APPLY? In progress.

In July 2019, the UK government launched its "Green Finance Strategy" which aims to create a greener financial system which supports cleaner and more environmentally sustainable investment and growth. The government intends that climate and environmental factors be fully integrated into mainstream financial decision-making across all sectors and asset classes.

As part of this, the government has announced a number of measures including the establishment of the Green Finance Institute to collaborate between the private and public sectors with respect to green finance.

The government has also committed at least to match the ambition of the three key objectives of the EU's Sustainable Action Plan:

- to reorient capital flows towards sustainable investment;
- to manage financial risks from climate change by considering environmental and social goals in financial decision-making; and
- to increase transparency in financial products so customers can make informed decisions about their investments.

Finally, the government also stated that it intends to require the PRA and FCA to have regard to the COP21 Paris Agreement when considering their objectives and discharge of their functions and would seek to establish a joint taskforce with UK regulators to ensure a co-ordinated approach on climate related financial issues (including disclosures).

10 FCA Feedback Statement on Climate Change and Green Finance

WHAT IS THIS? FCA's statement on its intention to focus on climate change and green finance in its work.

WHO DOES THIS APPLY TO? FCA authorised firms and issuers.

WHEN DOES THIS APPLY? Not yet known.

The FCA issued in October 2019 a feedback statement following Discussion Paper 18/8 on climate change and green finance.

The FCA stated that it plans to focus on the following three key areas in its work:

- provision of information by issuers on their exposure to material climate change risks and opportunities;
- integration by authorised firms of the consideration of material climate change risks and opportunities into their business, risk and investment decisions; and
- access to consumers of suitable green finance products and services including appropriate information and advice.

In connection with this, the FCA said that it intends to issue, in **early 2020**, a Consultation Paper proposing new climate-related disclosure rules for certain issuers (on a comply or explain basis) and clarifying existing climate change disclosure obligations.

The FCA will also consider whether other types of sustainability disclosures are adequate and also whether other authorised firms should be required to make additional climate-related disclosures. It will also carry out further work on "greenwashing" including policy analysis and, if required, enforcement action. In addition, the FCA will look into the role of firms' culture, governance and leadership in managing climate change.

PART D: GOVERNANCE

11 Senior Managers and Certification Regime – Extension to FCA Solo-regulated Firms

WHAT IS THIS? The regime which replaced the Approved Persons Regime, a calibrated version of the regime which has been applying to UK banks, UK branches of foreign banks, building societies, credit unions and dual-regulated investment firms since March 2016.

WHO DOES THIS APPLY TO? All "solo-regulated" FCA authorised firms (other than pure benchmark administrators) and persons who work in, or hold certain positions in respect of, those firms.

WHEN DOES THIS APPLY? 9 December 2019 (already applies); 9 December 2020 for completion of the initial certification process, training of non-SMCR staff and submission of data for the Directory.

The Senior Managers and Certification Regime (**SMCR**) was extended to all firms authorised under the Financial Services and Markets Act 2000 and subject to solo regulation by the FCA on 9 December 2019. Such firms should now be compliant with the bulk of the regime's requirements. For instance, they must have identified all of their Senior Managers and Certification Staff and ensured that they are trained on the new regime. The Conduct Rules applied to them as from 9 December 2019.

However, there is a one-year transitional period as regards certain aspects of the regime so that firms have until **9 December 2020** at the latest:

- to complete the initial certification process – i.e. to complete their fitness and propriety assessments and issue the first annual certificate in respect of Certification Staff;
- to train all those employees (other than ancillary staff) who are not Senior Managers or Certification Staff, but who are nonetheless within the scope of the Conduct Rules; and
- to upload via Connect all the data about individuals that they are required to provide for the purposes of the FCA's new Directory.

12 Senior Managers and Certification Regime – Extension to pure Benchmark Administrators

WHAT IS THIS? The proposed extension of the SMCR regime to pure benchmark administrators.

WHO DOES THIS APPLY TO? "Pure benchmark administrators" – i.e. firms that do not undertake any regulated activity other than benchmark administration.

WHEN DOES THIS APPLY? 7 December 2020 (subject to consultation).

Although the SMCR regime was extended to FCA solo-regulated firms on 9 December 2019, the Treasury and the FCA agreed that the extension would not apply for the time being to benchmark administrators *that do not undertake any other activities*. (Firms that carry out benchmark administration *together with other regulated activities* were subject to SMCR as of 9 December 2019 alongside other FCA solo-regulated firms.) A "benchmark administrator" is a new category of authorised firm introduced by the EU Benchmark Regulation – i.e. a firm which has authorisation to carry on the regulated activity of administering a specified benchmark.

In November 2019, the FCA published a consultation paper which proposed the extension of the SMCR to "pure benchmark administrators" – i.e. authorised firms that do not undertake any regulated activities other than benchmark administration on **7 December 2020**. Until then, the Approved Persons Regime will continue to apply to such firms.

The SMCR regime, in terms of the senior management functions and prescribed responsibilities, will be calibrated further to take account of the specific nature of the firm's activities. For instance, core or limited scope benchmark administrators will not be subject to the Certification Regime. However, amongst other things, they *will* be required to:

- satisfy themselves at least annually that their senior managers are fit and proper;
- request and provide regulatory references when a Senior Manager moves from one organisation to another;
- have a Statement of Responsibilities for each Senior Manager that clearly sets out the areas they are responsible for;
- train all employees who are subject to the Conduct Rules;
- notify the FCA when they have taken action against a person for breaching a Conduct Rule; and
- undertake criminal records checks when appointing relevant Senior Manager and (for core firms only) non-executive directors.

The closing date for feedback on the proposals is **28 February 2020**.

13 Senior Managers and Certification Regime – Extension to FMI Institutions?

WHAT IS THIS? A recommendation within a report from the House of Commons Treasury Committee on IT failures in the Financial Services Sector.

WHO DOES THIS APPLY TO? FMI firms supervised by the Bank of England (in terms of the specific SMCR recommendation; other aspects of the report deal more broadly with IT failures and operational risk within the wider financial services sector).

WHEN DOES THIS APPLY? Not yet specified; not expected in 2020.

The SMCR regime does not currently apply to Financial Markets Infrastructure (**FMI**) institutions – i.e. payment systems, central securities depositaries, securities settlement systems, central counterparties and trade repositories.

However, in its report IT failures in the Financial Services Sector (Second Report of Session 2019-20), the House of Commons Treasury Committee recommended that the regime should be extended to include FMI firms supervised by the Bank of England so as to ensure that senior individuals within those firms are accountable.

14 UK Stewardship Code

WHAT IS THIS? Changes to the Stewardship Code including a broader scope and stricter reporting and governance requirements.

WHO DOES THIS APPLY TO? Firms which comply with the Stewardship Code.

WHEN DOES THIS APPLY? 1 January 2020 (already applies).

The Financial Reporting Council's revised Stewardship Code took effect on **1 January 2020**.

Key changes included the extension of the stewardship principles beyond UK listed equities to all types of assets including bonds, private equity holdings and infrastructure investments as well as the inclusion of environmental, social and governance factors when fulfilling stewardship responsibilities.

The revised Stewardship Code also includes more rigorous reporting requirements and enhanced governance requirements.

The approach taken by the FCA to the Stewardship Code in its rules has not changed, and non-venture capital firms which manage investment for professional clients (which are not natural persons) must continue either to comply to with the Stewardship Code or explain their alternative investment strategy. However, firms which "explain" rather than "comply" should ensure that their explanation of their alternative investment strategy continues to comply with the FCA's rules. In particular, any explanation that a firm does not comply with the Stewardship Code on the basis that it only invests in non-equities is likely to have to be revised given that the Stewardship Code now covers all types of assets.

The Financial Reporting Council is expected to publish a list of the first signatories to the revised Stewardship Code during the course of 2021.

15 ESMA Compliance Function Guidelines

WHAT IS THIS? ESMA consultation on changes to its guidelines on the MiFID II compliance function.

WHO DOES THIS APPLY TO? MiFID firms and AIFMs providing MiFID investment services.

WHEN DOES THIS APPLY? ESMA aims to publish the final guidelines in Q2 2020 – date of application currently unclear.

In July 2019 ESMA issued a consultation paper on an update to its guidelines on the MiFID II compliance function (**Compliance Guidelines**) first published in 2012. The consultation closed in October 2019 and the final Compliance Guidelines are expected to be issued in the **second quarter of 2020**.

These apply to MiFID firms and to AIFMs when providing MiFID investment services under their MiFID "top-up" permission. They are also now expressed to apply to product governance arrangements.

The consultation draft builds on and reorders the existing Compliance Guidelines but also includes some new and supplemental requirements. For instance, under the proposed Compliance Guidelines, *all* compliance staff (not just the compliance officer) should have appropriate skills, knowledge and expertise and the compliance officer must demonstrate high professional ethical standards and personal integrity. The firm's compliance culture should also be supported by senior management. If appropriate and subject to proportionality, firms should consider having a core team focussing solely on MiFID II compliance.

The proposed Compliance Guidelines also state that firms should put in place arrangements for an effective exchange of information between the compliance function and other functions e.g. auditors or risk management.

16 EuVECA Delegated Regulation on Conflicts of Interest

WHAT IS THIS? New rules on identifying, preventing and managing conflicts of interest.

WHO DOES THIS APPLY TO? European venture capital funds.

WHEN DOES THIS APPLY? 11 December 2019 (already applies).

The Delegated Regulation on conflicts of interest applicable to European venture capital funds (**EuVECA**) came into force on **11 December 2019**.

This Delegated Regulation includes guidance on what constitutes a conflict of interest; a requirement for managers of EuVECA to establish, implement and maintain a written conflicts of interest policy, and a requirement to take steps to prevent and manage conflicts of interest.

Managers of EuVECA must also develop strategies for determining when and how to exercise voting rights held in the portfolio for the benefit of both the EuVECA and its investors. These must include the monitoring of corporate actions, ensuring that the exercise of voting rights is in accordance with the investment objectives and policy of the fund, and prevention and management of any conflicts of interest arising from the exercise of those voting rights. Investors must also be provided with a summary description of those strategies and the details of any resulting actions taken.

17 FCA Guidance on LIBOR transition

WHAT IS THIS? FCA guidance on how firms should manage transitioning away from LIBOR.

WHO DOES THIS APPLY TO? FCA authorised firms whose financial products or other financial arrangements are referenced to LIBOR – including asset managers.

WHEN DOES THIS APPLY? Now.

The interest rate benchmark LIBOR is expected to cease after the end of 2021 – this is when the voluntary agreement of panel banks to continue to submit to LIBOR ends. The FCA expects firms to take appropriate steps to ensure they can transition to suitable alternative interest rate benchmarks (such as the "Sterling Overnight Index Average Rate" or "SONIA") ahead of that date.

MANAGING THE TRANSITION

On 19 November 2019, the FCA provided some guidance on its expectations for firms on managing the transition away from LIBOR (the London Inter-Bank Offered Rate). The short page links to a longer document setting out Q&As about conduct risk during LIBOR transition.

The FCA considers that firms' senior managers and boards should understand the risks associated with the transition away from LIBOR and take appropriate action to move to alternative rates ahead of the end of 2021. Where appropriate, firms subject to the FCA's Senior Managers & Certification Regime that are impacted by LIBOR transition should identify the Senior Manager responsible for overseeing transition away from LIBOR and detail those responsibilities in the relevant Senior Manager's Statement of Responsibilities. Firms should also consider whether LIBOR–related risks need a separate, dedicated risk framework.

The FCA notes that firms will need to amend contracts (where possible) for LIBOR-linked products that mature beyond the end of 2021. In doing so, firms must ensure that any replacement rate is fair and should not be used as a way to adopt higher rates or inferior terms. The FCA indicates that a replacement rate is more likely to be considered to be fair if it is one adopted as a suitable replacement within the market or industry.

The FCA also recommends that firms seek to avoid new LIBOR-linked products which mature after the end of 2021.

APPLICATION TO ASSET MANAGERS

The FCA emphasises that LIBOR transition is not just an issue for banks and insurers. "Buy-side" firms, such as asset managers, should be preparing for LIBOR transition too since their clients may have exposure to LIBOR within a fund or through the firm's portfolio management activities. Asset managers will therefore have to look at investing in instruments linked to alternative risk-free rates (**RFRs**) and actively engaging with issuers of securities and derivative and loan counterparties to get LIBOR-linked instruments and products switched to an RFR or other alternative rates. Asset managers are therefore expected to take steps to:

- identify the extent of exposure they and their clients have because of instruments within their asset portfolios that are linked to LIBOR; and
- consider how they are going to manage the impact of transition in the advance of LIBOR discontinuance, including the impact on contract continuity, interest rates and falling liquidity.

18 EU Whistleblowing Directive

WHAT IS THIS? New EU directive granting protection against retaliation to persons who report breaches of EU law using certain specified channels.

WHO DOES THIS APPLY TO? All persons including legal entities.

WHEN DOES THIS APPLY? 17 December 2021.

The Directive on the protection of persons who report breaches of EU law (**Whistleblowing Directive**) has been published in the Official Journal. EU member states are required to transpose the directive by **17 December 2021**.

The Whistleblowing Directive applies to persons who acquired information on a relevant breach in a work-related context (including self-employed workers, shareholders and members of management or supervisory bodies) and properly make a report of that breach.

Relevant breaches for these purposes are breaches of those areas of EU law set out in the Whistleblowing Directive which include laws relating to financial services, products and markets and the prevention of money laundering or terrorist financing as well as data protection law. "Information on breaches" is not limited to actual, past breaches but also includes potential breaches and reasonable suspicions of breaches.

The Whistleblowing Directive prohibits any retaliation against persons who make such reports, including in the form of dismissal, unfair treatment and blacklisting.

In order to benefit from protection, such persons must have reasonable grounds to believe that the information on breaches reported was true at the time of reporting and that such information fell within the scope of the Whistleblowing Directive. They must also have made the report in one of three ways:

- through internal reporting channels and procedures of the relevant entity;
- through designated external official reporting channels; or
- in certain limited cases only, by way of public disclosure.

In addition, legal entities must establish channels to enable workers to make internal reports and comply with certain follow-up and other internal procedure requirements. For non-financial services private sector firms, this applies to entities with 50 or more employees but for firms carrying on EU regulated financial services activities, this applies to all such firms.

19 FCA's Asset Management and Alternatives Supervision Strategies – Dear CEO letter

WHAT IS THIS? Dear CEO letter: FCA expectations for asset managers and alternative investment firms to address the key risks of harm to their customers and the markets.

WHO DOES THIS APPLY TO? Asset managers including those managing or advising on alternative assets and/or alternative investment vehicles.

WHEN DOES THIS APPLY? Now.

The FCA has written to Chief Executives of both asset managers and also alternative investment firms setting out its view on the key risks of harm that such firms pose to their customers and the markets more generally. The FCA defines "alternative investment firms" as firms managing or advising on alternative assets and/or alternative investment vehicles (such as hedge, credit or private equity funds). Asset managers include FCA authorised firms which directly manage or advise on mainstream investments, particularly retail investments.

In the two letters, the FCA has also set out some priorities on which it expects asset managers and alternative investment firms to focus in order to address such risks. While none of these measures is new, firms should consider their current practices and procedures in light of the FCA's comments and assess whether any improvements should be made.

The FCA states that the overall standards of governance of alternative investment firms and asset managers (especially at regulated entity level) generally fall below its expectations.

The FCA warns that it may carry out visits to such firms to assess their compliance with the FCA's rules and other legislation and that firms may also be required to take part in related work by the FCA. The FCA has specifically identified some areas where it will be contacting or visiting firms.

We summarise the FCA's key comments below.

ALTERNATIVES ASSET MANAGEMENT SUPERVISION STRATEGY

Suitability, appropriateness and client money

Firms which offer products or manage investments with exposures to alternative assets and strategies should consider the appropriateness or suitability of those investments for their target investors. In particular, firms should make sure that they identify the client type and investment need when manufacturing or distributing products (bearing in mind that certain products may only be suitable for a niche market). We assume that this refers to the product governance rules and so, in relation to distributors, would apply only to target investors which are the firm's clients.

Firms should also ensure that any decision to opt-up investors to elective professional status is done on the basis of a robust assessment (for both clients and non-client investors).

The FCA intends to review retail exposure to alternative investments. It will test whether firms are aware of who their customers are and that they are placing a clear focus on acting in the best interests of their clients and funds. In addition, the FCA will be looking to assess whether firms have taken reasonable steps to ensure that investors adequately understand the risks of their investments and are not exposed to products outside the scope of their risk profiles. As part of the retail investor review, FCA will also look at client money and asset controls within firms.

Market abuse

The FCA observed that market abuse controls across the sector "have significant scope for improvement".

Firms are required to make sure that their market abuse controls are sufficient to enable them to discharge their obligations under the Market Abuse Regulation and that they are sufficiently comprehensive and tailored to the firms' business models. The FCA sent a market abuse questionnaire to asset managers in 2018, followed by a number of firm visits. The FCA may include alternatives firms in future questionnaires.

Market integrity and disruption

Firms must operate robust risk management controls to avoid excessive risk taking and to ensure that the potential for harm or disruption to financial markets is appropriately mitigated. In particular, firms adopting very high-risk investment strategies, particularly those employing significant leverage, should have appropriately high-quality risk management controls and may be subject to FCA review.

Financial crime

Firms should be alert to the risk that they may be used to facilitate financial crime and have appropriate and proportionate systems and controls. Of particular importance are due diligence on third parties and know your client (KYC) checks. The FCA intends to review firms' systems and controls in this area, paying particular attention to money laundering and terrorist financing.

BREXIT

For both asset managers and alternative investment firms, the FCA expects firms to consider how the end of the implementation period following the UK's withdrawal from the EU will affect firms and their customers and what action they will need to take to be ready for 1 January 2021.

ASSET MANAGEMENT SUPERVISION STRATEGY

Liquidity management

The FCA confirms that effective liquidity management in funds is a central responsibility for authorised fund managers, even where investment management is delegated to a third party.

The FCA also expects firms to take any necessary or appropriate action in light of PS19/24 on illiquid assets and open-ended funds, its letter of 4 November 2019 to the boards of AFMs outlining its expectations regarding liquidity management and the FCA and the Bank of England's joint review of liquidity risks in open-ended investment funds.

Firms' governance

Firms should ensure that their boards engage in robust discussion and challenge around important business decisions, without undue reliance on group structures. In addition, firms should recognise and take steps to mitigate harm arising from any conflicts of interest between affiliates, notably between an authorised fund manager and any delegate investment manager.

Firms should have refreshed and improved their approach to governance in line with SMCR including through clear lines of accountability and responsibility for senior management functions (SMFs). The FCA will review firms' governance and SMCR implementation in the first half of 2020.

Asset Management Market Study

Following the Asset Management Market Study, fund managers should carry out value assessments on their authorised funds. The FCA will review firms' work in this area in the first half of 2020. Funds' objectives should also be clear, fair, not misleading and comply with new rules around objectives disclosure.

Governing bodies of managers of authorised funds should also ensure that they have at least one quarter (and no fewer than two) independent members. The FCA will look to see evidence of meaningful challenge by the independent members including on costs, fees and product design.

Product governance

Firms subject to product governance requirements should ensure that products are designed with the best interests of a specified target market in mind and do not include features that are manifestly not in the interests of customers (e.g. funds tracking an undisclosed index or where fees exceed target returns). The FCA is currently reviewing firms' compliance.

Where authorised funds are managed by fund managers which are not in the same group as the investment manager (including host ACDs), the FCA has concerns that such fund managers may not be carrying out their responsibilities properly, particularly in respect of conflicts. The FCA is undertaking a further review of these types of arrangements.

LIBOR transition

Firms should also aware of their responsibility to ensure an effective transition away from LIBOR and should be planning on the basis that LIBOR will cease from the start of 2022.

Operational resilience

Firms should manage their technology and cyber risk appropriately, including through appropriate oversight of third party firms and intra-group service providers, taking into account the FCA's review of technology resilience for asset managers. The FCA may also carry out proactive technology reviews on firms which have a greater risk of causing harm.

20 Changes to firms' details

WHAT IS THIS? Requirement for firms to verify their firm details annually within 60 business days of their Accounting Reference Date.

WHO DOES THIS APPLY TO? All firms other than other than ICVCs, certain EEA AIFMs marketing in the UK and managers of certain non-UK funds.

WHEN DOES THIS APPLY? 31 January 2020.

From 31 January 2020, firms subject to the reporting requirements under SUP 16.10 of the FCA's Handbook will be required to check, amend and/or confirm the accuracy of their firm details on an annual basis. Firms will be required to verify and confirm that the details remain correct even where there have been no changes over the previous year.

Broadly, SUP 16.10 applies to all firms other than ICVCs, EEA AIFMs marketing in the UK (but not managing a UK AIF) under an EEA passport and managers of certain non-UK funds. The details to be verified include the firms' contact details and corporate information.

This must be done within 60 business days of their Accounting Reference Date (previously the requirement was within 30 business days) by way of the FCA's Connect system.

PART E: FINANCIAL CRIME AND MARKET ABUSE

21 EU Fifth Money Laundering Directive and UK Money Laundering Regulations

WHAT IS THIS? Directive amending MLD4 and implemented in the UK by amendments to the UK Money Laundering Regulations 2017.

WHO DOES THIS APPLY TO? All credit institutions, financial institutions, professional advisers, trust or company service providers, estate agents, high value dealers, casinos.

WHEN DOES THIS APPLY? 10 January 2020 (applies now).

The Fifth Money Laundering Directive (**MLD 5**) applied as from 10 January 2020 and was implemented in the UK by way of the Money Laundering and Terrorist Financing (Amendment) Regulations 2019 which amend the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the **MLRs**).

The main changes reflected in the amendments to the MLRs are as follows:

- There are stricter requirements when carrying out customer due diligence; including requirements to obtain and verify additional information when carrying out customer due diligence on a body corporate and to understand the business, ownership and control structure of their customers, however constituted.
- There are a new set of prescribed enhanced due diligence measures that firms will be required to carry out in relation to new business relationships or transactions involving high risk third countries (i.e. countries which have been identified by the European Commission as high risk third countries). These include obtaining additional information on the customer and its beneficial owner, the intended nature of the business relationship and obtaining the approval of senior management for establishing or continuing the business relationship.
- Where the customer appears on a beneficial ownership register (e.g. the UK PSC Register) relevant firms are required to collect proof of such registration or an excerpt of the register and to report to a relevant person (e.g. the registrar of companies) any discrepancies they discover between the information they hold and the information that appears on the register.
- Where the firm is part of a group, it is already required to establish and maintain policies, controls and procedures throughout the group for data protection and the sharing of information; however, the amended MLRs require firms to have to have policies requiring customer, account and transaction information to be provided to them from their branches and subsidiaries.
- There is clarification of the circumstances in which firms will be required to refresh customer due diligence on existing customers – broadly this will be when the firm has any legal duty to contact the customer for the purpose of reviewing any information which is relevant to the firm's assessment for that customer and which relates to the beneficial ownership of the customer and/or when the firm is required to contact the customer in order to fulfil any duty under the International Tax Compliance Regulations 2015.
- Certain cryptoasset activities are brought within scope.

We discussed the changes in more detail in the following briefings: MLD 5: the MLD 4 upgrade and MLD 5: HMT consultation on UK transposition.

In terms of cryptoassets, on 10 January 2020 the FCA became the AML/CTF supervisor for businesses carrying on certain cryptoassets activities. Cryptoasset activity covers:

- cryptoasset exchange providers – including cryptoasset ATM providers, Peer to Peer providers, and issuers of new cryptoassets (e.g. by way of initial coin offerings or initial exchange offerings); and
- custodian wallet providers – i.e. firms which provide services to safeguard cryptoassets on behalf of clients or private cryptographic keys.

Any new businesses wanting to carry out cryptoasset activity within the scope of the MLRs must be registered with the FCA *before* conducting business – registration forms are available on Connect. All existing businesses that were

conducting cryptoasset ativity before 10 January 2020 are permitted to carry on their business but must ensure their compliance with the MLRs from that date. They will be required to be registered by 10 January 2021, but in order to meet this deadline the FCA requires them to have submitted a completed application for registration via Connect by **30 June 2020**.

The amendments to the MLRs which came into force on 10 January 2020 did not take account of the MLD 5 requirement that all express trusts should be registered, regardless of whether they generate tax consequences. This matter was postponed to allow for a technical consultation on MLD 5 and the UK Trust Registration Service which was launched by HM Revenue & Customs and H.M. Treasury on 24 January 2020. In this consultation, which is open until **21 February 2020**, it is proposed that certain types of express trust should be excluded from the registration requirement. These include:

- statutory trusts;
- express trusts established in a specific form to meet the conditions of legislation (e.g. to meet qualifying conditions for beneficial tax treatment), such as approved share option and profit-sharing schemes;
- trusts which are registered pension schemes for the purposes of Part 4 of the Finance Act 2004; and
- trusts arising out of, or in connection with, a provision of a subscription agreement under which bonds are, or are to be, issued to: an authorised person, subscribers procured by an authorised person or a subscriber through a central securities depositary which is authorised under Article 16 EU Central Securities Depositories Regulation (**CSDR**) (or which has made an application for authorisation pursuant to Article 17 CSDR that has not been determined).

The consultation invites respondents to provide examples of other types of express trust that should be exempt from registration.

On 23 December 2019 the FCA published a webpage highlighting some specific new areas that firms will need to comply with under the amended MLRs. Given that the amending statutory instrument was published only three weeks before the date on which the changes to the MLRs were due to come into force, the FCA expressed a limited degree of regulatory forbearance:

"We expect firms to comply with the new, amended regulations from 10 January 2020. In assessing our approach to firms that may not be compliant on that date, we will take into account evidence that they have taken sufficient steps before that date to comply with these new obligations."

In the light of the FCA's comments, firms should prioritise the finalisation of updates to their policies and procedures so that they are able to show evidence of significant progress.

22 Review of the EU Market Abuse Regulation

WHAT IS THIS? Review discussing potential changes to the Market Abuse Regulation including extending its scope to include spot FX, clarification of its application to funds and amendments to the provisions regarding inside information and PDMRs.

WHO DOES THIS APPLY TO? All persons but particularly persons dealing in spot FX, issuers, funds and PDMRs.

WHEN DOES THIS APPLY? Not yet known – the review is ongoing and the scope any changes, and the date of their application, is yet to be finalised. Not expected to apply in 2020.

Under the EU Market Abuse Regulation (**MAR**), the European Commission is required to present a report assessing various provisions of MAR. As part of this, the European Commission made a request to ESMA for technical advice and ESMA issued a consultation which closed on 29 November 2019. ESMA's final report is expected to be submitted in **Spring 2020**.

The areas covered by the consultation include the topics mandated by MAR as well as some additional topics raised by the European Commission and ESMA.

SPOT FX

One of the most significant topics included in the consultation is whether spot FX should be included in the scope of MAR. This was not one of the areas on which the European Commission was required to opine under MAR but the European Commission thought that this should be considered in light of the size of the spot FX market.

ESMA identifies a number of arguments in favour of the inclusion of spot FX contracts within the scope of MAR. However, ESMA also considers that it might be advisable to wait for the review of the FX Global Code of Conduct and that there would be significant practical difficulties in accomodating spot FX within the MAR regime. In particular, ESMA identifies practical difficulties around the application of MAR concepts to the FX market (such as surveillance and reporting requirements) and the fact that it is predominantly an OTC market.

INSIDE INFORMATION

One of the areas to be considered by the European Commission is whether the definition of inside information is sufficient to combat market abuse. In connection with this, ESMA is consulting on three specific areas: inside information for commodity derivatives, inside information with respect to front-running and pre-hedging.

In respect of commodity derivatives, ESMA is consulting on whether it is appropriate or necessary that, in addition to the standard criteria for inside information, information on commodity derivatives should meet a further criterion of being expected or required to be disclosed in order to be caught by MAR. As regards front-running, ESMA discusses whether the current description of front-running is sufficiently wide or whether it should include, for example, any persons who are aware of a future relevant order and not just those charged with the execution of that order.

The consultation also addresses the delayed disclosure of inside information. In particular, ESMA notes the divergence in approaches taken within different member states and also considers whether MAR should be amended to include a requirement for issuers to establish and maintain effective arrangements, systems and procedures for the identification, handling and disclosure of inside information.

Clarification of the market sounding regime is also covered in the consultation. In particular, ESMA discusses clarifying that persons must comply with the market sounding requirements in MAR in order to be protected against allegations of the unlawful disclosure of inside information and asks whether certain categories of transactions should be excluded. The consultation also considers the simplification of the market sounding procedures.

Finally, ESMA also addresses potential amendments to insider list obligations including whether insider lists should more precisely indicate persons who have actually accessed inside information (which could be a significant change to current requirements for some firms), whether the requirement to maintain an insider list should be expanded e.g. to include auditors and notaries and the role of the permanent insider section in the insider list.

Given the potential for operational impact in changing the market sounding and insider lists regimes, firms should monitor developments in this area.

PERSONS DISCHARGING MANAGEMENT RESPONSIBILITIES

In the case of persons discharging management responsibilities (**PDMRs**), ESMA consulted on whether the threshold for the notification obligation, in respect of transactions in shares or debt instruments of the issuer or related investments, is too low at €5,000 (or €20,000 if increased by the relevant regulator) and should be made higher to avoid undue administrative burden. ESMA also asks for views on the separate 20% threshold where the related investments are unit or shares in a collective investment undertaking (or provide exposure to a portfolio of assets in either case where the relevant exposure does not exceed 20%).

The consultation also addresses the prohibition on trading by PDMRs during closed periods (broadly the period of 30 calendar days before any interim financial report or year-end report which the issuer is required to make public). In particular, ESMA asks whether clarifications are needed to the regime, whether the closed period restrictions should be extended to apply to the issuer and to persons closely associated with the PDMRs and whether any further exemptions are needed.

COLLECTIVE INVESTMENT UNDERTAKINGS

Following clarification that MAR can apply, in certain cases, to collective investment undertakings, ESMA discusses whether amendments are required to MAR to include (or explicitly exclude) such entities.

If included, clarification may be needed around the application of the PDMR obligations to collective investment undertakings and their managers and other relevant persons as well as the identity of the person responsible for the

disclosure of inside information (particularly for collective investment undertakings without legal personality) and the application of the insider list obligations.

OTHER TOPICS

The review also addresses the application of the benchmark provisions and modification of the reporting obligation for buy-back programmes as well as the establishment of an EU framework for cross-market order book surveillance and common administrative sanctions.

PART F: TRADING

23 Securitisation Repositories

WHAT IS THIS? New rules on operational standards for securitisation repositories and the information required in applications for registration as a securitisation repository.

WHO DOES THIS APPLY TO? Originators and sponsors of securitisations, securitisation special purpose entities and persons seeking to become securitisation repositories.

WHEN DOES THIS APPLY? Expected Spring 2020.

In November 2019, the European Commission adopted two delegated regulations supplementing the Securitisation Regulation. The first delegated regulation (and annex) sets out operational standards for securitisation repositories particularly in respect of data collection. The second delegated regulation specifies the information required from securitisation repositories in their application for registration.

Under the Securitisation Regulation, the originators, sponsors or securitisation special purpose entities (**SSPEs**) of a securitisation are required to make certain specified information on the securitisation available to holders of a securitisation position, the competent authorities and, upon request, potential investors. This information must be made available by way of a securitisation repositary (broadly an entity, registered with ESMA and meeting certain standards, which centrally collects and maintains the records of securitisations) or, if there is no registered securitisation repository, by means of a website which meets certain conditions.

As it happens, there are no securitisation repositories currently and therefore the originators, sponsors or SSPEs of securitisations are having to make the required information available through a website as required.

The delegated regulations now need to be considered by the European Parliament and the Council who have three months to endorse the standards in them. The delegated regulations are therefore expected to come into force in **Spring 2020**. Once in force, ESMA will be able to receive and assess applications for registration as a securitisation repository. ESMA has up to 60 days to assess applications.

The delegated regulations are a further step towards the establishment of registered securitisation repositories. Once one or more securitisation repositories are registered then the originators, sponsors or SSPEs of securitisations will need to enter into arrangements for the reporting of information with at least one of those registered securitisation repositories. Firms should therefore ensure that they are in a position to do so.

24 EMIR 2.1 – Expanded Definition of "financial counterparty"

WHAT IS THIS? Amendments to EMIR which, among other things, expand the scope of AIFs that are classified as financial counterparties or deemed financial counterparties and introduce a sub-classification of financial counterparties in FC+s and FC-s.

WHO DOES THIS APPLY TO? AIFs and their AIFMs.

WHEN DOES THIS APPLY? 17 June 2019.

On 17 June 2019, an amendment to the European Market Infrastructure Regulation (**EMIR**), known as "**EMIR 2.1**" came into force. Amongst other things, this expanded the scope of AIFs that are classified as financial counterparties (**FCs**). As before, EEA or non-EEA AIFs whose manager is authorised under AIFMD remain FCs. However, in addition:

- EEA AIFs whose manager is not authorised under AIFMD were previously non-financial counterparties (**NFCs**) but under EMIR 2.1 are now FCs.
- Non-EEA AIFs managed by a non-EEA manager were previously "*deemed* NFCs", but under EMIR 2.1 are now "deemed FCs" when facing EEA brokers/banks as counterparties.

The key implication of the reclassification of certain AIFs as FCs (or deemed FCs) is that FCs and deemed FCs are required to exchange collateral as margin in respect of most uncleared derivatives transactions on a daily basis and, depending on the product, to clear certain types of derivatives transactions.

The introduction of a new category of "small FCs" (**FC-s**) provided a derogation from the mandatory clearing obligation (but not the margin requirements) for some AIFs.

We summarised the changes in the legal briefing from our Derivatives & Structured Products Group at the end of May 2019.

25 MiFIR Derivatives Trading Obligation – ESMA consultation

WHAT IS THIS? Consultation on whether the application of the OTC derivatives trading obligation under MiFID should be aligned with the clearing obligation under EMIR (as amended by EMIR 2.1).

WHO DOES THIS APPLY TO? Small financial counterparties (FC-s).

WHEN DOES THIS APPLY? Not yet known – ESMA's report is expected by 18 May 2020 and the European Commission is required to report to the European Parliament and Council by 18 December 2020.

On 4 October 2019, ESMA published a consultation paper which considered whether the OTC derivatives trading obligation under MiFIR should be aligned with the changes recently made in EMIR 2.1. The consultation closed on 22 November 2019.

Because of the changes made by EMIR 2.1 there is now a misalignment between the types of counterparties subject to the mandatory clearing obligation under EMIR and those subject to the OTC derivatives trading obligation under MiFIR. EMIR 2.1 introduced an exemption to the clearing obligation for a new sub-categorisation of "small financial counterparties" – i.e. financial counterparties whose open positions in OTC derivatives do not exceed the relevant clearing thresholds (FC-s). However, corresponding amendments were not made to MiFIR which still refers to "financial counterparties" as defined in EMIR but does not recognise the sub-categorisation into FC+s and FC-s.

As a result of the misalignment, small FCs which fall outside the scope of the EMIR clearing obligation will technically continue to be subject to the OTC derivatives trading obligation under MiFIR where relevant. EMIR 2.1 did provide that the European Commission should look into the issue and report back to the European Parliament and the Council. The ESMA consultation is part of that review process and, following the feedback, ESMA will report to the European Commission in preparation for the delivery of its own report.

EMIR 2.1 also modified the mechanism by which NFCs above the clearing threshold become subject to the clearing obligation. Previously, if an NFC exceeded the clearing threshold in any of the relevant derivative classes it would become subject to the mandatory clearing obligation in respect of *all* other specified classes (NFC+) even in respect of those where its trading was below the relevant threshold. Now, NFCs are generally only subject to the clearing obligation in respect of those asset classes where their trading has exceeded the clearing threshold. However, the relevant provision in MiFIR no longer cross-refers to the relevant provision in EMIR, as amended, which reflects this, resulting in some uncertainty as to which NFCs are caught by the derivatives trading obligation.

As an interim measure, ESMA issued a statement advising regulators not to prioritise enforcement action against counterparties which are technically subject to the MiFIR derivatives trading obligation but which, as a result of the EMIR 2.1 amendments, fall outside the scope of the EMIR clearing obligation.

ESMA's report is expected by 18 May 2020. EMIR 2.1 requires the European Commission to report to the European Parliament and the Council by 18 December 2020. Any consequential legislative amendments will therefore not be forthcoming until 2021 at the earliest.

26 SFTR Reporting

WHAT IS THIS? Obligations to report details of securities financing transactions to a trade repository come into force for remainder of FCs and for NFCs.

WHO DOES THIS APPLY TO? AIFs, UCITS and other FCs not yet subject to reporting obligation. Also NFCs.

WHEN DOES THIS APPLY? 11 October 2020 for FCs and 11 January 2021 for NFCs.

The EU Securities Financing Transactions Regulation (**SFTR**) has applied from 12 January 2016, although certain requirements entered into force on a phased basis. The final set of substantive obligations under the SFTR that have not yet entered into force are those which relate to the requirement for counterparties to securities financing transactions (**SFTs**) to report details of those transactions to a trade repository. Note that this is a requirement that applies to the principals to a SFT trade and is different in this respect to, for example, the FCA's transaction reporting regime. Legislation has finally been published meaning that such reporting obligations will commence on a staggered basis over the next year depending on the type of institution. The commencement dates are as follows:

- 11 April 2020 – credit institutions (such as banks) and investment firms;
- 11 July 2020 – central securities depositaries (**CSDs**) and central counterparties (**CCPs**);
- 11 October 2020 – all other FCs – this includes AIFs and UCITS; and
- 11 January 2021 – NFCs (such as listed and unlisted corporates).

This means that affected firms will have to use the next few months to finalise their preparations so that they are ready to report their SFTs by the relevant start date: this will include having to establish internal procedures and relevant external legal arrangements (regarding, amongst other things, the collection of data and its onward transmission to a trade repository (or to a third party service provider who will report on their behalf)).

Points to note with regards to the reporting obligation include:

- In terms of territorial scope, and put broadly, the reporting requirement will apply:
    - to the principal counterparty to the transaction where it is established in the EEA (subject to the below);
    - to an EEA branch of a non-EEA entity where the transaction is concluded through the branch; and
    - *according to ESMA*, to a non-EEA AIF with an AIFM registered or authorised under AIFMD (i.e. regardless of the fact that the AIF is established outside the EEA). However, this was a passing comment from ESMA in its Final Report which accompanied its Guidelines on reporting under Articles 4 and 12 SFTR published on 6 January 2020; but this comment was not reflected in the Guidelines themselves nor does it appear to be consistent with the provisions of SFTR itself and trade associations have made representations to that effect.
- A reporting counterparty may appoint a third-party service provider as its delegate to report on its behalf or some firms may be able to rely on "delegated reporting" services provided by their SFT dealers (although the reporting counterparty will remain responsible and legally liable).
- Reportable SFTs will include repos, securities and commodities lending transactions/securities and commodities borrowing transactions, buy-sell backs and sell-buy backs and margin lending transactions. Note that the definition of "margin lending transaction" has been helpfully clarified in a recital to the delegated legislation fleshing out the specifics of the SFTR reporting obligations.

27 Credit Servicers Directive

WHAT IS THIS? New EU regime in respect of credit servicing activities and purchasing credit agreements.

WHO DOES THIS APPLY TO? Persons carrying on credit servicing activities and credit purchasers.

WHEN DOES THIS APPLY? Not expected to be during 2020.

The EU's proposed Directive on credit servicers and credit purchasers (**Credit Servicers Directive**) was originally proposed in 2018 and continued its journey through the EU legislative process in 2019 with a number of revised proposals.

The Credit Servicers Directive provides for a new regime for persons carrying on credit servicing activities, including administering and enforcing loans on behalf of a creditor (but possibly capturing a broader range of activities beyond this). The new regime includes a requirement to seek authorisation, contractual requirements, additional record keeping and outsourcing obligations as well as a cross-border "passporting" regime. New requirements are also proposed for the purchasers of credit agreements including information and notification obligations. The original version of the Credit Servicers Directive also provided for an accelerated extra-judicial collateral enforcement procedure; this has now been removed under the revised proposals.

The revised proposals also propose a narrowing of the scope of application of the Credit Servicers Directive. In particular, it has been proposed that AIFMs, UCITS management companies and MiFID investment firms which are carrying on credit servicing activities be exempted.

Further negotiations (and lobbying by trade associations) on the Credit Servicers Directive are expected during 2020. As the Credit Servicers Directive is anticipated to come into force post-Brexit, it is not yet clear whether it would be implemented in the UK but current indications are that it may not be. We discussed the original proposals in more detail in our 2019 New Year briefing.

PART G: FINANCIAL MARKETS INFRASTRUCTURE

28 EU Central Securities Depositories Regulation – Settlement Discipline Regime

WHAT IS THIS? The introduction of the settlement discipline regime as provided for by the **CSDR**.

WHO DOES THIS APPLY TO? CSDs, CCPs and parties in the settlement chain.

WHEN DOES THIS APPLY? 13 September 2020.

As we have previously reported, CSDR, the Regulation on improving securities settlement in the European Union and on central depositories (Regulation (EU) No 909/2014), came into force on 17 September 2014 and has been subject to a lengthy process of phased, piecemeal implementation over a number of years with some measures still yet to come into force. For instance, the mandatory dematerialisation of newly-issued securities will not enter into force until January 2023, while the mandatory dematerialisation of existing securities will come into force two years later in January 2025. The introduction of the settlement discipline regime established by CSDR takes place this year (see below).

By way of reminder, the CSDR broadly divides into two parts:

- The first part addresses the process of securities settlement and applies broadly to market particpants and so-called "settlement internalisers" (as defined in Article 2(11) CSDR) – the overriding policy aim is to improve settlement efficiency and safety.

- The second part focuses on the regulation of the CSDs themselves, imposing among other things specific conduct of business and prudential requirements.

The CSDR is directly applicable in EU member states, and is subject to a number of Level 2 implementing measures by way of regulatory and technical implementing standards and delegated acts. One of these, Commission Delegated Regulation (EU) 2018/1229 (the regulatory technical standards (RTS) on settlement discipline) will come into effect on **13 September 2020**. This marks the start of the settlement discipline regime by setting out measures to prevent settlement fails, as well as measures to address them. While specific provisions apply to CSDs and CCPs, all market participants in the settlement chain will be impacted to a greater or lesser degree. It is expected that the impact will be minimal, with the main uplift being updates to CSDs' rules to accompany the new regime.

In summary, the RTS contains:

- measures designed to mitigate the risk of settlement fails and to encourage settlement discipline – including measures concerning professional and retail client disclosures, settlement facilitation and processing, matching of settlement instructions, bilateral cancellation facilities at CSDs, hold and release mechanisms and partial settlements;
- measures to address settlement fails when they happen – including measures on monitoring systems at CSDs, the reporting of settlement fails and public disclosures of settlement fails;
- provisions on cash penalties – including how they are calculated, applied, collected and distributed;
- details of the buy-in process – including the incorporation of contractual arrangements between counterparties in the settlement chain, provisions applying to transactions (with different permutations depending on whether or not they are cleared by a CCP and/or executed on a trading venue), the calculation and payment of cash compensation, buy-in costs and payment by the failing party of any price difference (i.e. broadly, the difference between the price agreed at the time of the trade and the price effectively paid on the buy-in, where higher) and timeframes for the buy-in process; and
- measures addressing consistent and systematic settlement fails.

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