

## Financial Markets Law Committee (“FMLC”)



### Banking Scoping Forum

Date: Monday 28 September 2020

Time: 2.00pm to 3.30pm

Virtual meeting

#### Attendees:

Monica Sah (Moderator)

Chris Allen

Tom Callaby

Thomas Donegan

Laura Feldman

Jons Lehmann

John McGrath

Dorothy Livingston

Julia Smithers Excell

Ferdisha Snagg

Paul Wilden

Clifford Chance LLP

Standard Chartered Bank

CMS Cameron McKenna Nabarro Olswang LLP

Shearman & Sterling LLP

Freshfields Bruckhaus Deringer LLP

Fried, Frank, Harris, Shriver & Jacobson (London) LLP

Dechert LLP

Herbert Smith Freehills LLP

White & Case LLP

Cleary Gottlieb Steen & Hamilton LLP

Apex Group Ltd

Chhavi Sinha

FMLC Secretariat

Katja Trela-Larsen

FMLC Secretariat

#### Guest Speaker:

Laura Douglas

Clifford Chance LLP

#### Regrets:

Mark Kalderon

Freshfields Bruckhaus Deringer LLP

Etay Katz

Allen & Overy LLP

Suhail Khawaja

Wilmington Trust

Jan Putnis

Slaughter and May

Registered Charity Number: 1164902.

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## Minutes:

### 1. Introductions

1.1. Ms Sah opened the meeting and briefly introduced the topics to be discussed.

### 2. Did you know the FMLC is moving premises? (Katja Trela-Larsen)<sup>1</sup>

2.1. Ms Trela-Larsen informed members that the FMLC Secretariat will be moving out from the current offices in the Bank of England to new premises offered by the City of London later this year. In light of the coronavirus pandemic, many FMLC meetings have been held virtually and there is a possibility of continuing to schedule meetings online in the future. Ms Trela-Larsen observed that some meetings and events are better face to face and, when in-person meetings resume, the FMLC Secretariat would appreciate offers to host events and meetings.

### 3. Brexit—Uncertainties in relation to rules under the Temporary Transitional Power and substituted compliance for firms under the Temporary Permissions Regime (Laura Douglas)

3.1. Ms Douglas commented that the onshoring of retained EU legislation and the U.K. regulators' proposed exercise of their Temporary Transitional Powers ("TTP") offers an opportunity to revisit what the U.K. regulatory landscape would look like at the end of the Brexit transition period and to examine whether the U.K. legal regulatory framework is clear and fit for purpose going forward. Banks have expressed concerns around the opacity and complexity of the new regulations and the short time period within which they would have to adapt. Ms Douglas noted that determining which regulations will apply to a firm after the transition period is a complex question. Ms Douglas gave the example that for a deposit-taking firm operating under the Temporary Permissions Regime ("TPR"), or run-off regime, the starting point for which rules will apply differs from the Financial Conduct Authority ("FCA") and Prudential Regulatory Authority ("PRA").

3.2. Ms Douglas stated that the PRA's starting position is that the rules applicable to firms accessing the U.K. market under the TPR will be the same as those to which other Third Country firms are subject but with some modifications. The FCA's starting

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<sup>1</sup> Please see Appendix I

position is that firms accessing the U.K. market under the TPR will have to comply with rules that applied to them pre-Brexit, albeit with some modification. This approach is set out in General Provision 2.2.26 of the FCA Handbook.<sup>2</sup> Ms Douglas remarked that this effectively preserves the *status quo* for firms which, after the end of the Brexit transition period, will access the U.K. market under the TPR. She noted the FCA is willing to accept “substituted compliance” in certain cases where firms can demonstrate that their Home State’s rules are equivalent to those in the FCA Handbook. Ms Douglas commented that the territorial scope of the rules remains uncertain. Another question concerns how the TPR will interact with rules available in “onshored” E.U legislation, such as Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories (the “**European Market Infrastructure Regulation**” or “**EMIR**”) which has been “onshored” in the U.K. by the Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2018.

- 3.3. Ms Douglas noted that the FCA has stated that European Level III Guidance and Q&As previously issued by the European Securities and Markets Authority (“**ESMA**”) and the European Banking Authority (“**EBA**”) will continue to apply with the necessary modifications. For example, where a Q&A refers to ESMA, the reference is to be read as one to the appropriate U.K. authority. She observed that a detailed analysis may be required as although in some cases the applicable provision will be obvious this is not always the case. Ms Douglas gave the opinion that there is a problem of scale as much as any individual point of uncertainty. Ms Sah asked members to consider what input the FMLC could have on this topic. Members agreed that the U.K. TPR and TTP only provides a stop-gap measure. A member suggested the uncertainty might be resolved by the publication of clearer consolidated material. Members agreed this is an issue for banks to put to regulators; they did not recommend the FMLC consider work on this issue unless any legal ambiguity arises in the guidance.

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<sup>2</sup> General Provision 2.2.26 of FCA Handbook, available at: <https://www.handbook.fca.org.uk/handbook/GEN/2/2.html>

#### 4. The Investment Firms Regulation and preparing for the U.K. Investment Firms Prudential Regime (Tom Callaby)

4.1. Mr Callaby stated the E.U. prudential regime for investment firms—namely Regulation (EU) 2019/2033 on the prudential requirements of investment firms (the “**Investment Firm Regulation**” or “**IFR**”) and Directive (EU) 2019/2034 on the prudential supervision of investment firms (the “**Investment Firm Directive**” or “**IFD**”)—will apply to all investment firms authorised in the E.U. from the end of June 2021. Mr Callaby noted that the EBA recently consulted on Regulatory Technical Standards under the IFR/IFD (“**Draft RTS**”).<sup>3</sup> Meanwhile, as the E.U. regime will be introduced after the scheduled end of the Brexit transition period, the U.K. will introduce its own prudential regime for investment firms. A high level framework is expected from the FCA on a U.K. Investment Firms Prudential Regime (“**U.K. IFPR**”).

4.2. Mr Callaby noted that the FCA published a discussion paper on a new U.K. prudential regime for investment firms (the “**FCA Discussion Paper**”).<sup>4</sup> The FCA Discussion Paper comments on the E.U.’s new prudential regime under the IFR/IFD, and seeks feedback from stakeholders on the appropriate rules for the U.K. to apply in this area. Mr Callaby commented that the FCA Discussion Paper raised a number of questions. A consultation paper is expected to follow which will likely give more clarity on the position the new U.K. regime will pursue. Mr Callaby observed that the lack of detailed information means that firms are unable to prepare for the potential new regime. Mr Callaby noted that until the FCA publishes the expected consultation paper, there remains uncertainty for firms.

4.3. Mr Callaby gave an overview of some of some of the current challenges and points of interest that firms are facing regarding the preparation for the U.K. IFPR. It is expected that the U.K. IFPR will alter the current range of FCA prudential categories. A key issue is the scope of the U.K. IFPR and how it may apply to business not regulated under Directive 2014/65/EU on markets in financial instruments, such as that

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<sup>3</sup> EBA, Consultation Paper EBA/CP/2020/06 (4 June 2020), available at: [https://eba.europa.eu/sites/default/documents/files/document\\_library/Publications/Consultations/2020/CP%20on%20draft%20RTS%20on%20prudential%20requirements%20for%20Investment%20Firms/884615/EBA-CP-2020-06%20CP%20on%20draft%20RTS%20on%20prudential%20requirements%20for%20Investment%20Firms.pdf](https://eba.europa.eu/sites/default/documents/files/document_library/Publications/Consultations/2020/CP%20on%20draft%20RTS%20on%20prudential%20requirements%20for%20Investment%20Firms/884615/EBA-CP-2020-06%20CP%20on%20draft%20RTS%20on%20prudential%20requirements%20for%20Investment%20Firms.pdf)

<sup>4</sup> FCA, Discussion Paper DP20/2: “A new UK prudential regime for MiFID investment firms” (23 June, 2020), available at: <https://www.fca.org.uk/publication/discussion/dp20-2.pdf>

conducted by non-bank depositaries. Another key question is whether there will be a change in the U.K.'s approach to prudential consolidation. The Draft RTS, under the IFR, adopts a prescriptive approach; a question remains as to whether the FCA will follow this detailed approach. Mr Callaby brought to member's attention other points of interest such as issues around remuneration and outsourcing.

4.4. Members discussed these questions. They agreed that the law regarding the U.K. IFPR is at a premature stage and it might be too early to recommend issues for the FMLC to address. While there is current uncertainty, Mr Callaby noted that FCA is likely to address these issues in its consultation paper. Members resolved to review the position after the FCA publishes its consultation paper.

## 5. **The FCA's and PRA's operational resilience and outsourcing consultations (Laura Feldman)**

5.1. Ms Feldman gave examples of operational disruption in the financial services sector to provide the context around which reform in relation to operational resilience and outsourcing was being considered. Referring to her slides, she discussed recent high-profile operational failures resulting in IT disruption. Quoting from several Bank of England (the "**BoE**") and FCA statements, Ms Feldman explained the meaning of operational resilience and why it is seen as a priority.

5.2. Ms Feldman gave an overview of the regulatory landscape and developments around operational resilience in the U.K. and the E.U. She stated that in the U.K., the PRA, BoE and the FCA lead standards for operational resilience. In December 2019, the BoE published several consultation papers setting out proposals for improving the operational resilience. These consultation papers follow a discussion paper published by U.K. regulators on operational resilience,<sup>5</sup> and a report published by the House of Commons Treasury Select Committee on IT failures in the financial services sector.<sup>6</sup> In the E.U., the Basel Committee on Banking Supervision ("**BCBS**") have published Operational Resilience Principle, the European Banking Authority ("**EBA**") has issued

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<sup>5</sup> BoE, PRA and FCA, Discussion Paper on "Building the UK financial sector's operational resilience" (July 2018), available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/discussion-paper/2018/dp118.pdf>

<sup>6</sup> House of Commons Treasury Committee, "IT failures in the financial services sector: Second Report of Session 2019–20" (22 October 2019), available at: <https://publications.parliament.uk/pa/cm201919/cmselect/cmtreasy/224/224.pdf>

Outsourcing Guidelines and the European. Commission Digital Finance Strategy has been published.<sup>7</sup>

- 5.3. In the U.K. context, Ms Feldman drew attention to the three main consultations (i) the PRA’s Outsourcing Consultation;<sup>8</sup> (ii) the PRA’s Operational Resilience Consultation (building impact tolerances for important business services);<sup>9</sup> and (iii) the FCA’s Operational Resilience Consultation (building impact tolerances for important business services).<sup>10</sup> She stated the U.K. regulators propose to publish their final policy on the proposals in the final quarter of 2020 or in early 2021, with implementation of most proposals shortly after. She gave an overview of the approach in the aforementioned FCA and PRA Consultation Papers, describing a four-pronged approach for supervisory expectations and assessments. This includes mapping of important business services, setting impact tolerance for each important business service, taking actions—through “scenario testing”—to be able to remain within their impact tolerances, and senior manager responsibility for oversight and approval of self-assessment documents.
- 5.4. Ms Feldman went on to provide an overview of the PRA’s Outsourcing Consultation. She stated the consultation proposals supplement existing PRA and FCA principles. For example, risks from outsourcing should be identified, assessed, monitored and managed—regardless of whether an arrangement is formally outsourcing—in accordance with the regulators’ expectations. Oversight is intended to be proportionate and based on principles rather than being prescriptive. There are likely to be further proposals on concentration risk, as numerous institutions relying on the same

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<sup>7</sup> BCBS, Consultative document on “Principles for operational resilience” (August 2020), available at : <https://www.bis.org/bcbs/publ/d509.pdf>;

EBA, EBA Guidelines on outsourcing arrangements (February 2019), available at <https://eba.europa.eu/eba-publishes-revised-guidelines-on-outsourcing-arrangements>;

European Commission, Digital Finance Package (September 2020); available at: [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/digital-finance\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/digital-finance_en)

<sup>8</sup> BoE and PRA, Consultation Paper CP30/19: “Outsourcing and third party risk management” (December 2019), available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2019/cp3019.pdf?la=en&hash=4766BFA4EA8C278BFBE77CADB37C8F34308C97D5>

<sup>9</sup> FCA, Consultation Paper CP19/32: “Building operational resilience: impact tolerances for important business services” (December 2019), available at: <https://www.fca.org.uk/publications/consultation-papers/cp-19-32-building-operational-resilience-impact-tolerances-important-business-services>

<sup>10</sup> PRA, Consultation Paper CP29/19: “Operational Resilience: Impact tolerances for important business services” (December 2019), available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2019/cp2919.pdf>

outsourcing provider has been identified as an area of concern as a failure of the outsourcing provider may lead to a widespread failure across a sector. Ms Feldman noted that the House of Commons Treasury Select Committee has recommended producing a sector map that would allow the regulators to identify and understand commonly used service providers. Ms Feldman drew attention to lessons learnt owing to Covid-19, noting that the pandemic has not been seen as a significant disruption as necessary measures were already in place.

- 5.5. Members discussed the uncertainty around the definition of terms like “important business services” and “critical service providers”. They noted that U.K. Finance has also raised concerns around definitions. A member agreed that there is a risk of systemic concentration of power, particularly where bespoke technology is only available from one provider. A member commented that regulation in this area may benefit from being extended to cover the third party provider as institutions are likely to have difficulty negotiating contracts that fully address concerns around outsourcing. Members discussed challenges associated with the outsourced, third-party and intra-group arrangements. Members agreed to watch the developments in this space, particularly, how the regulators would go about identification of outsourcing arrangements.

## **6. Any other business**

- 6.1. No other business was raised.

# Did you know ... the FMLC is moving?

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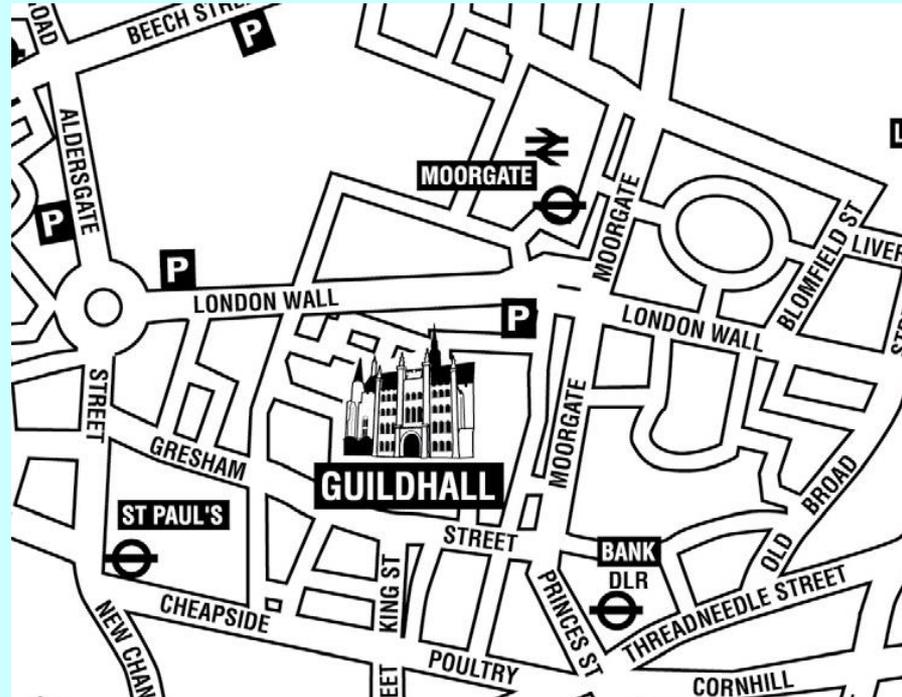
**Katja Trela-Larsen**  
**Forums Coordinator**

**Registered Charity Number: 1164902.**

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# New Premises in the City of London

The FMLC Secretariat will be moving from the current offices in the Bank of England to new premises offered by the City of London later this year. We are not moving far, the Secretariat's new office is less than a five minute walk from the Bank of England.



# New ways of working

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In light of the coronavirus pandemic, many of our meetings have been held virtually.

When we return to face-to-face meetings the FMLC will no longer be able to host Scoping Forum meetings at the Bank of England facilities.

The Secretariat is exploring the possibility of continuing to schedule more of the FMLC's meetings online in future.

We would also appreciate offers to host some meetings for us.

# FMLC Events

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In addition to in-person Scoping Forum meetings, we would appreciate help with annual FMLC events, including:

- Judicial Seminar
- Quadrilateral Conference
- Spring and Autumn Seminars
- Patrons' Dinner, and
- Festive drinks reception

Help may take the form of hosting and catering for the event, or even providing logistical support, such as printing.

# Supporting the FMLC

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If you wish to find out more about upcoming FMLC events and the ways you can offer support, please contact Rachel Toon ([executivesupport@fmlc.org](mailto:executivesupport@fmlc.org))

As ever, if you have an issue of legal uncertainty you would like to raise with the FMLC, or if you or your organisation would like to contribute to the FMLC's work via a Scoping Forum or Working Group, please contact Venessa Parekh ([research@fmlc.org](mailto:research@fmlc.org)) or Katja Trela-Larsen ([forums@fmlc.org](mailto:forums@fmlc.org))