

WELCOME



TODAY'S TOPICS

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- Nigel Brahams, Partner & Head of Financial Services
Crypto regulatory update
- Hardeep Tamana, Co-founder & MD - Avenir Registrars Ltd
Next-gen digital registrars
- Abbie Coleman, Associate
FCA's Consumer Duty
- Robin Henry, Partner & Head of Commercial Disputes
FCA – A New Approach to Non-Financial Misconduct
- Q & A



CRYPTO REGULATORY UPDATE - FEB' 24

NIGEL BRAHAMS, PARTNER
& HEAD OF FINANCIAL SERVICES

08/02/2024

FUTURE FINANCIAL SERVICES REGULATORY REGIME

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- **HM Treasury Consultation and call for evidence February 2023**
- *“The government’s firm ambition is for the UK to be home to the most open, well-regulated, and technologically advanced capital markets in the world.”*
- *“The government’s view is that cryptoassets and the activities underpinning their use should follow the standards expected of other similar financial services activities.”*
- **Phase 1 and Phase 2 Implementation**
- **Financial Services and Markets Bill 2022 lays legislative foundations to bring stablecoins and cryptoassets into financial services regulation**

FUTURE FINANCIAL SERVICES REGULATORY REGIME - PHASE 1

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1. **Anti Money Laundering Regime** - introduced for Cryptoassets in January 2020 with FCA registration compulsory from January 2021
2. **Financial Promotion Regime** extended to cover Cryptoassets in October 2023
3. **Fiat-backed Stablecoin Regime** - used for payments - next phase of cryptoasset regulation. *FCA Discussion Paper 23/4* – FCA seeking views from industry and public

FUTURE FINANCIAL SERVICES REGULATORY REGIME - PHASE 2

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1. Issuance activities

- Admitting a cryptoasset to a cryptoasset trading venue
- Making a public offer of a cryptoasset

2. Operating a cryptoasset trading venue for exchange of cryptoassets for

- (i) other cryptoassets (ii) fiat currency or (iii) other assets (e.g. commodities)

3. Investment activities

- Dealing in cryptoassets as principal or agent
- Arranging (bringing about) deals in cryptoassets / Making Arrangements

4. Lending, borrowing and leverage - Operating a cryptoasset lending platform

5. Safeguarding and /or administration (custody) activities

PHASE 2 (IMPLEMENTATION)

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- Government's long-term intention to expand the list of "specified investments" in Part III of the RAO to include cryptoassets
- FS&M Bill 2022 amends Section 22(4) FSMA to allow inclusion of "cryptoassets" under the definition of "investments" in RAO as secondary legislation
- Persons undertaking activities involving cryptoassets "by way of business" would be performing regulated activities and require Part 4A of FSMA authorisation
- FCA would have the power to write and amend their Handbook rules and regulatory regimes for newly added activities
- Cryptoasset firms would be subject to same financial crime standards and rules under FSMA as regulated firms. Financial crime rules in FSMA broader than MLR, covering anti-bribery and corruption, sanctions, fraud etc...

AML REGIME FOR CRYPTOASSETS

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- 5MLD brought into English law via insertion of new Reg 14(A) into the MLRs 2017
- Since 10th January 2020, FCA AML/CTF supervisor of certain UK cryptoasset businesses.
- Since 10 January 2021 “cryptoasset exchange provider” and “custodian wallet provider” required to register with FCA for AML / CTF financing purposes
- **Cryptoasset** “a cryptographically secured digital representation of value or contractual rights that uses a form of distributed ledger technology and can be transferred, stored or traded electronically”

- **Since 8 October 2023, via an amendment to Financial Promotion Order 2005 as amended (FPO), all firms marketing cryptoassets to UK consumers, including firms operating from overseas, required to comply with UK's fin prom regime**
- **What is a financial promotion?** *An invitation or inducement to engage in investment activity which could have an effect in the UK*
- **Section 21 of FSMA restricts a person from communicating promotion unless:**
 - They are an FCA **authorised person** (with Part 4A FSMA permissions); or
 - The promotion has been approved by an authorised person (with Part 4A FSMA permissions); or
 - An exemption in the FSMA (Financial Promotion) Order 2005 (FPO) applies, such as the promotion being made to a high net worth or sophisticated investors.

FINANCIAL PROMOTIONS (2)

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- The FCA's Conduct of Business (COB) Rules require that all financial promotions must be clear, fair and not misleading
- Communication to a retail customer requires greater disclosure and explanation. Note also new obligations under Consumer Duty
- Real time vs. non-real time financial promotions
- A real time financial promotion means a live meeting or telephone call where A attempts to sell B some form of financial service or product. Cryptoassets almost always promoted via direct offer non-real time financial promotions, i.e. websites, mobile apps, social media posts and online advertising

- **What cryptoassets are covered by the new rules?**
- **FPO defines a “cryptoasset” as** *“any cryptographically secured digital representation of value or contractual rights that: (a) can be transferred, stored or traded electronically, and (b) uses technology supporting the recording or storage of data (which may include distributed ledger technology);”*
- **The FPO defines a “qualifying cryptoasset” as a cryptoasset which is transferable and fungible (i.e. interchangeable as per cash) – this includes BTC, Ether, Tether etc; but not NFTs (which by their nature are unique and non-fungible)**
- **Also excluded are crypto products which are already covered by the existing FCA regulatory framework, i.e. “electronic money” or “controlled” investments, i.e. deposits, equities, futures, fund units. etc...**

- **Health Warnings & Cooling Off Period** - Any firm promoting or endorsing cryptoassets is now required to ensure that potential buyers have the appropriate knowledge and experience to invest in crypto
- **All promotions must contain clear risk warnings. Products targeted at retail customers, must contain a range of mandatory health warnings.**

Example from the FCA's COB rules:

“Don’t invest unless you’re prepared to lose all the money you invest. This is a high-risk investment and you should not expect to be protected if something goes wrong.”

- **24-hour one off cooling off period which applies the first time a consumer requests to view a Direct Offer Financial Promotion of cryptoassets from a specific firm**

STABLECOINS (1)

WHAT ARE STABLECOINS?

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- **What is a Stablecoin?** *“a category of cryptoassets that aim to maintain a stable value relative to a specified asset, or basket of assets, providing perceived stability when compared to the high volatility of unbacked cryptoassets”.* DP 23/4
- **What assets can back a stablecoin?** Usually a country's currency, such as the US dollar, but can be other assets (i.e. gold, real estate etc...)
- **More than 200 fiat currency backed cryptoassets**
- **Major Stablecoins:** Tether (USD), USDC (USD), Binance Dollar (USD), DAI (Ethereum backed assets approved by “Maker Governance.”), Paypal USD
- **Total stablecoin market capitalisation of \$123.4 billion**

STABLECOINS (2) UPCOMING LEGISLATION

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- **Under FS&M Bill, Government is taking forward legislation to enable HMT:**
 - to bring activities such as issuance and custody of fiat-backed stablecoins into FCA regulatory perimeter via statutory instrument (under FSMA)
 - to establish via statutory instrument a mechanism for facilitating dual regulation (to fall under the remit of the FCA, the Bank of England and the PSR)
- **Amends to Electronic Money Regulations 2011 (EMRs) & Payment Services Regulations 2017 (PSRs) to apply regimes to fiat-backed stablecoins used in retail payments**

STABLECOINS (3) ISSUANCE & CUSTODY

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- **FCA will regulate the issuance and custody of fiat-backed stablecoins under FSMA**
- **Stablecoin backing assets:** discussion re acceptable backing assets. Probably limited to short-term cash deposits and government treasury debt instruments (maturities of one year or less – discussed shorter dated)
- **GBP and other fiat-backed stablecoins expected to be in scope**

STABLECOINS (4) PAYMENT SERVICES

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- Proposed extension of Payment Services Regulations 2017 (PSR) to cover use of stablecoins as a means of payment in UK
- PSRs work by regulating the transfers of 'funds', including transfers of non-cash and electronic money but currently do not capture transfers of value through other assets, i.e. cryptoassets / stablecoins, unless already within definition of EMoney
- May allow greater and cheaper money transfer liquidity and cross border payments

STABLECOINS (5) OTHER ISSUES

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- SYSC / SMCR to regulated stablecoin issuers and custodians. FSCS?
- FCA proposes stablecoin issuers and custodians to be subject to Consumer Duty
- Omnibus vs individual wallet structure
- Separation of custody from other services, custodians already. Whoever holds need permissions

Next-Gen Digital Registrars

Collyer Bristow - Financial Services Update Seminar

Avenir Registrars Limited



An introduction....

- What is meant by digital registrars?
- What is 'next generation'?
- Why change?
- Why Avenir?



Process of Digitisation

The three steps towards Digitisation:

- Paper vs digital mechanisms
- Security
- Dividend cheques



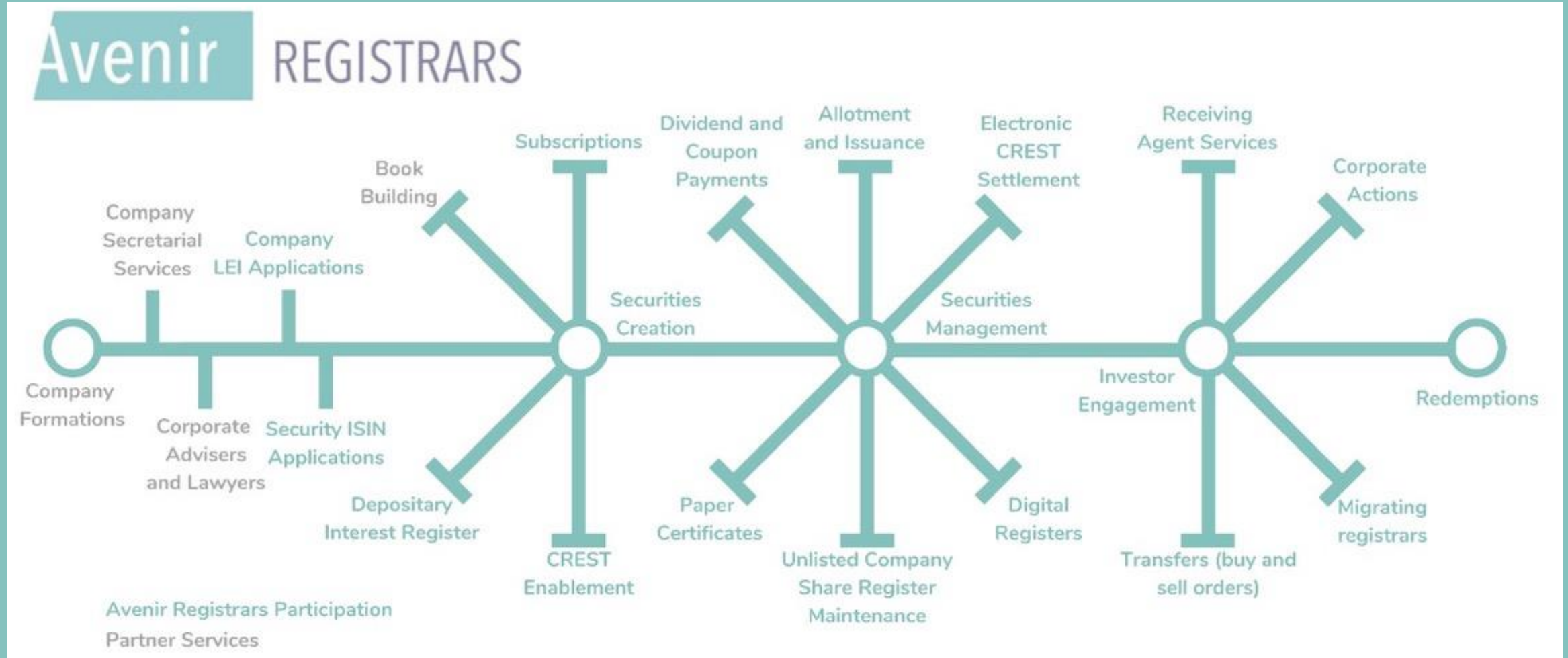
Benefits of Digitisation

Whilst the digitisation taskforce is an evolving project, issuers can begin future-proofing their procedures and reap the benefits of digitisation now:

- Key savings achievable by going paperless.
- Operate digital and paper share certificates side-by-side.
- Meet ESG goals



The Roadmap: From Inception to Redemption



Find us:

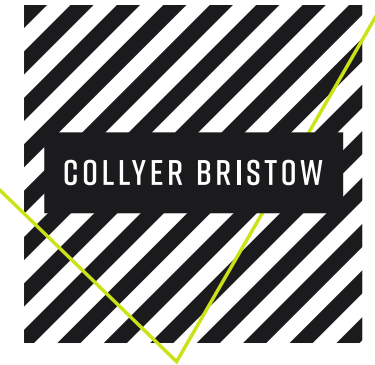
UK: <https://avenir-registrars.co.uk>

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CONSUMER DUTY

ABBIE COLEMAN, ASSOCIATE, COMMERCIAL DISPUTES

FCA CONSUMER DUTY

Recap



How it's been
going so far
(enforcement &
litigation)



Looking
ahead

FCA CONSUMER DUTY - WHAT IS IT?

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Rationale

Provide higher and clearer standards of consumer protection

Applies to

All **regulated providers of financial services** when they are dealing with **retail customers**

FCA CONSUMER DUTY - WHAT IS IT?

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New Principle

A firm must act to deliver good outcomes for retail customers

Cross-Cutting Rules

1. Act in good faith towards retail customers
2. Take reasonable steps to avoid foreseeable harm
3. Enable and support retail customers to pursue their financial objectives

Outcomes

1. Communications
2. Products & Services
3. Customer Service
4. Price & Value

Put retail customers at the heart of decisions

Recap



**How it's been
going so far
(enforcement &
litigation)**



Looking
ahead

HOW IT HAS GONE SO FAR

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- Do we have clarity yet?



- Use your own judgment
- FCA Head of Competition Policy, Ed Smith – “A good outcome will depend on the context, including the size of firm, the client base and the products and services that firm supplies”.
- More ‘detailed’ guidance coming

- What have some firms done?



ENFORCEMENT

- FCA
 - Prioritising the most serious breaches
 - “The worst offenders who are at risk of having the biggest impact on our financial services industry”
- Financial Ombudsman Service
 - Chief Executive, Abby Thomas: “We have started to receive complaints where the duty might be a consideration, and we will continue to engage with firms and the FCA through the year”

LITIGATION

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Action by retail customers

Private right of action?

Implied terms?

Breach of contract or tort?

Action between regulated firms

Duty applies to all firms within a distribution chain

Include obligations in contracts?

Recap



How it's been
going so far
(enforcement &
litigation)



Looking ahead

Applies to closed products from 31 July 2024

- *A closed product is one which is no longer marketed or distributed to retail customers, nor open to renewal*
 - Applicability

Crypto

- *Promotions are subject to the Consumer Duty*
- *More care needs to be taken over what financial products are accessible to retail customers*
- *But that doesn't mean high risk investment products are off the table*

FCA CONSUMER DUTY SUMMARY

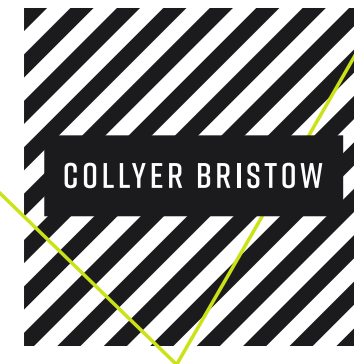
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We still don't have clarity
But that doesn't mean firms
can be complacent

We need to keep up to date
with how the Consumer Duty
is developing

FCA is taking enforcement
action & FOS is receiving
complaints already

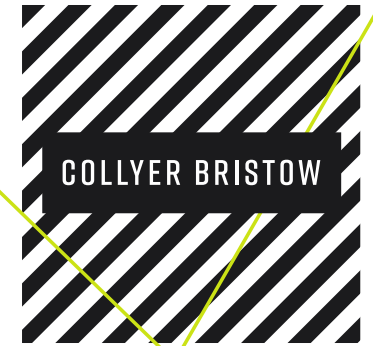
If in doubt, reach out to the
FCA for guidance



A NEW APPROACH TO NON-FINANCIAL MISCONDUCT

ROBIN HENRY, PARTNER
& HEAD OF COMMERCIAL DISPUTES

08/02/2024



PSYCHOLOGICAL SAFETY
& HEALTHY WORK
ENVIRONMENTS

RECENT INCREASE
IN PUBLIC
SCRUTINY E.G.
CRISPIN ODEY

***WHY SUCH
A HOT
TOPIC?***

PROPOSED APPROACH IS
CONSISTENT WITH OTHER
REGULATORS

MAINTAIN PUBLIC
CONFIDENCE IN THE
FINANCIAL SYSTEM

WHAT IS NON-FINANCIAL MISCONDUCT?

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- **Not defined by the FCA but includes:**
 - Sexual misconduct
 - Bullying
 - Harassment
 - Discrimination
- **Lack of clarity and consistency in cases so far**
- **Currently governed by:**
 - FCA *Fitness and Proprietary Test* (FIT 1.3)
 - COCON Rules 1 and 2

- **Fit and proper test applies to** anyone carrying out an approved FCA function **(or a candidate)**
- **No prescriptive rules but the most important considerations are:**
 - Competence, capability
 - Honesty, integrity, and reputation
 - Financial soundness
- **The test is ‘continuing’ – approval can be withdrawn**
- **Non-financial misconduct has previously been taken into account:**
 - Dishonesty outside work
 - Sexual offences outside work (e.g. Frensham case)

NON-FINANCIAL MISCONDUCT

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- **FCA conduct rules (COCON)** apply to all financial services staff
 - **Rule 1** - Acting with integrity
 - **Rule 2** - Acting with due skill, care and diligence
- **Breaches of COCON are taken into account in “fit and proper test”**
- **To date conduct rules only applied to performance of functions relating to financial activities**
- **So behaviour wholly outside work has not been regarded as an issue**
- **But new rules to be provided by 2025**



THE NEW APPROACH

NEW RULES AND GUIDANCE
PROPOSED BY THE FCA

- FCA propose to explicitly include NFM within COCON rules

Rule 1: Acting with integrity

- Scope of rule expanded to cover bullying & harassment
- Rules will also clarify what conduct is “out of scope” i.e. personal/private
- Disciplinary action only to be taken for ‘serious breaches’
- Emphasis on ‘intention’ not ‘effect’

- **Rule 2:** *Acting with due skill, care and diligence*
- **Managers may be liable for failing to adequately deal with non-financial misconduct**
- **New rules relating to Rule 2:**
 - Not protecting staff from activities breaching Rule 1
 - Not taking seriously or dealing with complaints effectively
- **Regulatory actions by Lloyds of London against CFC Underwriting and Atrium**
- **Odey Asset Management**

- FCA also proposing to amend Fit and Proper Test
- Matters out of scope of COCON because personal or private may still be taken into account for fitness and propriety
- *“Misconduct ... outside the regulatory system may show the person lacks moral soundness, rectitude and steady adherence to an ethical code, which in turn raises doubts as to whether they will follow the requirements of an ethical system”*

Questions





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