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Back to school

A round up of the summer months and a look ahead to the rest of the year

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REGULATORY STRATEGY
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Contents

Foreword

A busy summer, especially for UK banks, with the FCA demonstrating how it will operate under the new Consumer Duty

This year, we have combined two of our mid-year publications – the Interim Regulatory Outlook and the Back to School note. This document summarises developments over the summer months, looks back at how the predictions we made in our 2023 Regulatory Outlook have fared and looks ahead to what we can expect over the rest of this year.

As always regulators remained active over the summer months. In the UK, we had the first deadline for compliance with the Consumer Duty and, linked to that, significant activity on cash savings. The UK banks were also in the spotlight in relation to “debanking”. Both these issues are covered in more detail below. In other developments, there was progress on Solvency 2 reform, in both the UK and EU, an important report from the FCA on fund managers’ assessments of value and plenty of activity in relation to sustainable finance (especially disclosures) and on UK retail payments regulation.

Looking back, the predictions we made in our RO23 have played out much as we anticipated and we expect this trend to continue for the remainder of the year. The one significant exception relates to banking, where we saw three unexpected developments - one global and two, more recently, specific to the UK.

The global issue is the banking market turmoil which began in March 2023 and saw the collapse of SVB and several other US regional banks, as well as the rescue merger of Credit Suisse by UBS. Although in some respects very different, these events shared some similarities, including very rapid liquidity outflows and underlying business model weaknesses. Both the Basel Committee on Banking Supervision and the Financial Stability Board are undertaking “lessons learned” exercises. We do not detect much appetite for a significant rewrite of global standards. Instead, any significant regulatory responses will be more localised, in the countries most directly affected. But we have seen increased supervisory vigilance across the board on liquidity risk, IRRBB and business model viability.

Two unanticipated UK issues dominated the summer months. The first relates to whether UK banks are passing on the benefit of interest rate increases to cash savers sufficiently quickly. The way that the FCA has tackled this issue has given us an early insight into what we can expect its approach to be under the Consumer Duty - it will aim to identify practices that may not be delivering good outcomes for customers quickly and pursue them through data requests, interventions and, where necessary, disciplinary action.

The second concerns the issue of “debanking” and whether UK banks are refusing to open or are closing the accounts of individuals or businesses because of expressions of political and/or other opinions and are thereby curtailing freedom of expression. The FCA has issued information requests on account closures and implementation of its 2017 guidance on Politically Exposed Persons – both of which are pre-cursors to near-term changes to the UK policy framework.

We expect these two UK-specific issues to remain high on the agenda for the rest of 2023. In addition, we expect the final Basel 3.1 rules in the EU and UK, further progress on Solvency 2 and, with a fair wind, the long-awaited consultations on the UK Green Taxonomy and the UK stablecoins framework.

David Strachan

Partner

Suchitra Nair

Partner

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Regulatory themes for the remainder of the year

Although credit quality has so far shown little sign of deterioration, supervisors remain vigilant and will focus on credit risk management and treatment of borrowers and other customers in difficulty.

UK market events have given rise to a renewed focus on financial crime, and the functioning of the PEP regime in the UK. The FCA will set out next steps on reforms to its rules on both PEPs and account closures in the coming months, with the UK government due to bring forward secondary legislation on the latter.

Implementation of the UK Consumer Duty is at the forefront for FCA supervisors and firms. Increases in interest rates over the course of 2023 have catalysed supervisory interest in how rate rises are passed through to customers, especially cash savers.

Prudential regulators will continue to revise the prudential framework – with the Basel 3.1 rules due to be finalised in the UK and EU, consultations from the PRA on Solvency UK, Solvency 2 trilogues ongoing in the EU, and fund liquidity a priority in the UK.

Globally, a new standard on nature-related financial disclosures will be finalised and COP28 will provide a focal point for an assessment of progress against Paris commitments. In the UK, attention will be on the FCA, as it develops its disclosure requirements and takes further steps to reduce greenwashing risk.

The regulatory framework around innovative products and services will continue to develop, with the EU and UK due to finalise frameworks for regulation of AI, and UK regulators due to consult on approaches to regulating stablecoins and unbacked digital assets.

Key regulatory publications over the summer

Banking

US agencies [Notice of Proposed Rulemaking (NPR)] on Basel "endgame" (27 July)

US proposed rules diverge both in timing and content from the Basel standards and the approaches in the EU and UK

The US banking regulators consulted on rules for the implementation of the Basel 3.1. standard which, if adopted as published, would diverge significantly from the approaches taken by both the UK and EU. The US proposal also envisages a transition period of three years, starting 1 July 2025 with a fully phased-in date of 1 July 2028. This differs significantly from the UK and EU, which so far have been working to a 1 January 2025 implementation and a five-year transition period.
The differences in timing and content, at relatively short notice, will create implementation challenges for banks operating in US and UK/EU jurisdictions. In particular, the differences in timing, if they endure, will mean banks operating in both US and UK/EU jurisdictions will have to manage half year reporting on both Basel 2 and Basel 3.1 bases. Among the more difficult differences in the substance of the rules are likely to be differential risk weights for retail exposures (higher in US proposals than UK/EU) and implementation of the Internal Loss Multiplier (ILM) for Operational Risk with a *floor* at 1 (as opposed to *setting* the ILM to 1 for all banks in the UK /EU). On balance, and notwithstanding industry comment, we expect the UK and EU to hold the line on a 1 January 2025 implementation date.

HMT Cash access policy statement and FCA new powers to protect cash access (18 August)

New rules on the way

HMT published its policy on cash deposits and withdrawal services for both individual and business accounts. HMT's policy is that levels of coverage should be maintained as present (access within maximum 1 mile/3 miles for urban/rural users respectively). The FCA will consult on new rules for designated banks under the cash access regime and it expects the new rules will be effective by the summer of 2024.

ECB Consultation on Risk Data Aggregation and Regulatory Reporting (RDARR) (22 July)

Insufficient progress since ECB's 2016 thematic review

The Consultation comes with the ECB's assessment of how banks have complied with the BCBS 239 principles on risk data aggregation since its thematic review in 2016. The ECB regards the progress made so far by banks as insufficient and concludes that many banks still have structural deficiencies in how they aggregate and report risk data. The ECB's specific areas of focus and concern include:

- Responsibilities of the management bodies in relation to BCBS 239 governance, resourcing and approval.
- The need for banks to ensure that their implementation of the principles cover all forms of reporting: internal, external financial and regulatory.
- Effective data governance and an integrated data architecture, with uniform definitions and clear validation rules.

Results of the BoE 2022/23 ACS stress test and the 2022 EU-wide stress test (12 and 28 July)

UK and EU banks remain resilient to shocks

The BoE judged UK banks to be resilient to the macroeconomic scenario and having the capacity to support households and businesses through a stress more severe than the current environment. The results show a capital depletion leading to an aggregate 10.8% CET1 ratio. The BoE did not require any of the banks to submit a revised capital plan.

In its EU-wide exercise, the EBA found that the EU banking sector is well-prepared to withstand a prolonged adverse scenario, with banks able to absorb more than 496bn EUR of losses. After the stress, banks' aggregate CET1 ratio was projected to fall to 10.4%. Only three banks in the 70-bank set did not to meet the SREP capital requirements threshold post-stress.

Rod Hardcastle
Banking Sector Lead

The year so far:

Significant unexpected developments/delays — Regulatory progress as expected

The collapse of Credit Suisse and several US regional banks in March raised regulatory concerns around liquidity and interest rate risk management and resolution of failing banks. While the regulatory response will take time to emerge, we expect supervisors to continue to increase their focus in these areas. Meanwhile, the FCA has been more vocal than expected on the pass through of higher interest rates to savers.

Looking ahead…

- *Basel 3.1 finalisation in the EU and UK expected by the end of the year.*
- *Credit risk remains to the fore, especially where inflation remains high.*
- *ECB and PRA supervisors will continue to scrutinise banks' regulatory reporting, taking enforcement action where necessary.*
- *UK policymakers may propose reforms to the deposit insurance framework.*

What to watch out for

- PRA Basel 3.1 Policy Statement - Q4
- HMT secondary legislation on ring-fencing reform - Q4
- BCBS and FSB reflections on banking market stress - Q4
- EBA ITS and examination programme on resolution - Q4

Key regulatory publications over the summer

Capital Markets

UK: Chancellor Hunt's Mansion House speech (11 July)

Edinburgh Reforms progress in the City

In addition to modifying the Prospectus Regulation, the government committed to establishing a new "intermittent trading venue" by the end of 2024 to improve private companies' access to capital markets before they publicly list. In parallel, HMT accepted the findings of the independent Investment Research Review which aim to increase the supply of research on smaller cap companies, improve access to research by altering the MIFID II "unbundling" rules, and allow greater access to research for retail investors. The FCA will publish the final rules by the first half of next year.

UK: PRA, FCA and HMT consulting on reforms to the Securitisation regulation, (July and August)

Three-pronged review to bolster securitisation markets

Regulators and HMT are consulting on changes to the retained EU Securitisation Regulation – focused primarily on lightening the due diligence requirements for institutional investors; making risk-retention requirements, transparency requirements, credit granting standards and restrictions on securitisations more proportionate; and clarifying changes to the scope of the rules and simple transparent and standardised (STS) securitisations (as a means to support their increased issuance). Changes will be made from Q2 24, subject to the progress of HMT's draft legislation.

UK: FCA portfolio letter for Principal Trading Firms (PTF) (4 August)

Extensive book of work ahead

The FCA is increasing its focus on financial and operational resilience of PTFs as well as governance, oversight, compliance and risk monitoring for algorithmic trading and commodity trading firms. The FCA will review firms' compliance with MiFID RTS 6 and 7 and capital and liquidity in light of the Investment Firm Prudential Regime and assess operational resilience implementation plans.

UK: FCA revokes the Share Trading Obligation and amends the Derivatives Trading Obligation (29 August)

Delivering the Wholesale Markets Review findings

In line with the outcome from the Wholesale Markets Review, the FCA announced the removal of the share trading obligation (STO), allowing firms to make a decision to trade on any trading venue and OTC in the UK and overseas to deliver the best outcomes for their clients. The FCA has also amended the scope of the derivatives trading obligation (DTO) to align it with the EMIR clearing obligation.

EU: ECB draft guide on financial conglomerate reporting of significant risk concentrations and intragroup transactions (21 August)

Ironing out its approach to financial conglomerates

The purpose of the guide is to provide consistency and transparency on the ECB's approach to financial conglomerates. Specifically, it outlines the types of concentration risk and intragroup transactions that need to be reported, relevant thresholds and reporting formats. For instance, the ECB expects financial conglomerates to report counterparty risk concentrations above the lower of €300m or 10% of their own funds and intragroup transactions that equal or exceed the lower of €300m or 5% of capital adequacy requirements. The ECB invites comments to the draft by 6 October.

UK: PRA and FCA margin requirements for non-centrally cleared derivatives (18 July)

Extending the existing exemption

The PRA and the FCA are consulting on an extension to the temporary exemption for single-stock equity options and index options from bilateral margining requirements, under UK EMIR, by two years to January 2026. This will allow regulators more time to develop a permanent UK framework. The consultation, which is closing on 18 October, also sets out the proposed approach to pre-approving bilateral initial margin models.

Margarita Streltses
Senior Manager, Capital Markets sector lead

The year so far:

Significant unexpected developments/delays — Regulatory progress as expected

Despite the historically volatile markets of the past year, neither UK nor EU capital markets regulatory processes have been diverted away from their original goals (ensuring self-sufficiency vs promoting open, innovative and competitive capital markets).

Looking ahead...

- *More clarity on the European Council and Parliament's positions in relation to the EMIR "active account" requirement for clearing is expected towards the end of the year.*
- *With the US T+1 migration approaching, affected firms will focus on testing and updating their infrastructure, whilst visibility on UK and EU policymakers' intentions may also increase.*
- *The EU Green Bond standard is due to be released at the start of Q4*

What to watch out for

- EU Parliament and Council to set out negotiating positions on EMIR "Active Account" - H2
- FCA Consultation on primary markets - Q3
- FCA Consultation on waivers regime - Q3
- UK Accelerated Settlement Taskforce initial findings - Q4
- UK Digital Securities Sandbox launch - Q4
- UK FCA Policy Statement on consolidated tape - Q4

Key regulatory publications over the summer

Insurance

PRA: Closure of the first PRA Consultation on Solvency UK (SUK) – (1 September)

The first step on a long road

The PRA published its first SUK consultation introducing a range of reforms including: a Risk Margin reduction to result in significant capital release, a new calculation method for the Transitional Measures on Technical Provisions to reduce the operational burden of these calculations, a reduction of the number of internal model tests and more flexibility for IM approvals, and a wider use of capital add-ons. The proposed reforms also aim to improve the overall competitiveness of the UK insurance industry by facilitating the entrance of new insurers in the market and third-country branches. The overall impact of the proposals will depend on how the PRA chooses to implement the rules in practice.

Whilst the reforms will result in a capital relief for many firms, the cost of implementing the reforms and the increased potential for regulatory uncertainty on key aspects such as internal models will be a key concern for firms. Importantly, insurers need to wait until later this month to understand the details of the Matching Adjustment and investment flexibility reforms to obtain a full picture of the new regime and its impact.

PRA: Approach to insurance supervision (1 August)

A more proportionate and judgement-based approach

The new approach outlines how the PRA will deliver the new competitiveness and growth objective under the FSMA 2023. The PRA will look to tailor regulation to UK circumstances, adopting a more proportionate supervisory approach. There will be "substantial flexibility" for the PRA to tailor requirements based on the circumstances of an insurer or the nature of its concerns, opening the door to modifications or waivers. We expect the new approach to encourage firms to engage with the PRA on various firm-specific issues. The SUK review in particular will present an opportunity for the PRA to exercise flexibility and proportionality in a number of areas.

EU: Beginning of the trilogues on Solvency II and the Insurance Recovery and Resolution Directive (IRRD) (18 July)

Bridging the gap in the trilogues

After eight months of negotiations, the European Parliament (EP) ECON Committee voted to adopt draft reports on Solvency II and IRRD. Whilst the EU Council's General Approach on Solvency II was relatively close to the EU Commission's proposal, the EP's final report diverged materially. It notably proposes to include reforms to the Long-Term Guarantee (LTG) measures in the Directive instead of the Delegated Acts as initially planned. Firms should explore the impact of Solvency II reforms on reporting and sustainability risks where co-legislators' views are less divergent. But material uncertainty remains around LTG measures (Long-Term Equity Investment, Risk Margin, Volatility Adjustment calibrations) and proportionality thresholds. On IRRD, the EP and EU Commission appear to be more aligned, but some reforms, including resolution options, are still up for debate.

Trilogues, which start in September for both Solvency II and IRRD, are therefore likely to be complex, and final reforms may not be effective before 2027 given upcoming EU elections.

HMT: Response to Consultation on Insurer Resolution Regime (IRR) (2 August)

No surprises, but more clarity around final rules

After having consulted in January on the introduction of an IRR in the UK, HMT published its response and feedback to the Consultation in early July. Overall, respondents were supportive of HMT introducing an IRR regime. HMT does, however, set out a limited number of adjustments and provides several clarifications to its consultation, particularly in relation to the scope of the new IRR, cross-border arrangements, and valuation in resolution. HMT did not provide details on when the IRR will become reality, but will legislate whenever "parliamentary time allows". Given HMT's regulatory pipeline, this is unlikely to be any time soon. Regardless, systemically important insurers should review HMT's proposals in detail to understand where they might have capability gaps.

Kareline Daguer
Insurance sector lead

The year so far:

On the prudential front, regulatory and supervisory developments were announced in line with expectations, both in terms of their substance and timing. In the case of the EU IRRD, progress was even faster than expected.

Looking ahead…

- *For the remainder of 2023 and beyond, insurers' capital will be under growing supervisory scrutiny. In particular, non-life firms' underwriting discipline will come into focus following significant losses from climate-driven events. Meanwhile, life insurers will need to assess the capital impact of SUK reforms.*
- *On the conduct side, insurers are expected to turn to their closed books to achieve full compliance with the Consumer Duty by July 2024.*
- *Insurers should also continue to support customers throughout the cost-of-living crisis, while ensuring fair customer outcomes in the context of climate-driven events.*

What to watch out for

- Second CP on SUK (Matching Adjustment) - Q3
- EU trilogues on SII/IRRD - Q3
- FCA PS on multi-occupancy building policies - Q3
- PRA engagement on the timeline and design for Insurance Stress Tests - H2
- PRA Ease of exit consultation - H2

Key regulatory publications over the summer

Investment management

FCA: Multi-firm review on authorised fund managers' (AFMs') assessments of fund value (10 August)

FCA finds significant improvements, but further work is needed

The FCA found that many firms had significantly improved their value assessment processes since its last review in 2020/21, but there remain some significant shortcomings. These include firms putting too much emphasis on comparable market rates to justify their fees, firms prioritising their own profitability above value for fund investors, AFM Boards concluding that fees were justified even when improved management information raised significant questions or countered that position, and insufficient challenge from independent non-executive directors (iNEDs).

Firms will need to carry out a line-by-line gap analysis against the review's findings. In our view, it will be important for AFM Boards – including iNEDs - to read and understand the FCA's findings in detail and to use them as a basis to challenge the business. Many of the FCA's findings are also relevant to the price and value outcome under the Consumer Duty, so firms should apply their learnings to the rest of their fund range where relevant.

EU: Commission report on the functioning of the Money Market Funds (MMF) Regulation (20 July)

Commission decides not to reform the MMF Regulation, making it a clear outlier

The report concludes that overall the MMF Regulation has functioned well, enhanced financial stability and passed the test of recent market stress episodes. It identifies certain vulnerabilities in the market for MMFs that would merit further assessment but does not propose a revision of the legislation at this stage. Given that the FSB has proposed significant reforms to MMFs, that the US is pressing ahead with major reforms, and the UK has suggested that it may make significant reforms, the Commission's decision not to propose a revision of the MMF Regulation makes it a clear outlier.

Joy Kershaw

Senior Manager, IM&W sector lead

EU: Provisional agreement on the review of AIFMD and UCITS (20 July)

Reforms to AIFMD and UCITS receive provisional go-ahead

Negotiators from the European Parliament and the Council reached a provisional agreement which will need to be confirmed before it is formally adopted. It includes enhanced rules on delegation by investment managers but these are not expected to disrupt the current delegation model significantly. It also includes new rules on the availability and use of liquidity management tools, as well as a new EU framework for funds originating loans. Overall, the new regime is an evolution rather than a revolution. It will increase scrutiny in some areas, and open up opportunities for loan originating funds to operate on a cross-border basis across the EU.

EU: ESMA statement on securities lending (12 July)

Some firms are retaining too much revenue from securities lending

The statement sets out the regulatory requirements on securities lending in relation to retail client financial instruments, and highlights some shortcomings in current practices. Two particular shortcomings are that some firms are retaining too much revenue from securities lending, and that firms are not always gaining sufficiently explicit client consent for securities lending. The first of these was previously highlighted in ESMA's Common Supervisory Action on costs and fees. In our view, the principles set out in the statement are relevant to UK as well as EU firms, and UK firms should consider how much revenue from securities lending is passed on to the fund as part of the Consumer Duty's price and value outcome.

Lux: CSSF thematic review on the implementation of sustainability-related provisions in the investment fund industry (3 August)

CSSF shines spotlight on sustainability-related practices in investment funds

The report sets out the CSSF's observations and expectations of firms in this area. We expect the strong focus on sustainability to continue, particularly in view of ESMA's forthcoming Common Supervisory Action.

The year so far:

Significant unexpected developments/delays — Regulatory progress as expected

Key supervisory focus areas have been largely as anticipated (e.g. Consumer Duty, greenwashing, fund liquidity), and policy developments have progressed largely as expected (e.g. AIFMD/UCITS review, EU retail investment strategy). The EU Commission's statement that it considers significant reforms to money market funds to be unnecessary makes it an outlier among its global counterparts.

Looking ahead…

- *The FCA will scrutinise firms' implementation of the Duty. Particular focus areas for firms include information sharing between manufacturers and distributors, and MI and Board reporting.*
- *Fund liquidity will be a key focus area following the significant shortcomings found in the FCA's review and the international focus on this issue.*
- *Policy work on the UK's future regime for asset management will continue following the Edinburgh Reforms, DP23/2 and the Mansion House speech.*

What to watch out for

- Final text on the revised UCITS and AIFMD - Q4
- FCA consultation on future retail disclosure - H2
- FCA consultation on operationalising the Overseas Funds Regime - H2

Key regulatory publications over the summer

Financial crime

UK Government [announced plans](#) to clamp down on unfair bank account closures (20 July)

Banks must ensure customers' political views do not result in "debanking"

The UK government announced plans to bring forward secondary legislation to ensure that banks do not close customers' accounts as a result of legitimately held political beliefs. The aim is to protect freedom of expression. Banks will be required to disclose to customers the reason for their account being closed and allow them 90 days (currently 30) to challenge the decision through the Financial Ombudsman Service. The FCA and UK Chancellor of the Exchequer exchanged letters on freedom of expression and the provision of banking services on 3 August.

In this connection the FCA issued an extensive information request to the largest banks and building societies on account closures. The request covers the last 18 months and includes information on whether personal and business accounts have been closed because of expressions of political or other opinions, to which banks were expected to respond by 25 August.

FCA reviewing whether changes to the Politically Exposed Persons (PEP) regime are necessary (15 August)

Information requests to both banks and PEPs

Further to its request to firms to provide information on account closures, the FCA is reviewing how financial services firms have applied the PEP regime, and is considering whether changes to its 2017 guidance are needed. This follows a mandate included in the Financial Services and Markets Act 2023. To support the review, the FCA has invited UK PEPs (including MPs and peers) to share their experiences. The FCA will publish the full terms of reference for the review in September and publish a report by June 2024.

PSR Authorised Push Payment (APP) fraud consultations (15 August)

The details of the UK new APP scams reimbursement policy start to emerge

The PSR launched two consultations on specific aspects of its new APP fraud reimbursements requirements. Both consultations close on 12 September.

Consumer standard of caution – i.e. the standard of care that consumers should meet to be eligible for reimbursement of APP scams. The standard consists of three elements: heeding warnings, promptly reporting suspected APP scams to Payment Service Providers (PSPs), and cooperating with PSPs' reasonable information requests for assessing the claim. The standard will not apply to consumers deemed vulnerable.

Excess and maximum reimbursement level for FPS and CHAPS – the PSR is seeking views on structuring APP fraud claims excess. Options include a fixed amount or a percentage of a claim, with or without a cap. In consultation with the BoE, the PSR is also proposing a maximum reimbursement level per claim of £415k for both Faster Payments and CHAPS payments. While the claims excess would not apply to vulnerable customers, the maximum reimbursement level would.

FCA expectations for crypto firms complying with Travel Rule (17 August)

Robust expectations ahead of 1 September UK compliance deadline

The FCA set out its expectations on how firms should comply with the Travel Rule. The Travel Rule requires crypto service providers to obtain certain information on the beneficiary and originator of crypto-to-crypto and crypto-to-fiat transactions, in line with Financial Action Task Force recommendations. It is aimed at making crypto transfers more transparent. Some of the FCA's expectations are generally applicable, while others cover scenarios where a UK firm is sending a crypto transfer to – or receiving from – a jurisdiction without the Travel Rule:

- Transfer to: retain and store evidence of the information that the firm has collected to comply with its regulatory obligations.
- Transfer from: evaluate the risk associated with the jurisdiction that funds are received from – particularly where information is missing – and whether to allow the beneficiary to receive the cryptoassets.

Rod Hardcastle
Director, Financial Crime lead

The year so far:

The significant period of UK media attention on the issue of debanking was unforeseen and has resulted in the UK government taking action to ensure that customers' legitimately held political views do not result in withdrawal of banking services.

Looking ahead...

- *The location for the headquarters of the EU's Anti Money Laundering Authority (AMLA) is due to be announced before the end of the year. This is likely to prompt activity around recruitment and policy development.*
- *The UK government is also due to set out its view on potential reforms to AML/CTF supervision, with a single AML/CTF supervisor a possible outcome.*
- *Debanking and the treatment of Politically Exposed Persons will remain at the forefront of UK supervisors' minds for remainder of 2023 and the first half of 2024.*

What to watch out for

- Secondary legislation on the debanking issue - Q3/Q4 2023
- Terms of reference for FCA review of PEP regime - Q3
- UK Government follow-up to consultation on reforming AML/CTF supervision - Q4

Key regulatory publications over the summer

Retail conduct

FCA/Treasury Committee (TC): FCA Report on Cash Savings Markets Review 2023 (31 July), **Responses from High Street Banks and FCA on savings rate** (18 July) **and FCA Joint letter with ICO on data protection and effective communication to savings customers** (18 July)

Retail banks must take swift action to ensure good outcomes for savers

The TC put the "Big Four" UK banks in the spotlight early in July questioning both them and FCA on whether banks were passing on higher interest rates to savers quickly enough. Some banks argued data protection regulations prevented them from contacting customers to offer better rates. The FCA and ICO swiftly issued a Joint letter clarifying that data protection regulations do not prevent banks from informing savings customers about better deals. At the end of July, the FCA published its review of the Cash Savings Market 2023. The review includes a set of actions for both FCA and banks to ensure savers are getting good outcomes. While initial focus was on the "Big Four", the FCA's action plan applies to all banks and building societies.

Firms offering the lowest rates were required to submit their value assessments by 31 August 2023 and must take action before year end. Additionally, the FCA expects banks to accelerate their fair value assessments of off-sale accounts ahead of the 31 July 2024 deadline for closed products. The FCA will review the effectiveness of banks' communications to their customers by end of March 2024 with the largest banks required to submit self-assessments by end-2023.

The FCA will take swift action against banks that fail to demonstrate Duty compliance in this area. Banks will need to be prepared to answer questions on their approach to rate setting, differences between on and off sale rates and approach to customer engagement over the next four to six months.

FCA Advice Guidance Boundary Review Workplan (3 August)

Supporting consumers to make better financial decisions

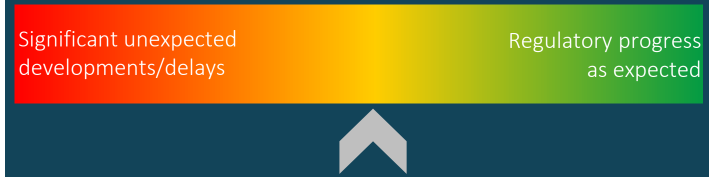
The FCA announced the basis of its joint review of the Advice Guidance Boundary with HMT. The objective of the review is to ensure consumers receive better, affordable support to make informed financial decisions. The FCA is clear that the solution to the issue of lack of support will not come from regulated advice alone. It will require risk management rather than risk elimination, will need to be commercially viable for firms, and should leverage the Duty. The FCA will roll the development of its core Investment Advice Regime proposals into this review and expects the review to involve substantial rule changes and take considerable time.

To assist firms while the review is carried out, the FCA published clarifications on the current requirements with practical examples of advice without personal recommendations. It also reminded firms that, as part of the Duty, overcautiousness about providing financial advice, could lead to foreseeable harm through lack of support to customers and referred firms to its joint letter with the ICO (see opposite) on data protection for more insight.

The FCA will provide more information on its review in a policy paper this autumn. Firms can already start reviewing their current practices as part of their compliance with the Duty and identify where they can provide more flexible support, with a focus on the practical examples provided by the FCA.

Kareline Daguer
Director, Retail Conduct lead

The year so far:



The Duty came into effect on 31 July 2023. However, interest rate rises and inflation have propelled issues of fairness for savers and support to those in debt to the top of the FCA's agenda quicker than expected. The Cash Markets Review has accelerated timeline considerations for closed products and the Mortgage Charter outlines a commitment for support of customers in financial difficulty.

Looking ahead…

- *The FCA will prioritise certain areas to supervise compliance with the Duty, including fair value, communications and support for customers in financial difficulty across sectors.*
- *Data matters: the FCA will use a data led-approach to monitor the Duty and firms will need to use data to demonstrate compliance.*
- *The Advice Guidance boundary review will kick off in the autumn. The FCA expects proposals to include substantial change.*

What to watch out for

- FCA and PRA: Joint Consultation Paper on Diversity and Inclusion - Q3
- FCA: Policy paper on Advice/Guidance boundary review - Q4
- FCA/HMT second draft legislation and CP on regulating BNPL firms - Q4

Key regulatory publications over the summer

Sustainable finance

Department for Business & Trade: Announcement on the UK Sustainability Disclosure Standards (SDS) (2 August)

UK policymakers take steps to adopt sustainability disclosure standards …

After the first part of the IFRS Sustainability Disclosures Standards issued by the International Sustainability Standards Board (ISSB) were finalised earlier this year, the UK government has announced how the framework will be adopted in the UK. The SDS – to be completed by July 2024 – will follow the international standards closely and only diverge from the global baseline if "absolutely necessary" for UK specificities.

In its Primary Market Bulletin 45, published on 10 August, the FCA subsequently set out its approach to replacing disclosures under the TCFD framework with ISSB standards. It will consult on rule changes in H1 2024, and final rules will come into force for accounting periods from 2025.

… while adoption of the standards globally is gaining momentum

On 25 July IOSCO determined that the ISSB standards are "appropriate to serve as a global framework for capital markets to develop the use of sustainability-related financial information". It is now calling on its member jurisdictions to consider methods for adopting the standards. In and of itself this determination does not change anything about the standards, but it should be an important step in accelerating adoption.

European Commission: Delegated Act on the first set of European Sustainability Reporting Standards (ESRS) (31 July)

Implementation of EU corporate sustainability reporting rules also moves on

The Commission published its adopted Delegated Act (DA) on the first set of ESRS. It made several changes to the draft proposal it received, with the aims of: achieving greater interoperability with ISSB standards; reducing the reporting burden; and making most of the disclosure requirements subject to materiality considerations. The standards are expected to come into effect from 1 January 2024 (subject to the remaining steps in the European legislative process), although many firms are already moving forward with their operational planning based on the current text.

Simon Brennan

Director, Sustainable Finance Lead

IAASB: Consultation on a proposed international sustainability assurance standard (2 August)

Wrapping up headlines on reporting, the proposed standard from the IASB on sustainability assurance sets out how practitioners should seek reasonable or limited assurance and provide a conclusion on the sustainability information in a report.

Transition Plan Taskforce (TPT): Status update on building momentum for transition plans (27 July)

Look ahead to the finalisation of the Disclosure Framework in the autumn

Those working on transition planning are looking ahead to the Disclosure Framework that the TPT will publish in October setting out the key elements of credible and robust transition plans. This status update from the TPT included information on timelines and what is likely to change in the final version of the recommendations. It also confirmed that it will consult on sector-specific guidance later this year.

On 10 August, the FCA in its Primary Market Bulletin 45, set out its plans to consult on expectations for listed companies' transition plan disclosures later this year. As expected, its guidance will be developed with reference to the final outputs from the TPT.

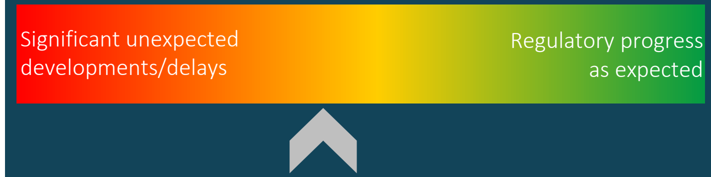
Also feeding into the mix of the UK's sustainability framework, the Green Technical Advisory Group (GTAG), which is advising the UK government on an approach to developing a UK taxonomy, published its final report Streamlining and increasing the usability of the Do No Significant Harm (DNSH) criteria, on 2 August.

Financial Stability Board (FSB): Updated roadmap for addressing financial risks from climate change (13 July)

Further clarity on the pipeline of policy work on climate-related financial risk

With limited recent developments in the sphere of climate-related financial risk, the FSB's roadmap on its planned work and overview of the plans of other international standard-setting bodies is a useful update. Amongst other things, the BCBS will consult this year on Pillar 3 standards for banks and may issue further clarifications on climate risks in Pillar 1.

The year so far:



There has been substantive progress in some key policy areas, most notably corporate sustainability disclosures and transition planning. Other policy initiatives, however, have been delayed because of technical complexity and political uncertainty. Overall, the "call to action" on climate we anticipated has materialised, but by mid-year nature risk is yet to gain prominence.

Looking ahead…

- *Internationally, a new standard on nature-related financial disclosures will be finalised and COP28 will provide a focal point for an assessment of progress against Paris commitments.*
- *In the UK, attention will be on the FCA in particular, as it develops elements of its disclosure requirements and takes further steps to reduce greenwashing risk.*

What to watch out for

- Taskforce on Nature-related Financial Disclosures publishes final standard - 18 September
- TPT disclosure framework - October
- FCA finalises fund labels rules and anti-greenwashing rule - Q4 (delayed from Q3)
- EBA final report on the prudential treatment of environmental risks - Q4
- UK Green Taxonomy consultation - Q4

Key regulatory publications over the summer

Innovation

Multiple retail payments regulatory developments from HMT

Future-proofing the UK regulatory framework for digital retail payments

The Electronic Money, Payment Card Interchange Fee and Payment Services (Amendment) Regulations 2023 (25 July) – As expected, **the Government laid a Statutory Instrument under FSMA 2023 to give the FCA and PSR enhanced rulemaking powers over payment services and e-money markets as retained EU laws are repealed. The new powers will allow FCA and PSR to react more dynamically to payment innovation, without waiting for Parliament to amend primary legislation.**

Response **to the Payments Regulation and the Systemic Perimeter consultation** (7 August) – HMT confirmed it will introduce legislation to extend the BoE's statutory perimeter to include new types of systemic payment providers, as proposed in July 2022. HMT will also simplify the legislative regime governing fair access to payment systems to strengthen PSR's intervention powers and provide clarity for firms. However timings are unclear. HMT only committed to introduce the reforms at "a future legislative opportunity".

Independent Future of Payments Review (11 July) – The Review will explore how retail payment are likely to evolve. In Autumn 2023, it will issue recommendations to government, regulators, and industry on the steps necessary to deliver the next generation of world leading retail payments.

HMT consultation on the Digital Securities Sandbox (DSS) (11 July)

Facilitating digital securities in the UK

The DSS will allow firms to set up and test Financial Market Infrastructures for trading and settling securities using digital asset technology, including distributed ledger technology. Firms will operate in a controlled environment but will be able to interact with real-world financial markets. They will benefit from a temporarily modified regulatory framework and BoE/FCA feedback. HMT invites potential applicants to express interest and answer some initial questions. The DSS is expected to launch by end-2023.

Valeria Gallo
Senior Manager, Innovation Lead

ESMA/EBA consultations on first set of Markets in Cryptoassets regulation (MiCA) technical standards (12 July)

The technical regulatory details for crypto firms start to emerge

ESMA's draft standards concern crypto service providers, while the EBA's standards are aimed at issuers of asset-referenced tokens, a type of stablecoin. Both sets cover authorisations, complaints handling, and acquisitions. ESMA's package also includes notifications by regulated firms of planned crypto services, and conflicts of interest. The draft technical requirements reaffirm that obtaining authorisation will require a significant shift in governance and risk management for many firms.

FCA feedback statement on potential competition impacts of Big Tech entry and expansion in retail financial services (12 August)

Increasing scrutiny of Big Techs' role and market power in FS

The FCA analysed the competition impact of Big Techs' growth in payments, deposit taking, consumer credit, and insurance. In response, it will launch a further Call for Input by end-2023 on Big Techs' role as gatekeepers in FS. The FCA will also work closely with the Government and the CMA Digital Market Unit as the new competition regime for digital markets is finalised. Finally, the FCA will review its supervisory approach to improve oversight of Big Techs' activities within and outside the regulatory perimeter.

EBA report on Machine Learning (ML) for IRB models (4 August)

Key adoption challenges and a call for regulatory clarity in EU AI Act

The EBA found that firms intend to use ML only in some areas of IRB modelling, primarily to estimate probability of default. Key challenges to adoption are explainability, traceability, model overfitting, management understanding, and skilled labour shortages. The EBA also calls for the EU AI Act to clarify that ML use for calculating capital requirements – rather than for assessing an individual's creditworthiness - is not a high-risk use case.

The year so far:

Significant unexpected developments/delays — Regulatory progress as expected

Cryptoassets and payments regulatory frameworks progressed broadly as expected. The EU MiCA is now in force, and the implementation countdown started. UK proposals to regulate stablecoin issuers and custodians are delayed but still expected in 2023, while crypto promotions rules have been finalised.

AI regulation accelerated. The EU AI Act entered final stages of negotiation, and the UK consulted on a principle-based AI regulatory framework.

Looking ahead…

- *MICA's technical standards will continue to emerge, covering key elements such as disclosures, and stablecoins governance and liquidity.*
- *Oversight of payments and e-money firms will continue to intensify, with the FCA set to use its enhanced FSMA 2023 rulemaking powers to bolster safeguarding requirements.*
- *AI will also remain in the spotlight as both the EU and UK are set to finalise their frameworks.*

What to watch out for

- Consultations on UK regulatory approach to stablecoins (Q3/Q4) and unbacked digital assets (Q4/Q1 2024).
- FCA consultations on safeguarding requirements for payments and e-money firms - Q3/Q4

Key regulatory publications over the summer

Cyber and Operational Resilience

EU Parliament and Council positions on the Cyber Resilience Act (19 July)

The EU's next major cybersecurity law moves to the final negotiating stage

Both the Council and Parliament reached their respective negotiating positions on the EU's Cyber Resilience Act (CRA). This enables the final phase of inter-institutional negotiations (trilogues) to begin in September.

The CRA aims to introduce harmonised minimum requirements for the cybersecurity of all connected digital products. These requirements are additive to the resilience-focused requirements of the EU Digital Operational Resilience Act (DORA) and would create a heavier compliance burden for firms if implemented.

The positions adopted by legislators ahead of trilogues put forward amendments mainly concerning:

- definitions, timelines and scope of the regulation;
- incident/vulnerability reporting;
- expected product lifetime and distribution of responsibilities;
- amendments to the critical products list;
- automatic mandatory security updates; and
- professional skills in the cybersecurity field.

FS firms should monitor the upcoming final negotiations closely, as well as the relationship between implementing the CRA and the DORA. Firms should also monitor the potential for the FS sector to be exempted from the CRA through a Delegated Act.

We expect finalisation of the CRA by Q1 2024.

Closure of the EU ESAs' first batch of Consultations on secondary technical standards for the Digital Operational Resilience Act (11 September)

Technical standard setting for the EU's landmark DORA law gets underway

The DORA requires the European Supervisory Authorities (ESAs) to develop 13 secondary technical instruments in two distinct batches, respectively due by 17 January 2024 and 17 July 2024.

The ESAs published a first batch of Consultations on those technical instruments, including four Regulatory Technical Standards (RTSs) and one Implementing Technical Standard (ITS) as set out below:

- **RTS on ICT risk management framework:** provides technical detail on the framework firms need to maintain under the DORA, including areas such as security policies, incident detection/response, and business continuity.
- **RTS on simplified ICT risk management framework:** outlines a simplified version of the framework above for small and medium-sized firms.
- **RTS on criteria for the classification of ICT-related incidents:** proposes classification criteria, materiality thresholds, and relevance criteria for ICT-related incidents and cyberthreats.
- **ITS on templates for the register of information:** sets out the templates firms should use to establish a register of information to be regularly shared with the Competent Authority.
- **RTS on policy for ICT third-party providers:** outlines the content of the policy FS firms need to implement for third-party providers supporting critical or important functions.

The Consultations are open for responses until 11 September 2023. The ESAs will then have to finalise and submit them to the European Commission by 17 January 2024.

Scott Martin
Associate Director, Cyber and Operational Resilience lead

The year so far:

2023 was always going to be a year of significant regulatory activity on cyber and operational resilience, especially in the EU where the DORA entered into force in January. The ESAs have now initiated the lengthy process of drafting the technical standards necessary for the DORA's implementation in January 2025. Over the course of this year, FS firms in both the EU and UK have seen mounting supervisory pressure to advance their operational resilience work and show their readiness to implement the new regulatory frameworks being put in place.

Looking ahead…

- *Implementation of the Operational Resilience regimes.*
- *Oversight of Critical Third Party Providers (CTPs).*
- *Cybersecurity and resilience of the ICT supply chain.*
- *Cyber incident reporting frameworks in the EU and UK.*

What to watch out for

- Second batch of EU Consultations on secondary technical standards for the DORA - Q4.
- Final negotiations on the EU Cyber Resilience Act - H2.
- UK Consultation on CTPs oversight - H2.
- UK Consultation on incident, outsourcing and TP reporting - Q4.