

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

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Financial Regulation Monthly Breakfast Webcast

Overview





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Operational resilience and outsourcing
Gabriel Lakeman

Operational Resilience and Outsourcing

- FCA, PRA and BoE have published the outcome of major work on Operational Resilience and Outsourcing:
 - New policy framework on Operational Resilience:
 - New sections of FCA Handbook and PRA Rulebook;
 - BoE policy statements for various FMIs; and
 - New and updated supporting material including: FCA and PRA Policy Statements (PS 21/3 & PS 6/21); FCA and PRA joint covering document; PRA Supervisory Statement SS1/21; PRA Statement of Policy; FCA microsite
 - New PRA Supervisory Statement on Outsourcing:
 - New PRA Supervisory Statement SS2/21 and accompanying Policy Statement PS7/21
- Proposals pre-date, but given added focus by, the Coronavirus pandemic

Scope of the Regimes

- **FCA requirements:** banks, building societies, designated (dual regulated) investment firms, insurers, recognised investment exchanges, enhanced scope SMCR firms, and payment institutions, registered account information services providers and electronic money institutions
- **PRA requirements:** banks, building societies, designated (dual regulated) investment firms, and insurers*

In its original consultation paper, the FCA raised the prospect of broader application: “[a]fter we publish our final rules, we will consider whether the proposals should be applied to other firms.” (CP19/32).

* PRA outsourcing requirements also apply to branches of overseas banks and insurers, and credit unions and non-directive firms

Key Themes

Some key themes across the frameworks:

- **Focus on service delivery:** regimes intended to ensure continued provision of services in light of operational disruption (both internal and third-party)
- **Regulatory alignment:** FCA and PRA aiming at regulatory alignment across separate regimes
- **Non-prescriptive approaches:** FCA and PRA have set out extensive guidance, but allowed for firms to take proportionate approaches in light of their different business models.

OpRes: Overview

FCA and PRA operational resilience regime is a new regulatory framework

At high level, requires firms to:

1. identify important business services;
2. set, and ensure these services remain within, specified impact thresholds;
3. maintain appropriate systems to ensure this is the case, including dependency mapping and scenario testing; and
4. conduct self-assessments and ensure senior management oversight

Requirements are dynamic and subject to ongoing review obligations

OpRes: Important Business Services (1 of 2)

- *Firms* are required to identify *important business services*

Definitions of “important business service”	
FCA	PRA
<p>A service provided by a firm, or by another person on behalf of the firm, to one or more clients of the firm which, if disrupted, could:</p> <ol style="list-style-type: none">1. cause intolerable levels of harm to any one or more of the firm’s clients; or2. pose a risk to the soundness, stability or resilience of the UK financial system or the orderly operation of the financial markets	<p>a service provided by a firm, or by another person on behalf of the firm, to another person which, if disrupted, could pose a risk to:</p> <ol style="list-style-type: none">1. where the firm is an O-SII, the stability of the UK financial system; or2. the firm’s safety and soundness

OpRes: Important Business Services (2 of 2)

Identifying important business services:

- The FCA has chosen *“not to publish a prescriptive taxonomy for firms to use when identifying their important business services”*, but has provided handbook guidance in SYSC 15A.2.4G
- *“A firm’s important business services will be a relatively short list of external-facing services for which the firm has chosen to build high levels of operational resilience in anticipation of operational disruption”*

PRA SS1/21

Examples:

- **Important business services:** client subscription/redemption request processing (asset manager); provision of an e-wallet (payment firm); provision of cash withdrawals (retail bank)
- **Not important business services:** internal services (e.g. payroll); central shared services (e.g. IT)

OpRes: Impact Tolerances (1 of 3)

- Firms are required to set *impact tolerances* for important business services, and ensure they can remain within them in the event of a *severe but plausible disruption* to their operations

Definitions of “impact tolerances”

FCA	PRA
means the maximum tolerable level of disruption to an important business service, as measured by a length of time in addition to any other relevant metrics, reflecting the point at which any further disruption to the important business service could cause intolerable harm to any one or more of the firm’s clients or pose a risk to the soundness, stability or resilience of the UK financial system or the orderly operation of the financial markets.	means the maximum tolerable level of disruption to an important business service or an important group business service as measured by a length of time in addition to any other relevant metrics.

OpRes: Impact Tolerances (2 of 3)

Setting impact tolerances for each important business service:

- Must be time-based metrics, setting out point at which further disruption to the important business services will cause intolerable harm
- Can use other metrics in addition to time, and can consider quantitative and qualitative indicators of intolerable harm
- No prescriptive guidance on thresholds or definition of what constitutes “intolerable harm”, however various regulatory guidance in FCA Handbook/PRA SS1/21 to assist firms in setting relevant levels

Examples: 2 hour disruption to provision of e-wallet; £x failed withdrawals.

OpRes: Impact Tolerances (3 of 3)

Remaining within impact tolerances:

- Firms are required to ensure they can stay within impact tolerances in the event of a severe but plausible disruption to their operations
- Dual regulated firms:
 - Application of the PRA and FCA's objectives may lead to differing tolerances under the respective regulators' rules
 - In practice, firms can focus on the more stringent tolerance, provided they have considered the PRA and FCA's objectives, have appropriate recovery and response arrangements in place, and have conducted appropriate scenario testing

OpRes: Systems, Mapping and Scenario Testing

- **Strategies, processes and systems:** firms are required to have in place sound, effective and comprehensive strategies, processes and systems to comply with the requirements
- **Mapping:** firms must identify and document the necessary people, processes, technology, facilities and information required to deliver each of its important business services
 - No prescribed format for conducting the mapping exercise: this must be documented in a proportionate way
- **Scenario testing:** firms must carry out regular scenario testing of their ability to remain with the impact tolerance for each of their important business services in the event of a severe but plausible disruption to their operations

OpRes: Governance and Self-Assessment

- **Self-assessment:** firms are required to make and update written self-assessment records of their compliance with the important business services requirements, to be provided to the relevant regulator on request
- **Governance:** governing body is required to sign off on identification of important business services, impact tolerance levels, and the firm's self-assessment

OpRes: Implementation Timeline



Phased introduction: by start of transitional period on 31 March 2022, firms must have:

- identified important business services and impact tolerances; and
- performed mapping and commenced scenario testing, however not to a full level of sophistication

Outsourcing: PRA Supervisory Statement SS2/21

- PRA has published a new Supervisory Statement on Outsourcing, SS2/21, implementing the EBA Guidelines on Outsourcings
- PRA states it has not materially diverged from the EBA Guidelines, and so many of the requirements will be familiar
- Some key differences:
 - PRA refers to “material”, rather than “critical or important” outsourcings, however the definitions will generally align
 - PRA expects firms to assess the materiality and risks of all third-party arrangements, in a proportionate manner, irrespective of whether they fall within the definition of outsourcing
 - PRA provides additional guidance on data security, and on business continuity and exit planning

Outsourcing: PRA Supervisory Statement SS2/21

Next steps:

- SS2/21 due to come into effect from 31 March 2022.
- Firms are no longer required to comply with the timeline for review of legacy outsourcing arrangements set out in the EBA Guidelines (31 December 2021)
- PRA is planning a follow-up consultation for an online portal for submission of outsourcing registers



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The Hill Review of the listing rules
James Inness

The Hill Review (The UK Listings Review) - Introduction

- The UK Listings Review, chaired by Lord Hill, was launched by the Chancellor on 19 November as part of a plan to strengthen the UK's position as a leading global financial centre
- The UK Listings Review was published on 3 March
- *The UK needs strong public markets. Not merely because they are a way of companies funding growth and investment which in turn creates jobs and pays wages across the countries and regions of the UK. But because increasing the opportunities for investors to share in that growth helps spread wealth. Strong and deep capital markets drive the economy, spread risk, and they help people to build up their savings and plan for old age*

The Hill Review (The UK Listings Review) - Introduction

- *Looking at our relative performance and the range of feedback we have had, it is clear that the current listing regime is in need of reform. As well as examples of over-complexity, duplication, overly long timescales and unnecessary and burdensome requirements, there are signs that the lack of flexibility in the premium listed segment in particular is playing a part in driving business to our competitors*

The Hill Review (The UK Listings Review) – Key Proposals

- SPACs
 - Response to wave of SPAC transactions in the US and now Euronext Amsterdam, but not London
 - Rule presuming suspension of a SPAC's listing on announcement of an acquisition to be removed. This means shareholders will continue to be able to trade a SPAC's shares post acquisition announcement, provided certain requirements are complied with
 - Additional investor protections proposed at the time of the acquisition – such as giving shareholders the right to vote on whether or not to proceed with the acquisition and also the right to redeem their investment when the acquisition takes place if they so choose
- Forward-looking financial information
 - Inclusion of forward-looking information in prospectuses (at IPO and afterwards) to be made easier by amending the liability regime for issuers and their directors

The Hill Review (The UK Listings Review) – Key Proposals

- Free float requirements
 - Reduction in the free float requirement from 25% to 15%
 - Allowing more choice for companies of different sizes to use measures of liquidity other than an absolute free float percentage
 - Larger cap companies should be able to demonstrate minimum numbers of shareholders and publicly held shares as well as a minimum market value of publicly held shares and minimum share price to support a liquid market
 - Smaller cap companies should have an agreement with an authorised broker to use best endeavours to find matching business in the absence of a registered market maker
 - Definition of free float to be reviewed and updated to consider whether the shares are in fact contributing to liquidity

The Hill Review (The UK Listings Review) – Key Proposals

- Dual class share structures
 - Dual class share structures to be allowed on the FCA's Premium Listing Segment (such structures are currently only permitted on the Standard Listing Segment)
 - Certain limitations to apply e.g. maximum duration of 5 years, maximum weighted voting ratio of 20:1, 'B' class shareholders to be company directors, limitations on 'B' class share transfers
- Financial track record
 - Extension of the revenue earning relaxations currently enjoyed by scientific research based companies to other high growth innovative companies
 - Financial track record requirements applicable to companies that have grown by acquisition to be simplified – "75% rule" to apply to most recent financial period only, not the entire 3 year track record

The Hill Review (The UK Listings Review) – Key Proposals

- Prospectuses
 - Whole purpose of the prospectus to be re-examined
 - Content requirements for public offer prospectuses and admission to regulated market prospectuses to be treated separately
- Standard Listing Segment repositioning
 - Name to be changed to Main Segment and segment to be repositioned and promoted more effectively
 - Companies on the Main Segment to be index-eligible

The Hill Review (The UK Listings Review) – Key Proposals

- FCA statutory objectives
 - FCA should be charged with the duty of expressly taking into account the UK's overall attractiveness as a place to do business
- Retail investors
 - Use of technology to improve retail shareholder involvement in corporate actions and their ability to undertake a stewardship role to be considered
 - Rules applicable to further capital raises to be amended to make them quicker, more efficient and more retail shareholder friendly
- Connected research analysts
 - Review to be conducted of the relatively recent rules relating to the inclusion of unconnected research analysts in an IPO process, which in practice have added a week to the IPO timetable

The Hill Review (The UK Listings Review) – Next Steps

- Some of the recommendations will require changes to primary legislation and as such will take some time to implement
- Other recommendations could be implemented relatively quickly by the FCA following the required consultation process
- FCA announced on 31 March that it will launch a consultation in relation to SPACs shortly and the consultation is to be open for a 4-week period with a view to implementing the revised rules in short order



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Brexit – the MoU between the UK and the EU
Anne Mainwaring

MoU on UK-EU regulatory co-operation

- HMT announced on 26 March that technical discussions on the text of the MoU on UK-EU regulatory co-operation in financial services had concluded
- The MoU, once signed, will create the framework for voluntary regulatory cooperation in financial services between the UK and the EU
- The MoU will establish the Joint UK-EU Financial Regulatory Forum which will serve as a platform to facilitate dialogue on financial services issues
- HMT expectation is that the formal steps to signing can be undertaken expeditiously on both sides

Genesis of the MoU

- Non-binding joint declaration on financial services regulatory cooperation was made alongside the UK-EU Trade and Cooperation Agreement published in December
- This declaration set out an intention to agree by March 2021 a MoU to facilitate structured regulatory cooperation on financial services, with the aim of establishing a durable and stable relationship between autonomous jurisdictions
 - Bilateral exchanges of views and analysis relating to regulatory initiatives and other issues of interest
 - Transparency and appropriate dialogue in the process of adoption, suspension and withdrawal of equivalence decisions
 - Enhanced cooperation and coordination including in international bodies as appropriate

Impact of the MoU

- Substantively no change
- Equivalence remains an autonomous and unilateral decision to be taken by the EU – the EU has been clear that it will only make equivalence decisions where it is in its interests to do so



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Conduct and Culture – latest regulatory insights
David Berman

Recent developments

- Two important FCA speeches from earlier this year – both focused on diversity and inclusion (more shortly)
 - Georgina Philippou (Senior Advisor to FCA) 21 January
 - Nikhil Rathi (CEO, FCA), 17 March
- Increasing broader focus on diversity and inclusion
 - ESG context
 - Leading financial institution pronouncements / expectations
 - Both from sell-side and buy-side

Some instructive recent quotes from the FCA

- *“How a firm prioritises and embeds diversity and inclusion are clear indicators of its culture ... It is the responsibility of everyone in the financial services industry to create and maintain cultures which embody diversity and inclusion”*
 - D&I: key elements / indicators of culture
 - How to define D&I?
 - Goal: to avoid ‘group-think’ and ensure that fresh and relevant perspectives are brought to bear → better decisions

Some instructive recent quotes from the FCA

- *“Leaders must acknowledge their status and actively recognise how their behaviour and actions can influence and support an environment of psychological safety and collaboration”*
 - Importance of self-awareness and empathy
 - Behavioural issues often an underlying cause of toxic environments
 - Do we really appreciate the importance of role-modelling?
 - Are we equipping our managers with the necessary skill-sets?

Some instructive recent quotes from the FCA

- *“Not only do people need to be able to ‘speak up’, leaders need to ‘listen up’ when they do. When employees do speak out, the response of an organisation is key to determining whether they or their colleagues will feel safe to do so again. Leaders have a very important role to play – one small mis-step from a senior person can undermine a brilliant strategy and years of action”*
 - Importance of meaningful response and feedback – goes to the integrity / perception of speak-up culture

Some instructive recent quotes from the FCA

- *“We introduced 5 conduct questions to help focus minds of senior managers on conduct risk. I would like to see this expanded – and a sixth added – for all firms: is your management team diverse enough to provide adequate challenge and do you create the right environment in which people of all backgrounds can speak up? This is much broader than representation. It is about a firm’s culture. Not just in relation to diversity, but inclusion, too. Do people feel comfortable in the work environment such that they can demonstrate, share and bring to bear their diversity of experience and background?”*

Some instructive recent quotes from the FCA

- *“In the years ahead, if we don’t see improvements in diversity at senior levels and better answers, we will also consider how to best use our powers. There are supervisory tools we can draw on. For example, I want to consider whether the diversity of management teams – and the inclusivity of the management culture they create – could be part of our consideration of senior manager applications”*
 - Likely 6th conduct question – two-limbed:
 - Diversity of thought and adequate challenge
 - Speak up environment suitable for employees of all backgrounds

Some instructive recent quotes from the FCA

- *“We also need to look hard at the way capital markets work. In the US, we have seen the Nasdaq take the lead with its listing rules, which will require all companies listed on its US exchange to have, or explain why they do not have, at least two diverse directors. As part of our regulatory work on diversity and inclusion and the listings framework, we will be exploring whether we should make similar requirements part of our premium listing rules. Many investors are already taking the lead in this area. One leading investment bank will only underwrite IPOs in the US and Europe where the company listing has at least one diverse board member. They said they would raise this target to two diverse candidates for each IPO client next year”*
 - Direction of travel seems clear ...
 - ESG, #Metoo and #BLM movements only likely to accelerate momentum

ESG Disclosure Landscape for Banks and Capital Markets in Europe

Latham & Watkins has collaborated with the Association for Financial Markets in Europe (**AFME**) to produce: The European ESG Disclosure Landscape for Banks and Capital Markets, a new report designed to help financial institutions navigate Europe's increasingly complex ESG reporting landscape.

[To access the report please click here.](#)



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