Consultation Paper

10/18**

Financial Services Authority

Implementing aspects of the Financial Services Act 2010

Feedback on CP10/11, final rules and further consultation

Financial Services Authority

July 2010

Contents

This Consultation Paper reports on the main issues arising from Consultation Paper 10/11 *Implementing aspects of the Financial Services Act 2010* and publishes final rules and guidance, including a new Handbook module, the Financial Stability and Market Conduct sourcebook.

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This Consultation Paper also extends the consultation period for our proposals to allow the Financial Services Compensation Scheme (FSCS) to recover management expenses from FSCS levy payers when it is acting for another scheme. This consultation periods ends on 23 August 2010.

The Financial Services Authority invites comments on this extended consultation. Comments should reach us by 23 August 2010.

Comments may be sent by electronic submission using the form on the FSA's website at (www.fsa.gov.uk/Pages/Library/Policy/CP/2010/cp10_11_response.shtml).

Alternatively, please send comments in writing to Sonal Vyas (contact details above).

It is the FSA's policy to make all responses to formal consultation available for public inspection unless the respondent requests otherwise. A standard confidentiality statement in an email message will not be regarded as a request for non-disclosure.

A confidential response may be requested from us under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Tribunal.

Copies of this Consultation Paper are available to download from our website – www.fsa.gov.uk. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

List of acronyms used in this Consultation Paper

CESR	the Committee of European Securities Regulators
COMC	the Code of Market Conduct
CP	Consultation Paper
DEPP	the Decision Procedure and Penalties Manual
ECHR	European Convention on Human Rights
EG	the Enforcement Guide
ETF	Exchange Traded Funds
FEES	the Fees Manual
FINMAR	the Financial Stability and Market Confidence sourcebook
FSA	Financial Services Authority
FSCS	Financial Services Compensation Scheme
FSMA	the Financial Services and Markets Act 2000
MAD	the Market Abuse Directive
MAR	Market Conduct
RDC	Regulatory Decisions Committee
SRR	Special Resolution Regime
The Act	Financial Services Act 2010

1 Overview

Introduction

1.1 On 26 April 2010 we published a Consultation Paper, CP10/11, which described our proposals on implementing aspects of the Financial Services Act 2010 (the Act).[1] It was published with a shortened consultation period for the reasons set out in paragraph 1.8, in the overview chapter of CP10/11, and the consultation closed on 25 June 2010.

1.2 We received 26 consultation responses.

The contents of this Consultation Paper

1.3 This Consultation Paper (CP) reports on the feedback we received and sets out our policy response to most of the areas covered in CP10/11. The exception is the proposed amendments to the FEES rules to allow the FSCS to recover management expenses in relation to acting for other compensation schemes. The consultation for this has been extended until 23 August 2010 to enable respondents to consider the cost benefit analysis and compatibility statement, which were omitted from CP10/11. The rules, if we decide to make them, are likely to be made in September, but only once we have considered the responses received during the extended consultation. By that stage we should also have greater clarity on when the provisions in the Act, which prompted the consultation, are brought into force.

1.4 As a result this CP covers:

- short selling disclosure rules (see Chapter 2);
- using our new enforcement powers (see Chapter 3);
- the financial stability information-gathering power (see Chapter 4);

1 See www.fsa.gov.uk/pages/Library/Policy/CP/2010/10_11.shtml.

- alterations to the FEES manual, to reflect amendments made by the Act in relation to the FSCS's contribution to the costs associated with resolutions under the Banking Act 2009 (see Chapter 5); and
- interim feedback and the extended consultation on the proposal to allow the FSCS to recover management expenses from FSCS levy payers when it is acting for another scheme (see Chapter 5).

1.5 With the exception of the FEES amendments noted at 1.3 above, the rules and guidance in this CP will come into force on 6 August 2010.

1.6 To ensure that we are in a position to satisfy our revised regulatory mandate and use the new powers parliament has given to us as promptly as possible, we have framed our policy response to the consultation responses on a shorter than usual timetable. A list of consultation responses received appears at Annex 1.

1.7 We did not receive any responses regarding the proposed consequential amendments reflecting changes made by the Act. The proposed amendments will be made to the FSA Handbook without change.

Short selling disclosure rules

1.8 In CP10/11 we set out our proposals to use the new powers in the Act to create new FSA rules and guidance concerning short selling. The new rules and guidance will form part of the Financial Stability and Market Confidence sourcebook (FINMAR). As regards the measures included in FINMAR, we proposed essentially to roll forward the short position regimes currently made under the Code of Market Conduct (COMC), except for one change which would narrow the scope of the rights issue disclosure obligation. The effect of this change would be that the disclosure regime would be restricted to UK companies and companies for whom a UK prescribed market is the main or sole trading venue for their securities. Our proposals – and in particular the proposal to separate short selling provisions from the market abuse regime – received a general welcome. The narrowing in scope of the rights issue regime was also supported. We therefore intend to proceed on this basis. In light of the comments received relating to the costs and benefits of the proposed requirement to take positions held through indices, baskets and Exchange Traded Funds (ETF) into account when calculating whether a disclosable net short position was held, we have decided to convert this into guidance to allow more flexibility in its application. This is the only change from our consultation proposals.

Using our new enforcement powers

1.9 In CP10/11 we set out our proposed policy for the following new enforcement powers given to us under the Act:

- the power to impose suspensions or restrictions on authorised and approved persons (the 'suspension power');

- the power to impose penalties on persons that perform controlled functions without approval (the 'non-approved persons penalty power'); and
- the power to impose financial penalties on persons who breach short selling prohibition rules or short selling disclosure rules (the 'short selling penalty power').

1.10 Respondents thought the list of examples of circumstances where we may consider it appropriate to impose a suspension was helpful. They agreed with several of the circumstances listed, but disagreed with others – in particular, the use of the suspension power where we consider it appropriate to reduce the proposed penalty because it would cause serious financial hardship. Respondents were also concerned that the suspension power would be used as a matter of course in the case of any breach, and that it would be used disproportionately. They suggested that the power should only be used as a last resort to address serious breaches. They also believed we would find it difficult to judge whether the combined effect of a suspension and a financial penalty will be disproportionate given that the financial consequences of a suspension are unpredictable and imprecise.

1.11 We believe that all the listed examples of circumstances where we may impose a suspension are appropriate, including where a financial penalty is reduced for serious financial hardship reasons. We also think we should be able to use the suspension power whenever it is appropriate to do so, which will not necessarily be in the most serious cases. We will decide the appropriate level of both suspensions and penalties by considering all relevant evidence. Except for some minor amendments, we are therefore proceeding with the proposed policy for the suspension power.

1.12 Respondents thought that, where an individual performs a controlled function without approval, it may often be more appropriate to take action against a firm, rather than the individual, especially where the firm decides which members of staff it should obtain approval for. We have clarified that this may be a relevant factor, which we would take into account in deciding whether to take action against the individual. We have made a few other minor amendments, but otherwise we are proceeding with the proposed policy for the non-approved persons penalty power.

1.13 Respondents raised no objections to our proposed policy for the short selling penalty power, so we are proceeding with it.

The financial stability information-gathering power

1.14 In CP10/11 we set out our proposed policy for the new financial stability information-gathering power we were given under the Act. The responses we received relating to our policy were broadly positive, with most respondents agreeing with the approach set out and the factors to be taken into account in both non-urgent and urgent procedures. We have considered the various suggestions and comments made by respondents about the consultation questions, and we believe that our policy already takes sufficient account of their concerns. We are therefore proceeding with the proposed policy. The policy will form part of the new FINMAR.

Alterations to the FEES manual

1.15 The consultation has not, to date, led us to change our proposal to change the FEES Manual to allow for the FSCS to recover management expenses from FSCS levy payers when it is acting for another scheme. However, due to an administrative error, we are extending the consultation period to 23 August 2010 and will consider any additional responses before making any rules in September 2010. We will proceed with making the changes to the FEES manual to reflect amendments made by the Act in relation to the FSCS's contribution to the costs associated with resolutions under the Banking Act 2009.

CONSUMERS

We did receive comments on our proposals from consumers or consumer bodies.

No issues of significant relevance to consumers have arisen since we published CP10/11.

2 Short selling rules

Introduction

2.1 This chapter summarises the responses to our proposals for the rules and guidance on short selling to be made under the new powers given to us by the Act and provides our feedback to them.

2.2 The new powers in the Act give us the ability to:

- require disclosure of information about short selling and prohibit short selling in specified cases;
- require information or documents to be produced to determine whether short selling rules have been contravened; and
- impose penalties or issue censures in the event a person has contravened short selling rules.

2.3 CP10/11 set out our proposals to remake the short selling disclosure measures as rules in a new module of our Handbook, FINMAR. The new rules would not be tied to the market abuse regime and the current short selling provisions in COMC would be deleted once these new rules come into force. We proposed that the two existing short position disclosure regimes – one for rights issue stocks and the other covering UK financial sector companies – would be carried forward largely unchanged in substance. However, we did propose a change to the rights issue disclosure regime to narrow the scope of the companies to which the regime applies.

2.4 We received 12 responses relating to short selling, the most significant of which came from three trade associations. Most of the other responses came from authorised firms and from an individual member of the public. We are grateful to all who responded.

Policy decisions

2.5 After taking into account all the comments we received, we have decided to go ahead with our proposals to include short selling provisions in the new FINMAR sourcebook. The new provisions will be carried forward substantively unchanged from the existing short selling provisions currently found in COMC, except for the narrowing of the scope of the rights issue disclosure obligation. This disclosure regime will now in effect be restricted to UK companies and companies for whom a UK prescribed market is the main or sole trading venue for their securities. In addition – in light of comments concerning costs and benefits issues, regarding the requirement to take positions held through indices, baskets and ETF into account when calculating a net short position – we are changing the proposed rule into guidance to provide more flexibility of application.

Feedback on policy proposals and our responses

2.6 This chapter sets out our feedback to the responses received to our proposals set out in Chapter 2 of CP10/11. Generally our proposals were well received.

Disclosure proposals

2.7 Firstly, we proposed that, pending the adoption of a permanent short selling disclosure framework, the two disclosure regimes (one for UK financial stocks and the other for rights issues) should be continued and that they should be enshrined in separate rules in our Handbook. This is because remaking the rules under the new powers will also allow us to bring greater legal certainty and clarity with little or no additional compliance burden for market participants.

> Q1: Do you agree with our proposal to re-cast the current disclosure obligations, contained in the Code of Market Conduct, as new FSA rules in the Financial Stability and Market Confidence sourcebook of the FSA Handbook?

2.8 All respondents agreed to our proposal that transferring the existing disclosure obligations, currently located in COMC, (also including matters contained in the FAQs about the current short selling regime) into FINMAR was in the best interests of the market and the FSA. Indeed, it was noted on more than one occasion that regulatory provisions on short selling would sit much better outside of the market abuse regime. It was argued that placing disclosure requirements on market participants under the market abuse regime could wrongly associate short selling, as an activity within itself, with market abuse. One respondent agreed in principle to our proposal but questioned whether the rights issue disclosure requirement was necessary since the Market Abuse Directive (MAD) should adequately cover this.

Our response: For the reasons set out in CP10/11 – and in view of the majority support for our proposals – using the new powers given to us in the Act, we will re-cast all the rules requiring those who hold significant net short positions in UK financial sector companies and companies engaged in a rights issue to disclose those positions and the identity of the position holder to the market as a whole. We continue to consider that a rights issue disclosure regime is necessary until a comprehensive short position disclosure regime is in place – MAD does not provide for this. Regarding whether or not the rights issue regime should be extended to IPOs and other types of issue, we think that it is important at this stage not to unduly complicate the existing regime, especially when neither of the two regimes is intended to be permanent and will be superseded by the prospective European short selling disclosure regime.

Scope of the regimes

2.9 We proposed not to extend the present scope of the disclosure obligations affecting net short positions held in UK financial sector companies as we consider this appropriate at this stage. Holders of significant net short positions in UK banks, UK insurers and the UK-incorporated parent undertakings of UK banks and UK insurers, as defined in the Glossary to the FSA Handbook, will still be required to disclose those positions.

2.10 We also proposed narrowing the scope of the current rights issue disclosure obligations, as we were conscious that the regime set out in MAR 1.9.2A applies to all companies admitted to trading on a prescribed market where the issuer is undertaking a rights issue. Our view was that the current scope potentially imposes a compliance burden that cannot always be justified. Our proposal is to reduce the scope so that it applies only to UK-incorporated companies and non-UK companies where a UK prescribed market is the main or sole venue for trading in a company's tradable securities.

Q2: Do you agree that it is appropriate to narrow the scope of the rights issue disclosure obligation as proposed?

2.11 Most respondents agreed that there was no need to modify the current disclosure obligations for those holding net short positions in UK financial sector companies. But one noted that those listed Lloyds vehicles who do not own a UK FSA-authorised insurance company would continue to fall outside the scope of the regime and argued that this could create a risk that such companies would be targeted by short sellers.

2.12 There was also broad agreement that it is appropriate to narrow the scope of the rights issue disclosure obligation. However, one respondent felt that the rights issue disclosure provisions should also apply to all premium-listed equities irrespective of whether a UK market is the main venue for trading the company's securities. Another respondent questioned why we had not also extended the rights issue regime to initial flotations or bonus issues.

Our response: For the reasons set out in CP10/11 – and in view of the overwhelming support for our proposals – we will maintain the scope of the disclosure obligation for holders of UK financial sector stocks and, as proposed, we will narrow the scope of the rights issue disclosure requirement. We consider the fact that a security is either premium-listed or standard-listed should not be the determinant of the scope of the disclosure obligations: the main/sole trading venue test is the key consideration here and follows the principles of the Committee of European Securities Regulators' (CESR) recommendations for a pan-European regime.

We have not seen evidence to justify the extension of the financial sector stocks regime to include those companies (including listed Lloyds vehicles) not currently covered in advance of the introduction of a comprehensive European short position disclosure regime. We will therefore carry forward the financial sector stocks regime with its current scope, although we will keep this under review. The disclosure regime is not intended to be permanent and will be replaced by a European disclosure regime when this has been finalised and adopted.

Disclosure thresholds

2.13 In remaking the regimes we consider it appropriate to maintain the existing disclosure thresholds for net short positions in UK financial sector companies and rights issue stocks. Currently, holders of net short positions of 0.25% and above in UK financial sector companies should disclose those positions to the market as a whole. When positions above 0.25% change by 0.1%, these should also be disclosed. A disclosure should also be made when the person's net short position falls below 0.25%. For rights issue stocks the requirement will continue to be to make a one-off public disclosure when the net short position reaches or exceeds 0.25%.

Q3: Do you have any comments on our proposal to maintain the disclosure requirements, including the thresholds, unchanged?

2.14 The majority of respondents agreed with our proposals that the thresholds set out above should remain in place without amendment. However, respondents urged that every attempt should be made to make the UK disclosure regime consistent with the disclosure thresholds across Europe when the pan-European regime comes into effect. They highlighted that inconsistencies in thresholds would create the biggest burden and highest cost for market participants. One other respondent would prefer aggregated disclosure, rather than individual disclosure of net short positions and argued that a lower threshold limit of 1% would suffice (i.e. not 0.25% as currently in place) with subsequent 0.25% bandwidths.

Our response: In light of the responses received, and based on our cost benefit analysis of short selling disclosure requirements in CP09/1, CP09/15 and DP09/1, we still consider that the costs of the disclosure obligations would be proportionate at the existing thresholds until a pan-European regime comes into force. We consulted on the issue of aggregate rather than individual disclosure when we conducted our major review of short selling last year. As noted in our feedback statement on this review (FS09/4), we do not believe that, in the UK context,

the informational benefits of a general requirement for collecting and disclosing aggregated short selling data are justified by the very significant additional costs involved.

How to calculate net short positions

2.15 We are also proposing to keep the methodology for calculating a short position in line with that for the existing regimes. Hence all economic interests in the issued capital of the issuer should be taken into account to determine the investor's economic exposure. The issued capital of a company has its ordinary meaning and includes ordinary shares and preference shares, but excludes debt securities (including convertible bonds). Among other requirements, any economic interest held as part of a basket, index or ETF would also need to be included. This also includes derivative products relating to an index. Calculations should be done on a net basis at the end of the day (not intra day). Calculating changes of short position should be undertaken in the same way as calculating a person's net short position.

Q4: Do you agree with the approach to calculation of net short positions, including changes of position, we propose? Are there any additional issues about which you believe we should make rules or provide guidance?

2.16 The majority of respondents either agreed in principle to our approach to the calculation of net short positions or did not comment on it. However, four respondents did raise concerns about having to take into account economic interests held as part of a basket, index or ETF. Of particular concern was the cost involved and how burdensome it would be to do the calculations in practice. One of these respondents was concerned that a cost benefit analysis had not been conducted when the requirement had been introduced in the UK financial sector companies regime and noted that the requirement did not exist in the rights issue regime. They considered that the costs of having to take such positions into account in the calculations outweighed the benefits of this requirement as an anti-avoidance provision.

2.17 Separately, the same respondent also argued that excluding convertible bond positions from calculations of short positions was a change to the existing regime for financial sector companies and would discourage market participants from subscribing to convertible bond issues by such companies. The same respondent also wanted implied short positions in nil paid rights not to have to be taken into account.

Our response: We intend to proceed with the approach to calculating net short positions as set out in CP10/11. However, given the comments on the question of positions held through indices, baskets and ETFs, we propose to change the provision from a rule into guidance. This will allow it to be applied flexibly. Market participants could (if they wished to) undertake the calculations of positions obtained through, inter alia, indices, on a best efforts basis. For example, it would not be necessary for them to have a daily feed of relevant data; historical information about the weighting of a stock in an index could be used instead provided it

was reasonably up-to-date. We will carry out a cost benefit analysis of the requirement and consult on this if we think that it is appropriate to change the status of the guidance to that of a rule.

Regarding whether positions in convertible bonds should be taken into account in calculating net short positions, we recognise that, while the prohibition on creating or increasing net short positions in UK financial sector stocks was in place, we had specified in an FAQ that a long position in convertible bonds could be hedged by a short position in the equity of the company. However, this lapsed when the prohibition lapsed and our FAQs for both the rights issues and financial sector stocks regimes have stated that, as far as the disclosure requirements are concerned, positions in debt securities are excluded. The proposals in CP10/11 therefore represent no change in this respect and we do not see a case for amending this, particularly in light of the fact that we are following CESR's recommended treatment of convertible bond positions under the prospective European short position disclosure regime. The question of implied short positions from nil paid rights under the rights issue regime was considered during the early days of that regime and we continue to consider it appropriate that such positions are taken into account in the calculations.

Netting

2.18 We also proposed to keep our approach to netting of short positions the same. Netting should be done at the legal entity level and not at the group level. If trading desks within a firm are housed within the same legal entity, the aggregate position of the trading desks within the legal entity should apply for these purposes, excluding positions taken under the market maker exemption (below).

Q5: Do you agree with the approach to netting of net short positions, that we propose? Are there any additional issues about which you believe we should make rules or provide guidance?

2.19 The majority of respondents agree with our approach set out in CP10/11 to the netting of net short positions. Several respondents made clear their full support for our decision to net at the legal entity rather than at the group level. There were no additional issues raised and no desire for further rules or guidance at this stage by any market participant.

Our response: For the reasons set out in CP10/11 – and given the consensus in feedback to this question – we will not change our approach to the netting of net short positions we have proposed.

Who is subject to the disclosure obligations?

2.20 Finally, we proposed that the disclosure obligation should continue to apply to the holder of the net short position (although, as we state in CP10/11, we recognise that where a person's investments are being managed by investment managers, they might authorise the investment manager or another person to make disclosures).

2.21 We also proposed that the market maker exemption should remain in place so that when market makers act in their genuine market making activity capacity, they do not need to disclose to the regulator their significant short positions. We believe market makers provide a vital role in the marketplace and without this exemption the markets would experience a significant loss of liquidity.

Q6: Do you have any comments on our proposals concerning who is covered by and who is exempt from the disclosure obligations?

2.22 All respondents concurred that there must be a market maker exemption. They agreed that the market maker exemption was vital for maintaining adequate levels of liquidity in the market. One market participant did note that market makers should still be required to privately report to the regulator.

2.23 One respondent, referring to our position on investment managers, questioned who has the responsibility and accountability to disclose a significant short position between two (or more) investment managers acting on a discretionary basis for the same client – they were concerned of the practical viability of this approach.

Our response: For the reasons set out in CP10/11 – and in light of the unanimity of support evident in the responses received, we will keep the market maker exemption in the current rules. We do not see significant benefits in requiring this, whereas there would be costs to market makers in having to do so. We also note that this would not be in line with CESR's recommendations for a European short position disclosure regime. Regarding the issue of investment managers acting on a discretionary basis, we note that the obligation is on the position holder to report disclosable short positions. If the client authorises the investment manager or another person to make disclosures, the client must ensure that they have all the necessary information to carry out this function.

3 Enforcement powers

Introduction

3.1 This chapter summarises the responses we have received regarding our proposed policies for the following new enforcement powers given to us under the Act (the 'new enforcement powers') and explains how we have addressed respondents' comments:

- the power to impose suspensions or restrictions on authorised persons, under section 206A of the Financial Services and Markets Act 2000 (FSMA), and on approved persons, under section 66 of FSMA (the 'suspension power');
- the power to impose penalties on persons that perform controlled functions without approval, under section 63A of FSMA (the 'non-approved persons penalty power'); and
- the power to impose financial penalties on persons who breach short selling prohibition rules or short selling disclosure requirements, under section 131G of FSMA (the 'short selling penalty power').

3.2 The new enforcement powers came into force on 8 June 2010. We set out our proposed policy on their use in Chapter 3 of CP10/11, and asked for comments on each of our proposed policies.

General comments

3.3 Respondents were of the view that we should use the new enforcement powers fairly and proportionately, and that our processes should be transparent. One respondent suggested that we undertake a review of their use and application at a fixed point in the future – for example, in two years time.

3.4 Respondents commented not just on our proposed policies for the new enforcement powers, but also on whether we should have been given them. Some respondents welcomed the new enforcement powers, while others questioned the need for them and wondered if they were a sign of our failure to adopt effective supervisory processes. One respondent was concerned that the risk of increased sanction will put

more pressure on persons to cooperate and admit culpability, and wanted it made clear that a person would not be considered uncooperative if they challenged our case for imposing a sanction.

3.5 Respondents were also concerned with other changes made by the Act which affect our enforcement processes but do not relate to the new enforcement powers. One respondent believed no case had been made in the Treasury White Paper for the amendment to section 66(4) of FSMA, which extended the time for taking action against an approved person for misconduct from two years to three years. They thought we should take account of the reputational and financial damage to a person of having possible enforcement action hanging over them for up to three years, and that we should not use the extra time to gather circumstantial evidence about a person's general behaviour in the market where it is quickly evident that the allegations have little merit.

3.6 Some respondents commented on the amendment made by the Act to section 391 of FSMA to allow us to publish decision notices as well as final notices. This change is subject to commencement by a Treasury Order. One respondent thought transparency around enforcement decisions is welcome, but we should also publish details where the Upper Tribunal clears a person of misconduct. Another respondent opposed the naming of a firm that is the subject of enforcement action before a final decision is made.

3.7 Respondents also commented on our general approach to enforcement. One respondent thought we should not rely on enforcement action to change firms' behaviour and that, in particular, we should not use final notices to do so; instead we should change our rules or guidance. They also thought it unhelpful to expect firms, especially small firms, to monitor a wide range of regulatory communications to understand our expectations, especially those relating to products they are not involved with. Another respondent thought our policies for using and applying our enforcement powers should also consider the nature and size of a firm, and the potential impact of the sanction upon it.

Our response: We are committed to using all our enforcement powers fairly, proportionately and transparently. In Chapter 2 of the Enforcement Guide (EG) we state at EG 2.2:

'(2) The FSA will seek to exercise its enforcement powers in a manner that is transparent, proportionate, responsive to the issue, and consistent with its publicly stated policies;

(3) The FSA will seek to ensure fair treatment when exercising its enforcement powers.'

We have no current plans to implement a review on the use of the new enforcement powers, but we would welcome comments as we start to implement the new policies.

Many of the comments we received concerned the appropriateness of the FSA gaining these new powers. However, CP10/11 concerned our proposed policies for these powers and therefore these comments fall outside the scope of the consultation.

We do not consider defending enforcement action, including challenging our case for imposing a sanction, amounts to a lack of cooperation.

Regarding the amendment to section 66(4) of FSMA, we do not intend to change our approach to taking enforcement action as a result of the extension to the limitation period

for taking action. While we note the comments received, we have not commented in this CP on the change to section 391 of FSMA given that this amendment is still subject to commencement by a Treasury Order.

We note the comments relating to our general approach to enforcement, which do not affect the policies we consulted on in CP10/11. We recognise that enforcement is one of a number of regulatory tools available to us and we do not rely solely on enforcement to change firms' behaviour. However, one of the main aims of enforcement action is to change firms' behaviour by deterring the firm that is subject to enforcement action, and others, from committing similar breaches in the future. We consider that final notices are an important method for us to set out to the industry our concerns with certain types of behaviour, and we have received feedback from industry that firms do change their behaviour as a result of final notices. We also think it appropriate to expect firms to take notice of enforcement action we have taken in relation to other products, as the same principles could apply to the sale of their products.

We take action where we consider it appropriate to do so, regardless of the nature and size of the firm concerned. We do take into consideration the potential impact of a sanction upon a firm, as is evident from our financial hardship policy and from our policy for determining the length of a period of suspension.

The suspension power

3.8 Where an authorised person has breached our rules, or other regulatory requirements, the suspension power enables us to suspend any permissions the person has to carry on a regulated activity, or to impose restrictions on the carrying on of a regulated activity by the person. Similarly, for approved persons, the suspension power enables us to suspend a person from performing one or more controlled functions for which they are approved, or restrict the performance by them of one or more controlled functions for which they are approved. We can impose a suspension[2] on an authorised person for a period not exceeding 12 months and on an approved person for a period not exceeding two years. Our policy for the suspension power is set out in a new chapter of the Decision Procedure and Penalties Manual (DEPP) – DEPP 6A.

3.9 We asked:

> Q7: Do you have any comments about our proposed policy for the suspension power?

3.10 In CP10/11 we explained that the suspension power is an additional disciplinary measure, which is a different type of sanction to a financial penalty. We proposed to use the suspension power where we consider that the imposition of a suspension will be a more effective and persuasive deterrent than the imposition of a financial penalty alone, and we provided a non-exhaustive list of examples of circumstances where we may consider it appropriate to use the suspension power.

2 For the purposes of this policy statement, as in the CP10/11, unless otherwise stated we will use the terms "suspension/suspend" to cover both the power to suspend and the power to impose limitations or other restrictions.

3.11 We also proposed that we would have regard to relevant factors in determining the length of the suspension period, and set out factors that may be relevant. We said we would decide upon a length that we consider appropriate for the breach concerned and is a sufficient deterrent, having regard to the relevant factors.

3.12 We also explained the approach we intended to usually take regarding the interaction between the suspension power and financial penalties. This approach was to determine independently whether each sanction was appropriate and, if so, the length of the suspension period and level of penalty. We would then look at whether the combined impact of both sanctions would be disproportionate to the breach and, if so, reduce either or both of the sanctions.

3.13 Finally, we stated our intention for the Regulatory Decisions Committee (RDC) to be the decision maker for giving warning notices and decision notices for cases where the suspension power is used.

General comments

3.14 Respondents asked for clarification on several issues relating to the suspension power. One respondent wanted us to make it clear that the new power to suspend applies only to misconduct that took place after the power came into force. They also asked us to provide examples of limitations or other restrictions that may be imposed on those found guilty of misconduct, and disagreed with the statement in the proposed DEPP 6A.1.3 G that the principal purpose of sanctions is deterrence, arguing instead that it should be to impose the appropriate punishment on the wrongdoer for the misconduct.

3.15 In situations where we suspend a specific business area, respondents asked if we would also take separate enforcement action against an individual who worked in that area, and also what firms should do about employees who had not committed misconduct. We were also asked how we would publicise suspensions, including whether the suspension would appear on a person's entry in the FSA Register and, if so, how the scope of the suspension would be made clear.

3.16 Other respondents had queries relating to action that firms and individuals would have to take as a result of the suspension power being used. One respondent wondered what compensatory and other arrangements firms would have to put in place if a consumer product was suspended. Another respondent questioned whether firms and individuals would have to re-apply for authorisation and approval respectively after the suspension period ends, and also what action or redress is available to a person if we wrongly decide to impose a suspension.

Our response: Our policy for the suspension power and the non-approved persons penalty power will come into force on 6 August 2010. We will only use these new enforcement powers in respect of misconduct that occurs on or after that date.

We have amended DEPP 6A.1.3 G to provide examples of limitations or other restrictions that may be imposed on a person who is guilty of misconduct. These examples are:

(i) We may limit an authorised person's carrying on of a regulated activity so that they can only sell certain products.

(ii) We may restrict an approved person's performance of their controlled functions so that they can only give advice to consumers or deal in certain products if they are appropriately supervised.

We have not made any changes to the statement in DEPP 6A.1.3 G that the principal purpose of sanctions is deterrence. We make the same statement in DEPP 6.1.2 G in relation to penalties and public censures, and we consider the statement is true in respect of all these sanctions.

We would take enforcement action against an individual, even if we were suspending the area in which they worked, if we thought it appropriate to do so. We consider it is for firms to decide how they should treat employees who are not guilty of misconduct when the area in which they work is suspended. We will adopt the same processes for publicising suspensions as we do for publicising other enforcement action. As set out in EG 6.8, this means we will ordinarily publish a final notice, often accompanied by a press release. We will also consider what information about the matter should be included on the FSA Register.

If a firm was restricted from selling a particular consumer product, we would expect firms to adopt suitable arrangements for providing compensation and other assistance to consumers. At the end of the suspension period, the suspended person would not have to re-apply for authorisation or approval; instead, their pre-suspension permissions or approvals would automatically resume. However, a person would have to apply for a new approval if, for example, they changed job during the suspension period.

If a person disagrees with an FSA decision to impose a suspension, they can make a referral to the Upper Tribunal. The same process applies as for other enforcement powers.

The circumstances in which we will use the suspension power

3.17 Many respondents accepted there may be cases where suspension is an appropriate enforcement action and thought the list of examples of circumstances was helpful. There was agreement with several of the circumstances listed: previous regulatory action against the person; failure to carry out a redress package or other remedial measures; and widespread misconduct on the part of a number of individuals.

3.18 However, one respondent thought the circumstances were too broad while others raised concerns with some of the circumstances listed. One respondent thought suspending a firm because we had previously taken action for similar breaches and had failed to improve industry standards was unrealistic in relation to market abuse cases, which take a long time to resolve. Another respondent disagreed with the possibility of suspending a person where their competitive position in the market had improved as a result of the breach because it would not be appropriate for the FSA to use an enforcement remedy to bring about a competition remedy.

3.19 There was most disagreement with the possible use of the suspension power where a financial penalty is reduced for serious financial hardship reasons. Respondents argued that it was difficult to envisage circumstances where this would be appropriate; that the suspension would exacerbate the hardship; that it may be

a disincentive to individuals claiming financial hardship; and that it is wrong in principle to re-open consideration of suspension on the basis of an individual's financial circumstances.

3.20 A couple of respondents objected to our proposal that suspension would not necessarily relate to the particular business area in which there had been a breach, for example, where the relevant business area had been restructured. They thought the power should only be applied to unrelated activities in exceptional circumstances.

3.21 An over-riding concern of respondents was that the suspension power would be used as a matter of course in the case of any breach, and that it would be used disproportionately. They suggested that, given the potentially serious consequences of suspension for a person, the power should only be used sparingly and as a last resort to address a real risk or breaches of a serious nature. To avoid it being used disproportionately, respondents suggested that we assess whether the desired outcome can be achieved through supervisory activity; that a person should be able to make representations before action is taken; and that evidence of misconduct should be robust, not circumstantial.

3.22 One respondent wanted a more explicit acknowledgement in our guidance of the potentially severe consequences of suspension, while another respondent thought that the potential impact on retail consumers means that the suspension power is likely to be used against firms almost exclusively in the wholesale context. We were also asked for more clarity on when we would suspend a firm rather than vary their permissions.

Our response: We have not made any changes to the list of examples of circumstances. These examples illustrate the situations when we may consider it appropriate to impose a suspension, and we do not consider the list to be too broad. However, the list is non-exhaustive as we think we need to have the option of being able to use the power in all circumstances where we consider it appropriate to do so.

We have still included the circumstance 'where the FSA has previously taken action in respect of similar breaches and has failed to improve industry standards' as we believe that suspension may be an appropriate response where firms do not appear to have been deterred by the fact that other firms have previously been disciplined for similar breaches. We have also kept in the circumstance 'where the person's competitive position in the market has improved as a result of the breach'. Section 2(3)(g) of FSMA provides that in discharging our general functions we must have regard to 'the desirability of facilitating competition between those who are subject to any form of regulation by the Authority'. We consider it appropriate to be able to use enforcement action where a person's competitive position has unfairly improved as a result of their breaches.

We recognise that in some cases it may not be appropriate to impose a suspension where a financial penalty has been reduced on the grounds of serious financial hardship. In DEPP 6A.4.3 G we state 'The FSA will take into account whether the person would suffer serious financial hardship in deciding the length of the period of suspension or restriction, and may decide not to impose a suspension or restriction if it considers such action would result in serious financial hardship'. However, we consider it appropriate to keep this circumstance in the list of examples as, for example, we may choose to suspend a person rather than impose a financial penalty which would cause them serious financial hardship.

We consider that DEPP 6A.2.4 G makes it clear that we will usually suspend a person from carrying out activities directly linked to the breach, but that sometimes it may be appropriate to suspend a person from carrying out activities not directly linked to the breach, and so we have made no changes to the guidance.

We note respondents' suggestions that we should only use the suspension power sparingly and to address breaches of a serious nature. However, we think we should be able to use the suspension power whenever it is appropriate to do so, which will not necessarily be in the most serious cases. We have therefore not changed our approach to using the suspension power.

We are not making changes to our usual enforcement practices and processes in terms of deciding whether to take action, the evidential standards that will apply, and the opportunity for persons under investigation to make representations. Our approach to enforcement is explained in chapter 2 of EG.

We do not consider it necessary to include in DEPP a statement on the severity of a suspension. The extent of the impact of a suspension will depend on the case, and we believe that the potential for the suspension to have a severe impact can be understood from the factors that we will take into account in considering its impact.

We will use the suspension power when we consider it appropriate to do so, having regard to our policy as set out in DEPP 6A. Although we will take into account the impact of suspension on consumers, we consider that there may be retail cases where we believe it is appropriate to use the suspension power.

We have amended DEPP to clarify when we would suspend a firm rather than vary their permissions. At DEPP 6A.1.4 G we make it clear that the suspension power is a disciplinary power and where we need to take action, for example, to protect consumers from an authorised person, we will seek to withdraw their authorisation or vary their permissions. Similarly, if we have concerns with an approved person's fitness, and consider it necessary to take action, we will seek to prohibit the approved person or withdraw their approval.

The length of the period of suspension or restriction

3.23 Respondents agreed that, in determining the length of the suspension period, it was appropriate to look at the impact of the suspension on the person in breach and on other persons. Some respondents asked for further details on what would be taken into account in assessing the impact. One respondent asked if compensation that would have to be paid to consumers following the suspension of a product line would be included in the calculation of the loss a firm incurs as a result of suspension. Another respondent suggested that we should look at the potential impact of suspension upon an individual's earnings over the remainder of their career, not just the period of suspension.

3.24 One respondent queried what we would do if there were unforeseen consequences of suspension – for example, if contractual obligations were breached, leaving the firm exposed to consequential financial penalties. They also thought that the suspension power would be much more likely to be used against smaller and newer businesses due to the potential impact on consumers of taking action against larger established businesses.

3.25 Another respondent thought the maximum length of the suspension periods, for both authorised persons and approved persons, was too short, although they thought they could be acceptable if, following the suspension, the person was required to re-train and to report cases to the FSA for the following few years.

Our response: We have amended DEPP 6A.3.2 G(4)(c) to make it clear that compensation that would have to be paid to consumers following the suspension of a product line would be taken into account in assessing the impact of suspension on a firm. We have made no changes to DEPP 6A.3.2 G(4)(f) as we think this makes it clear that we will seek to understand the potential impact of suspension on an individual.

As part of the enforcement process, persons will have the opportunity to make representations on the likely impact of suspension on them. If, having imposed a suspension, it has unforeseen disproportionate consequences, we have the power under section 206A(6) and section 66(3D) of FSMA to withdraw or vary the suspension. We do not anticipate using the suspension power only against smaller and newer firms; we will use it where we consider it appropriate to do so.

FSMA provides that the maximum length of the suspension power is one year for authorised persons and two years for approved persons, so we are not able to impose suspensions of longer periods of time. As suspension is a disciplinary measure, we do not consider it appropriate to impose specific requirements on the person once the suspension period ends.

The interaction between the suspension power and financial penalties

3.26 Some respondents welcomed our proposal to reduce the level of one or both of the sanctions if the combined effect of a financial penalty and suspension was disproportionate. However, another respondent thought it will be difficult to judge whether the combined effect will be disproportionate due to the fact a suspension is unpredictable and imprecise in its financial consequences. One respondent suggested that we should set out how we will take into account the actual loss incurred by a suspension when setting a financial penalty.

3.27 Respondents also believed that a suspension would usually have a greater impact on a person than a financial penalty. One respondent suggested that the proposed DEPP 6A.4.1 G should be revised to acknowledge this, while another thought that we would therefore often choose to impose a suspension.

3.28 Another comment was that it is unclear how those determining whether we should suspend or impose a financial penalty in an individual case will be separated – for example, through a Chinese wall – and how the enforcement staff will interact with both processes.

Our response: In DEPP we recognise the need to look at the proportionality of imposing both a penalty and a suspension. Although the impact of a suspension will be more difficult to assess, we will decide the appropriate level of both suspensions and penalties by considering all relevant evidence.

We do not believe that a suspension will necessarily have a greater impact on a person than a financial penalty. However, we have revised DEPP 6A.4.1 G to make it clearer that the deterrent effect and impact of a suspension, or the combination of a suspension and penalty, does not have to be limited to the level of a financial penalty; in many cases the deterrent effect and impact may be greater. As explained above, we will impose a suspension when we consider it appropriate to do so, in accordance with our policy set out in DEPP 6A.2.

It will be the same FSA staff who will decide whether we should seek to impose a suspension as who will decide whether we should seek to impose a penalty. But the use of the suspension power will be subject to the same internal checks, such as legal review by a lawyer independent of the investigation team, which exist for other FSA disciplinary action. We do not consider there to be any need for Chinese walls in this matter.

Decision maker

3.29 All respondents who commented on this issue agreed that the RDC should be the decision maker for giving warning notices and decision notices for cases where the suspension power is used.

Our response: We have made no changes to our proposed policy, so the RDC will be the decision maker.

The power to impose penalties on persons that perform controlled functions without approval

3.30 The non-approved persons penalty power enables us to impose a penalty on a person, of an amount we consider appropriate, if we are satisfied that:

a) the person has at any time performed a controlled function without approval; and

b) at that time the person knew, or could reasonably be expected to have known, that they were performing a controlled function without approval.

3.31 Our policy regarding the non-approved persons penalty power has resulted in amendments being made to Chapter 6 of DEPP.

3.32 We asked:

> Q8: Do you have any comments about our proposed policy for the non-approved persons penalty power?

3.33 In CP10/11 we proposed that DEPP 6.2 – which sets out our policy for deciding whether to take action to impose a financial penalty or public censure – would also apply when we decide whether to take action against a person who performs a controlled function without approval, but we would also have regard to certain additional considerations in such cases.

3.34 We also proposed that our new five-step policy for determining the level of a penalty to be imposed on individuals, set out in DEPP 6.5B, should apply when we

determine the appropriate level of penalty to impose on a person who has performed a controlled function without approval, but that additional factors should be included at steps two and three of that policy.

3.35 Finally, we stated our intention for the RDC to be the decision maker for giving warning notices and decision notices for cases where a penalty is imposed on a person who has performed a controlled function without approval.

General comments

3.36 Many of the comments we received regarding the non-approved persons penalty power did not relate to our proposed policy for its use, but instead were concerned with the implications of the new power for firms and individuals.

3.37 Several comments concerned the approval process, in particular the interaction between firms and individuals. One respondent asked for clarification that it is not just individuals who are responsible for approval. It was pointed out that, as the onus on obtaining approval is on firms, individuals will often be unaware that they could be subject to sanctions, and we were asked how we would publicise our policy to ensure non-approved persons are aware of the new power. There was also concern that the FSA and firms will spend lots of time agreeing categories of individuals requiring approval.

3.38 One respondent disagreed that, in a potentially criminal case, the onus should be on the individual to prove to the FSA that they did not know they were performing a controlled function without approval, when the onus was on the firm to obtain the approval – for example, in relation to proprietary traders who undertake activities that may have a significant influence on the firm and so may require approval for CF29. They were concerned that the impact of the new penalty power could be that many individuals will feel obliged to adhere to approved persons requirements, even if not performing a controlled function. They also questioned if the power would be found to be criminal in nature in terms of the European Convention on Human Rights (ECHR).

3.39 We also received comments on the scope of the approved persons regime. One respondent thought that the regime, as amended by PS 09/14: *The approved persons regime – significant influence function review*, does not provide legal certainty, so many firms will require comfort or further guidance from us about whether their current arrangements are compliant. Other respondents were concerned with the scope of the CF00 function, as proposed in CP10/3: *Effective corporate governance (Significant influence controlled functions and the Walker review)*. One respondent suggested there should be a presumption of reasonable ignorance if the firm has not informed a CF00 function holder (a person in a parent entity exercising a significant influence function) about the need for approval and the function holder is otherwise unfamiliar with the UK regulatory regime. Another respondent thought individuals of an overseas parent company that is removed from the regulated entity, or who sit on the board of an unregulated entity in a shareholder capacity only, should not be required to be approved as a CF00.

Our response: The non-approved persons penalty power does not make any changes to the approval process. As explained in SUP 10.12.3 G, it is the firm, not the individual, who must submit applications for approval. The new power provides that we can only impose such a penalty if we are satisfied that the person performing the controlled function without approval knew, or could reasonably be expected to have known, that they were doing so. Where a firm has decided that an individual does not require approval, and it was reasonable for the individual to rely on the firm's judgement, we will take this into consideration in deciding whether to take action. We have amended DEPP 6.2.9A G(5) to make this clear.

We do not intend to take any further steps to publicise the non-approved persons penalty power beyond this consultation process. We are not imposing any new requirements – instead the potential consequences for non-approved persons who perform controlled functions have changed. We expect further publicity to be given to the power when we first use it, as the use of the power will be outlined in final notices. We do not consider that ignorance of the new power is an excuse.

We expect firms already to be assessing which of their staff should be approved. If they are uncertain about whether a particular person needs approval, we would suggest that they approach their supervisors or our Permissions, Decisions and Reporting Division.

As the non-approved persons penalty power is concerned with the approved persons regime, we do not regard the penalty power as 'criminal' for the purposes of the ECHR and the Human Rights Act. In our view it is right to categorise a penalty imposed on an approved person as 'disciplinary' in nature; and it would be strange if a penalty imposed on a person who is seeking to escape from the approvals regime were to be considered a criminal sanction.

In respect of the comments on the scope of the approved persons regime, particularly regarding the scope of the CF00 function, we are considering the points raised and any further clarification will be given in the Policy Statement providing feedback on CP10/03, in which the CF00 function and a number of other changes to the approved person regime were proposed.

The circumstances in which we will impose a penalty on a person that has performed a controlled function without approval

3.40 Many of the comments on when we would use the non-approved persons penalty power also related to the relationship between the firm and the individual. Respondents thought that it may often be more appropriate to take action against the firm, especially where the firm decided who needed to apply for approval. They also thought we should speak with the firm before imposing such a penalty, and that both the firm and the individual should have an opportunity to make representations. We were also asked what we would do if the firm disagreed that the individual was performing a controlled function.

3.41 One respondent commented that we should only fine if the individual benefited from their actions. Another respondent thought we should not always assume that more senior individuals should have more knowledge of the regulatory regime, especially where the parent company is unregulated and the directors are outside the UK. They also thought it would be reasonable for senior executives to rely on their firm to ensure appropriate approvals are obtained, especially where the proposed CF00 applies.

Another respondent said it may not be clear if an executive within an unauthorised group company, with responsibilities for the business of the authorised firm, may require approved status, and asked us to clarify the position of such a person.

Our response: As mentioned above, whether it is appropriate to take action against the firm instead of the individual is one of the factors we will take into account in deciding whether to take action. We are not making any changes to our usual enforcement practices in terms of representations that can be made during the enforcement process. We will decide whether it is appropriate to take action on the basis of relevant evidence. If a firm or individual disagrees with our decision, they can challenge it by making a referral to the Upper Tribunal.

Whether an individual financially benefited from performing a controlled function without approval is a factor, but not the only factor, that we would take into account in deciding whether to take action.

DEPP 6.2.9A G(2)(c) states that one of the circumstances in which we would expect to be satisfied that a person could reasonably be expected to have known that they were performing a controlled function without approval is if their seniority or experience was such that they could reasonably be expected to have known this. That does not mean that we would assume that a senior individual should always be aware that they were performing a controlled function; their seniority will just be one factor that we take into account.

Also, as explained above, if a firm is unsure whether any of their staff requires approval, they can discuss the matter with their supervisor.

Other changes

3.42 We have amended DEPP 6.2.9A G(1). The draft version implied that we would take into account whether, if a person had been approved, all of their actions would have amounted to misconduct. The revised version makes it clear that we will take into consideration whether, if a person had been approved, any of the actions carried out in performing the controlled function would have constituted misconduct.

3.43 We have also amended DEPP 6.2.9A G(2)(b) to make it clear that it is the firm that applies for approval for a person to perform a controlled function.

How we will determine the level of penalty

3.44 The only comment on the determination of the level of penalty that we received was that we should not look at the individual's entire income from their employment, but just at the income relating to the controlled function that they were carrying out.

Our response: We consider that it is appropriate to look at the individual's entire income from their employment in connection with which the breach occurred. This is consistent with the new penalties policy as set out in DEPP 6.5B. It should also ensure the penalty is sufficiently high to be a credible deterrent.

Other changes

3.45 We have amended DEPP 6.5B.2 G(9)(r)(ii) and DEPP 6.5B.3 G(2)(o) to make it clear that it is the firm that applies for approval for a person to perform a controlled function.

3.46 One of the factors that we will consider in determining the level of penalty to be imposed on a person that performed a controlled function without approval is whether, while doing so, they committed misconduct for which, if they had been an approved person, we would have been empowered to take action under section 66 of FSMA. We have moved this factor from Step 3 to Step 2 of the new penalty framework as we consider it to be concerned with the seriousness of the conduct. It is now included at DEPP 6.5B.2 G(9)(q).

Decision maker

3.47 The only respondent who commented on this issue agreed that the RDC should be the decision maker for giving warning notices and decision notices for cases where a penalty is imposed on a person that has performed a controlled function without approval.

Our response: We have made no changes to our proposed policy, so the RDC will be the decision maker.

Other consequential changes relating to the non-approved persons penalty power

3.48 We have amended EG 7.2(2) to include reference to the fact that we may impose a financial penalty on a person that performs a controlled function without approval.

The short selling penalty power

3.49 Sections 131E and 131F of FSMA, as amended by the Act, provide that we have the power to require a person to provide information and documents that we reasonably require for the purpose of determining whether a person, or a person connected to them, has contravened any provision of short selling rules.

3.50 Section 131G of FSMA, as amended by the Act, provides that we have the power to impose a financial penalty or public censure on a person that contravenes any provision of short selling rules or any requirement imposed under sections 131E or 131F, or on a person who was knowingly concerned in the contravention.

3.51 We asked:

> Q9: Do you have any comments about our proposed policy for the short selling penalty power?

3.52 In CP10/11 we proposed that DEPP 6.2, which sets out our policy for deciding whether to take action to impose a financial penalty or public censure, would also apply to the short selling penalty power. We also proposed that our new five-step policy for determining the level of a penalty to be imposed, set out in DEPP 6.5 to 6.5D, should apply when we determine the appropriate level of penalty to impose when we use the short selling penalty power. Finally, we stated our intention for the RDC to be the decision maker for giving warning notices and decision notices for cases where the short selling penalty power is used.

General comments

3.53 One respondent thought that the short selling penalty power has the potential to be considered criminal in ECHR terms, and so the same safeguards as are set out in section 174(2) of FSMA should apply in relation to the short selling regime.

Our response: We do not consider the short selling penalty power to be criminal for ECHR purposes.

The circumstances in which we will use the short selling penalty power to impose a penalty

3.54 Respondents agreed with our proposed policy.

Our response: We have made no changes to our proposed policy, so DEPP 6.2 will also apply to the short selling penalty power.

How we will determine the level of penalty

3.55 Respondents agreed with our proposed policy.

Our response: We have made no changes to our proposed policy, so DEPP 6.5 to DEPP 6.5D will also apply to the short selling penalty power.

Decision maker

3.56 The only respondent who commented on this issue agreed that the RDC should be the decision maker for giving warning notices and decision notices for cases where the short selling penalty power is used.

Our response: We have made no changes to our proposed policy, so the RDC will be the decision maker.

4 Financial stability information-gathering power

Introduction

4.1 This chapter summarises the responses we have received regarding our proposed policy on the use of the financial stability information-gathering power, and explains how we have addressed respondents' comments.

4.2 In CP10/11 we set out our proposed policy on the use of the financial stability information-gathering power (the power) found in sections 165A and 169A of FSMA. The power applies to authorised and unauthorised persons and will assist us in identifying threats to financial stability, including developing threats and those arising from unauthorised entities' activities.

4.3 CP10/11 set out the scope of the power, with examples of types of entity that the power applies to and different types of information requirement. It then set out and consulted on: a) the factors we propose to take into account when deciding whether to impose a requirement in general; b) our approach to non-urgent cases; and c) the factors we propose to take into account when considering whether to impose a requirement without delay.

4.4 Overall, responses were broadly positive – 12 respondents made comments that related to the financial stability information-gathering power and, of these, seven responded specifically to the consultation questions on our policy for using the power. Six respondents agreed with all three questions (that is, they agreed with the approach set out and the factors to be taken into account in both non-urgent and urgent procedures), and one respondent agreed with the approach to both non-urgent and urgent cases, but requested that in general, all other sources of information should be exhausted first. Of the five respondents that commented in some way on the power but not on the specific questions, two of these respondents welcomed the power. One raised issues related to how we use the data we may collect under the power, and issues related to operation of the wider financial stability regime. We welcome these comments, but as the respondent recognised, they were not directly relevant for the consultation on our policy on the use of the power.

4.5 A number of the respondents raised further issues. Several respondents asked specific questions about the scope of the power and specific entities that may be caught by it.

These responses have been covered under the heading of scope below, while the remaining responses have been summarised and grouped under the three questions that were posed in Chapter 4 of CP10/11.

4.6 We have considered the various suggestions and comments made by respondents to the consultation questions, and believe that our policy already takes sufficient account of their concerns. In accordance with section 165B(7) of FSMA, the statement of policy in FINMAR has been approved by the Treasury.

Scope of the power

4.7 Two respondents raised specific queries about the scope of the power and specific entities that may be caught by it, seeking to clarify that they or their clients are not relevant to financial stability and would not be covered by the power. One respondent suggested that we could go further in providing more detailed guidance on the likely conditions of use and institutions covered, particularly for the benefit of unregulated entities as they may be less familiar with our approach to information requirements. This respondent also suggested that financial stability is a generic and imprecise concept, resulting in an uncertain scope for this power.

Our response: The Act sets out clearly the scope of the power. For the purpose of illustration, to supplement the text in the Act we have provided in CP10/11 and in our policy set out in FINMAR 1.1.6 a non-exhaustive list of examples of types of entity covered by the power. As we stated in CP10/11, the history of financial crises demonstrates that each is caused by a different combination of circumstances. As a result, it is not necessarily possible to look at the last crisis and identify the likely source of a future financial crisis and for this reason we cannot describe a concrete list of entities that, now or in future, will create risks to UK financial stability.

We may only use this power when information or documents are, or may be, relevant to UK financial stability (FINMAR 1.2.5). CP10/11 makes clear the wide range of factors and circumstances that may contribute to an entity becoming relevant to financial stability, and the complexity of issues surrounding this subject. The point at which an entity or instrument becomes relevant to financial stability will depend on, among other things: the size and liquidity of the relevant market; the proportion of the market the entity's investments account for; the interconnectedness of the entity to other market players; and the volatility of the market. Activities that may not be considered a risk to financial stability during 'normal' market conditions may, in fact, create such risks if the markets they relate to are under stress or become unusually volatile. Also, activities that may not pose risks to financial stability when undertaken on a small scale by a single participant may become relevant to financial stability if they are practised widely. Given this complexity, and the description of relevant factors and circumstances set out in CP10/11, we believe that our policy set out in FINMAR is appropriate.

Deciding whether to use the power

4.8 In CP10/11 we set out the factors that we propose to take into account when deciding whether to impose a financial stability information requirement. These include: the nature and extent of the risks to financial stability; whether the information is more readily available from another source; and whether information or documents already exist.

4.9 We asked:

> Q10: Have we identified the right factors to take into account in deciding whether to use this power?

4.10 Of the seven respondents that answered this question, six agreed that we had identified the right factors to take into account. The other respondent did not disagree with the factors, but suggested that we should only impose a financial stability information request when all existing data sources have been exhausted.

4.11 The respondents raised several further issues under this section. Two respondents suggested that we take greater account of the likely costs to firms in responding to information requests from us, and that information requirements should be justifiable on a cost-benefit basis. One respondent suggested that we take account of the difficulty that unregulated entities may have in responding to a requirement. Another respondent suggested that we seek to gather information that already exists where possible. One respondent suggested that the decision to impose a financial stability information request should be taken by at least an FSA director and not a Head of Department, and one respondent said that it was unclear how these powers will change existing powers.

4.12 One separate respondent, not addressing a particular consultation question, suggested that the Alternative Investment Fund Managers Directive should alleviate our concerns about being able to gather information from unregulated entities.

Our response: We welcome the range of responses to this question. As stated in CP10/11, when considering a particular information request, we would take into account the burden on affected firms to help us decide whether a request should be made of an entity or class of entities, and we would only impose a higher burden when we believe it would be justified in terms of a higher benefit. In relation to non-urgent requests, our policy set out in FINMAR 1.3.2(5) states that, in determining the period for representations, we will take into account any cost implications for the person. In relation to urgent requests, our policy in FINMAR 1.4.2(3) states that we will take into account information concerning whether it is fair to impose the requirement without notice, as described in CP10/11 – this includes recognition of the cost to impose an urgent request. With regard to deciding whether to require verification or authentication, FINMAR 1.5.6(2) states that we will take into account, among other things, the likely additional cost to the person. When taking account of these costs, we would consider whether they are proportionate to the expected benefits of the timescale or verification imposed under the requirement. We therefore believe that our policy takes sufficient account of the burden imposed on persons subject to a requirement.

Our policy for non-urgent requests in FINMAR 1.3.2 (4) states that, in determining the period for representations, we will take into account whether the person is an authorised person. This allows us to take into account the difficulties that unauthorised persons may face in responding to a request – for example, because they may need more time if they have not previously had to comply with one of our information requirements.

With regard to exhausting all existing data sources, our policy in FINMAR 1.5.1 (3)(b) states that, in deciding whether to impose a financial stability information requirement, we will take into account whether the information is more readily available from another source, taking into account the likely time and cost implications of seeking information from that source. We have also stated in CP10/11 that in deciding what to ask for, we would focus where possible on documents or information that already exists, rather than asking firms to generate new data or produce new documents. We believe this sufficiently takes account of concerns raised in these areas.

Regarding the suggestion that a director should take the decision to impose a requirement, our policy in FINMAR 1.5.2 states that 'A decision to impose the financial stability information requirement will be taken by a member of FSA staff at the appropriate level of seniority'. As stated in CP10/11 we expect our approach to be broadly in line with our existing approach to imposing information requirements; generally this is likely to involve a Head of Department or above. We believe that this policy gives us the flexibility required to make decisions rapidly if necessary, but is broad enough to demonstrate that the decision may be made by a more senior member of staff where appropriate.

We recognise that in relation to authorised persons, the financial stability information-gathering power overlaps to some extent with our existing information-gathering powers. In deciding which to use, we will consider which has the most appropriate scope, and which best describes the purpose of our request.

With regard to the Alternative Investment Fund Managers Directive, we believe there are currently, and will be in the future, entities that are not covered by the directive that may pose risks to financial stability. While the directive will give regulators greater access to information over persons within the scope of that directive, we believe that this power is required so that we can assess information on the full set of risks to financial stability to carry out our new financial stability objective.

We believe that we have identified the right factors to take into account when deciding whether to use this power, and that our policy sufficiently takes account of the comments received.

Non-urgent cases

4.13 We set out our approach to non-urgent cases, including: giving a person a notice in writing; the time period in which representations may be made; the factors we would take into account in determining whether the period for representations should differ from a 28-day period; and our views on written versus oral representations.

4.14 We asked:

> Q11: Do respondents agree with this approach to non-urgent cases?

4.15 All seven respondents that answered this question agreed with the approach to non-urgent cases. However, one of these respondents suggested that the policy should expressly allow for in-time requests for extension to the initial time limit.

Our response: It is encouraging that respondents agree with our approach to non-urgent cases. With regard to requests for extension, in FINMAR 1.3.1 we have stated that we will give a person a notice in writing if we propose to impose a requirement, and the notice would include the time period in which the person may make representations to us. As set out in CP10/11, we will take 28 days as a starting point for determining a reasonable period for representations, in line with our current warning notice procedure. A person would be able to request an extension as part of the representations they make. In FINMAR 1.3.2 we have also stated the factors that we will take into account in determining whether the period for representations should differ from the 28-day period. We believe that this is a sufficiently clear and flexible approach.

Imposing a requirement without delay

4.16 We set out the information and circumstances that we would take into account when determining whether to impose a requirement without prior notice, including: the nature and extent of the risks to financial stability and whether the risk appears to be increasing rapidly; whether it is fair to impose a requirement without notice; and whether the information sought may lead to us acting promptly.

4.17 We asked:

> Q12: Have we outlined reasonable factors to take into account when considering whether to impose a requirement without delay?

4.18 All seven respondents that answered this question agreed that we had outlined reasonable factors to take into account when considering whether to impose a requirement without delay. Three of these respondents suggested that this procedure should be reserved for the most urgent, or exceptional, circumstances, where there is an immediate risk to financial stability. One respondent also suggested that a decision to impose a requirement without delay should be taken by a director or above.

Our response: It is encouraging that respondents agree with our approach to urgent cases. Our policy in FINMAR 1.4 recognises that this procedure will only be used where information is needed without delay, based on the facts of each case, and after taking into account the nature and extent of the risk to financial stability and whether the risk appears to be increasing rapidly, whether it is fair to impose the requirement without notice and whether the information sought may lead us to prompt action. Our response to the issue of level of seniority here is the same as described in our response in the section on the non-urgent procedure above.

Cost benefit analysis and compatibility statement

4.19 There were no specific responses to the cost benefit analysis or compatibility statement.

Our response: As stated in CP10/11, we are not required to provide cost benefit analysis on proposed guidance. In considering a particular information request, we would take into account our new financial stability objective and the burden on affected firms to help us decide whether a request should be made. Any requests to firms would be carried out in a proportionate manner.

5 Compensation amendments

Introduction

5.1 This section deals with those measures in the Act relating to the FSCS. The Act made two amendments concerning the FSCS. First, the Act enables the FSCS to act on behalf the other schemes (UK and non-UK schemes). Second, it makes amendments in relation to the FSCS's contribution to the Special Resolution Regime (SRR) costs.

5.2 In Chapter 5 of CP10/11, we consulted on proposals to amend FEES 6 to:

i. allow for management expenses incurred by the FSCS, when acting on behalf of another scheme, to be recouped from FSCS levy payers if the FSCS has failed to obtain reimbursement of those expenses from the relevant scheme or government; and

ii. reflect amendments made by the Act in relation to the FSCS's contribution to the costs of resolutions under the Banking Act 2009 and to reflect section 61 of the Banking Act 2009.

5.3 This chapter summarises the responses we have received to the consultation so far. In regard to the first proposal only, we have extended the consultation period and will consider any further responses received by 23 August 2010. This is because we omitted to publish a compatibility statement and cost benefit analysis for this proposal in CP10/11. We had concluded that the costs of this proposal are of minimal significance and did not require a cost benefit analysis. However, while we concluded that no cost benefit analysis was needed, we should have nonetheless included a statement to that effect in the consultation. The extended consultation corrects this oversight. We have included a cost benefit analysis statement and a compatibility statement at the end of this chapter.

5.4 We do not propose making any rules in relation to the first proposal until September 2010, by which time we will have had the opportunity to consider any additional responses received. In addition, any rules will only have effect once the relevant provisions under the Act have come into force.

5.5 The draft instrument for the proposal on management expenses, which is subject to extended consultation, is in Appendix 3 (in Part 2 of Annex A and Part 2 of Annex B) of CP10/11 *Implementing aspects of the Financial Services Act 2010*.

FSCS acting as an agent on behalf of another scheme

5.6 The Act identifies a role for the FSCS to act on behalf of other compensation schemes. In CP10/11, we explained that s.224D of FSMA, as amended by the Act, provides for grounds on which the FSCS can decline to act on behalf of another scheme including, among other things, that the FSCS is not satisfied that it will be able to obtain the information and assistance it needs to act on behalf of the other scheme.

5.7 We also said that there could potentially be situations where the FSCS has started work on behalf of another scheme, but experienced difficulty in recouping the management expenses for this initial work from the other scheme or government. In practice, we believe that such a scenario will be rare. In the event that it does occur, we believe that the costs are unlikely to be material for individual levy payers (relative to other levies).

5.8 We proposed making rule changes in our FEES manual to allow for these costs to be recouped from FSCS levy payers should they arise. However, in doing so, we have sought to ensure that the rules make it very clear that the FSCS should have tried its best to obtain reimbursement of the expenses from the relevant scheme before it imposes any additional levies on FSCS levy payers.

Comments received on the specific question and our response

Q13: Do you agree with our proposal to amend FEES 6 to allow for the management expenses to be recouped from FSCS levy payers if FSCS has failed to obtain reimbursement of these expenses from the relevant scheme?

5.9 We received 14 responses in total to our proposal to amend FEES 6. While there was general support for the expanded role of the FSCS, a number of respondents did not agree with the proposals to amend FEES 6 to allow for management expenses to be recouped from levy payers if the FSCS failed to collect these expenses from the relevant scheme. One respondent strongly opposed the proposal, saying that if the government steps in to order the FSCS to act on behalf of the foreign scheme, then it should seek assurances and guarantees from the foreign government to cover any outstanding expenses. This respondent and a number of others felt that FSCS levy payers already pay a considerable amount to the FSCS and should not have to pay additional levies. Another respondent felt that FSCS should carry out the necessary due diligence on the extent to which its costs will be reimbursed by the overseas scheme before acting for the scheme in question. In the event that the FSCS was not reimbursed, they suggested that the UK government should meet the costs.

5.10 In total five respondents agreed with the proposal. Two agreed with all of its aspects, while another agreed, but urged that situations in which the FSCS acted for another scheme should be kept to a minimum. The other two respondents agreed with the proposal, but felt that there was a lack of clarity about the allocation of the costs across different levy payers.

5.11 One respondent felt that any such costs should only be charged against the relevant sub class. Another suggested that if these proposals are implemented the basis for calculation and allocation is published.

Our response: We have considered the arguments against levying FSCS levy payers received so far. We continue to believe that the financial impact on levy payers will not be significant. As the likelihood of the FSCS acting for another scheme is low, the costs involved are likely to be minimal and the FSCS will have made every effort to recoup these costs from the relevant scheme or government before it allocates the levy. Whether the Treasury will step in to meet any costs is a matter for it to decide.

As the expenses are expected to be minimal, we do not believe that it would be proportionate to produce a detailed methodology for allocating the costs.

We will consider any responses received during the extended consultation. Subject to anything further coming out of the consultation, we propose to recommend to our Board that the rules are made in September 2010. We will publish a summary of any further responses and our response to these in Handbook Notice 104, which is due to be published on 24 September 2010. If we do make these rules and associated guidance we will also communicate this in the Handbook Notice.

Amendments to reflect changes to the FSCS's contribution to SRR costs

5.12 Changes to FEES that arise from the second proposal, which reflects the fact that FSCS can be required to contribute to interest costs associated with resolutions under the Banking Act 2009 and reflects section 61 of the Banking Act 2009, will be made in July. There were no responses on this proposal.

Cost benefit analysis

5.13 Section 155 of FSMA requires us to publish a cost benefit analysis of the implications of the proposed amendments. The requirement does not apply if there will be no increase in costs or if any increase in costs will be of minimal significance.[3] Given the nature of the proposed changes here, we expect that costs arising from this proposal will be of minimal significance and therefore, the requirement does not apply.

3 Section 155 (8) of FSMA

Compatibility statement

5.14 When we issue rules for consultation, we are required by section 155(2)(c) of FSMA to explain why we believe our proposals are compatible with our general duties under section 2 of FSMA and our statutory objectives which are set out in sections 3 to 6 of FSMA. This is known as a 'compatibility statement'.

Compatibility with our statutory objectives

5.15 In discharging our duties we are required to act in a way that is compatible with our five statutory objectives (market confidence, financial stability, public awareness, protection of consumers and the reduction of financial crime).

5.16 The proposed changes to FSCS rules relating to it acting as an agent help us meet our consumer protection objective directly by ensuring that consumers covered by other compensation schemes do not lose out in the event that those schemes are unable to make payouts. Improving the effective operation of the FSCS also supports our market confidence and financial stability objectives. We do not expect the proposals to impact on the reduction of financial crime.

Compatibility with the principles of good regulation

5.17 Section 2(3) FSMA requires that, in carrying out our general functions, we must have regard to the principles of good regulation. Of these, the principle that the burden of our amendments should be proportionate to the benefits is particularly relevant to our proposals.

5.18 The FSCS proposals will enhance consumer protection, but we do not expect the associated costs to be material.

Annex 1

List of non-confidential respondents

Association of Accounting Technicians

Association of British Credit Unions Limited

Association of British Insurers

Aviva Plc

Berwin Leighton Paisner LLP

Bluefin Insurance Services Limited

British Bankers Association

Consumer Panel

Hewitt Associates Limited

IG Index Limited

IG Markets Limited

Institute of Credit Management

International Financial Data Services (UK) Limited

Investment Management Association

JWG

Kingsley Napley LLP

Lloyds

Lloyds Banking Group Plc

Paradigm Risk Limited

Prudential Plc

Rosaline Attardo-Alake

The Alternative Investment Management Association Limited

The Association of Private Client Investment Managers and Stockbrokers

The City of London Law Society

Appendix 1

Enforcement powers (Financial Services Act 2010) Instrument 2010

ENFORCEMENT POWERS (FINANCIAL SERVICES ACT 2010) INSTRUMENT 2010

Powers exercised

A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000:

(1) section 63C(1) (Statement of policy);
(2) section 69(1) (Statement of policy);
(3) section 131J(1) (Statement of policy);
(4) section 157(1) (Guidance);
(5) section 210(1) (Statements of policy); and
(6) section 395(5) (The Authority's procedures).

Commencement

B. This instrument comes into force on 6 August 2010.

Amendments to the Handbook

C. The Glossary is amended in accordance with Annex A to this instrument.

D. The Decision Procedure and Penalties manual (DEPP) is amended in accordance with Annex B to this instrument.

Amendments to the Enforcement Guide

E. The Enforcement Guide (EG) is amended in accordance with Annex C to this instrument.

Citation

F. This instrument may be cited as the Enforcement Powers (Financial Services Act 2010) Instrument 2010.

By order of the Board
22 July 2010

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text.

breach in *DEPP*:

…

(4) behaviour amounting to *market abuse*, or to *requiring or encouraging market abuse*, in respect of which the *FSA* takes action pursuant to section 123 (Power to impose penalties in cases of market abuse) of the *Act*; ~~or~~

(5) a contravention of any directly applicable *EU* regulation made under ~~MiFID~~ *MiFID*; or

(6) a contravention in respect of which the *FSA* is empowered to take action pursuant to section 131G (Breach of short selling rules etc: Power to impose penalty or issue censure) of the *Act*.

Annex B

Amendments to the Decision Procedure and Penalties manual (DEPP)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1.1 Application and Purpose

Application

1.1.1 G This manual (*DEPP*) is relevant to *firms, approved persons* and other *persons*, whether or not they are regulated by the *FSA*. It sets out:

…

(2) the *FSA's* policy with respect to the imposition and amount of penalties under the *Act* (see *DEPP* 6);

(2A) the *FSA's* policy with respect to the imposition of suspensions or restrictions, and the period for which those suspensions or restrictions are to have effect, under the *Act* (see *DEPP* 6A);

…

Purpose

1.1.2 G The purpose of *DEPP* is to satisfy the requirements of sections 63C(1), 69(1), 93(1), 124(1), 131J(1), 169(7), 210(1) and 395 of the *Act* that the *FSA* publish the statements of procedure or policy referred to in *DEPP* 1.1.1G.

…

2 Annex 1G Warning notices and decision notices under the Act and certain other enactments

…

Section of the Act	Description	Handbook reference	Decision maker
...			
63(3)/(4)	when the *FSA* is proposing or deciding to withdraw approval from an *approved person**		*RDC*

63B(1)/(3)	when the *FSA* is proposing or deciding to impose a penalty on a *person* under section 63A*		*RDC*
…			
126(1)/ 127(1)	when the *FSA* is proposing or deciding to impose a sanction for *market abuse**		*RDC*
131H(1)/ (4)	when the *FSA* is proposing or deciding to take action against a *person* under section 131G*		*RDC*
…			
207(1)/ 208(1)	When, in respect of an *authorised person*, the *FSA* is proposing or deciding to publish a statement ~~in respect of an *authorised person*~~ (under section 205) or impose a financial penalty ~~on an *authorised person*~~ (under section 206) or suspend a *permission* or impose a restriction in relation to the carrying on of a *regulated activity* (under section 206A)*		*RDC*
…			

6.1 Introduction

6.1.1 G *DEPP* 6 includes the *FSA's* statement of policy with respect to the imposition and amount of penalties under the *Act*, as required by sections 63C(1), 69(1), 93(1), 124(1), 131J(1) and 210(1) of the *Act*.

…

6.2 Deciding whether to take action

…

6.2.9 G Where disciplinary action is taken against an *approved person* the onus will be on the *FSA* to show that the *approved person* has been guilty of misconduct.

Action under section 63A of the Act against persons that perform a controlled

function without approval

6.2.9A G In addition to the general factors outlined in *DEPP* 6.2.1G, there are some additional considerations that the *FSA* will have regard to when deciding whether to take action against a *person* that performs a *controlled function* without approval contrary to section 63A of the *Act*.

(1) The conduct of the *person*. The *FSA* will take into consideration whether, while performing *controlled functions* without approval, the *person* committed misconduct in respect of which, if he had been approved, the *FSA* could have taken action pursuant to section 66 of the *Act* and, if so, the seriousness of that misconduct.

(2) The extent to which the *person* could reasonably be expected to have known that he was performing a *controlled function* without approval. The circumstances in which the *FSA* would expect to be satisfied that a *person* could reasonably be expected to have known that he was performing a *controlled function* without approval include:

(a) the *person* had previously performed a similar role at the same or another *firm* for which he had been approved;

(b) the *person's firm* or another *firm* had previously applied for approval for the *person* to perform the same or a similar *controlled function*;

(c) the *person's* seniority or experience was such that he could reasonably be expected to have known that he was performing a *controlled function* without approval; and

(d) the *person's firm* had clearly apportioned responsibilities so that the *person's* role, and the responsibilities associated with it, were clear.

(3) The length of the period during which the *person* performed a *controlled function* without approval.

(4) Whether the *person* is an individual.

(5) The appropriateness of taking action against the *person* instead of, or in addition to, taking action against an *authorised person*. In assessing this, the *FSA* will take into consideration the extent of the culpability of an *authorised person* for the *person* performing a *controlled function* without approval. For example, a relevant factor may be that an *authorised person* decided that the *person* did not need to obtain approval and it was reasonable for the *person* to rely on the *authorised person's* judgment.

(6) The *person's* position and responsibilities. The more senior the *person* that performs a *controlled function* without approval, the

more seriously the *FSA* is likely to view his behaviour, and therefore the more likely it is to take action against the *person*.

…

6.5B The five steps for penalties imposed on individuals in non-market abuse cases

…

Step 2 – the seriousness of the ~~*breach*~~ breach

…

6.5B.2 G …

(9) Factors relating to the nature of a *breach* by an individual include:

…

(n) whether the individual took any steps to comply with *FSA rules*, and the adequacy of those steps; ~~and~~

(o) in the context of contraventions of Part VI of the *Act*, the extent to which the *behaviour* which constitutes the contravention departs from current market practice;

(p) in relation to a contravention of section 63A of the *Act*, whether the individual's only misconduct was to perform a *controlled function* without approval;

(q) in relation to a contravention of section 63A of the *Act*, whether the individual performed *controlled functions* without approval and, while doing so, committed misconduct in respect of which, if the individual had been an *approved person*, the *FSA* would have been empowered to take action pursuant to section 66 of the *Act*; and

(r) in relation to a contravention of section 63A of the *Act*, the extent to which the individual could reasonably be expected to have known that he was performing a *controlled function* without approval. The circumstances in which the *FSA* would expect to be satisfied that a *person* could reasonably be expected to have known that he was performing a *controlled function* without approval include:

(i) the *person* had previously performed a similar role at the same or another *firm* for which he had been approved;

(ii) the *person's firm* or another *firm* had previously applied for approval for the *person* to perform the same or a similar *controlled function*;

(iii) the *person's* seniority or experience was such that he could reasonably be expected to have known that he was performing a *controlled function* without approval; and

(iv) the *person's firm* had clearly apportioned responsibilities so the *person's* role, and the responsibilities associated with it, were clear.

…

(13) Factors which are likely to be considered 'level 1 factors', 'level 2 factors' or 'level 3 factors' include:

…

(c) there was no, or limited, actual or potential effect on the orderliness of, or confidence in, markets as a result of the *breach*; ~~and~~

(d) the *breach* was committed negligently or inadvertently; and

(e) in relation to a contravention of section 63A of the *Act*, the individual's only misconduct was to perform a *controlled function* without approval.

Step 3 – mitigating and aggravating factors

6.5B.3 G …

(2) The following list of factors may have the effect of aggravating or mitigating the *breach*:

…

(l) whether the *FSA* publicly called for an improvement in standards in relation to the behaviour constituting the *breach* or similar behaviour before or during the occurrence of the *breach*; ~~and~~

(m) whether the individual agreed to undertake training subsequent to the *breach*; and

(n) in relation to a contravention of section 63A of the *Act*, whether the *person's firm* or another *firm* has previously withdrawn an application for the *person* to perform the same or a similar *controlled function* or has had such an application rejected by the *FSA*.

…

Insert the following new chapter after DEPP 6. The text is not underlined.

6A The power to impose a suspension or restriction

6A.1 Introduction

6A.1.1 G *DEPP* 6A sets out the *FSA's* statement of policy with respect to the imposition of suspensions or restrictions, and the period for which those suspensions or restrictions are to have effect, under the *Act*, as required by sections 69(1) and 210(1) of the *Act*.

6A1.2 G For the purposes of *DEPP* 6A, "suspension" refers both to the suspension of any *permission* which an *authorised person* has to carry on a *regulated activity* (under section 206A of the *Act*), and the suspension of any approval of the performance by an *approved person* of any function to which the approval relates (under section 66 of the *Act*); and "restriction" refers both to limitations or other restrictions in relation to the carrying on of a *regulated activity* by an *authorised person* (under section 206A of the *Act*), and to limitations or other restrictions in relation to the performance by an *approved person* of any function to which any approval relates (under section 66 of the *Act*).

6A.1.3 G The power to impose a suspension or a restriction is a disciplinary measure which the *FSA* may use in addition to, or instead of, imposing a financial penalty or issuing a *public censure.* The principal purpose of imposing a suspension or a restriction is to promote high standards of regulatory and/or market conduct by deterring *persons* who have committed *breaches* from committing further *breaches*, helping to deter other *persons* from committing similar *breaches*, and demonstrating generally the benefits of compliant behaviour. Suspensions and restrictions are therefore tools that the *FSA* may employ to help it to achieve its *regulatory objectives*. Examples of restrictions that we may impose include:

(1) we may limit an *authorised person's* carrying on of a *regulated activity* so that they can only sell certain products or provide certain services;

(2) we may restrict an *approved person's* performance of their *controlled functions* so that they can only give advice to *consumers* or deal in certain products if they are appropriately supervised.

6A.1.4 G As the power to impose a suspension or a restriction is a disciplinary measure, where the *FSA* considers it necessary to take action, for example, to protect *consumers* from an *authorised person*, the *FSA* will seek to cancel or vary the *authorised person's permissions*. If the *FSA* has concerns with a *person's* fitness to be approved, and considers it necessary to take action, the *FSA* will seek to prohibit the *approved person* or withdraw its approval.

6A.2 Deciding whether to take action

6A.2.1 G The *FSA* will consider the full circumstances of each case and determine whether it is appropriate to impose a suspension or restriction. The *FSA* will usually make this decision at the same time as it determines whether or not to impose a financial penalty or a *public censure*.

6A2.2 G The *FSA* will take into account relevant factors in deciding whether it is appropriate to impose a suspension or restriction. These may include factors listed in *DEPP* 6.2. There may also be other factors, not listed in *DEPP* 6.2, that are relevant.

6A.2.3 G The *FSA* will consider it appropriate to impose a suspension or restriction where it believes that such action will be a more effective and persuasive deterrent than the imposition of a financial penalty alone. This is likely to be the case where the *FSA* considers that direct and visible action in relation to a particular *breach* is necessary. Examples of circumstances where the *FSA* may consider it appropriate to impose a suspension or restriction include:

(1) where the *FSA* (or any *previous regulator*) has taken any previous disciplinary action resulting in adverse findings against the *person*;

(2) where the *FSA* has previously taken action in respect of similar *breaches* and has failed to improve industry standards;

(3) where the *person* has failed properly to carry out an agreed redress package or other agreed remedial measures;

(4) where the misconduct appears to be widespread across a number of individuals across a particular business area (suggesting a poor compliance culture);

(5) where the *person's* competitive position in the market has improved as a result of the *breach*;

(6) if, in accordance with *DEPP* 6.5D, the *FSA* considers that a proposed penalty would cause the subject of enforcement action serious financial hardship and that it is appropriate to reduce the proposed penalty.

6A.2.4 G The *FSA* expects usually to suspend or restrict a *person* from carrying out activities directly linked to the *breach*. However, in certain circumstances the *FSA* may also suspend or restrict a *person* from carrying out activities that are not directly linked to the *breach*, for example, where an *authorised person's* relevant business area no longer exists or has been restructured.

6A.3 Determining the appropriate length of the period of suspension or restriction

6A.3.1 G The *FSA* will consider all the relevant circumstances of a case when it determines the length of the period of suspension or restriction (if any) that is appropriate for the *breach* concerned, and is also a sufficient deterrent. Set out below is a list of factors that may be relevant for this purpose. The list is not exhaustive: not all of these factors may be applicable in a particular case, and there may be other factors, not listed, that are relevant.

6A.3.2 G The following factors may be relevant to determining the appropriate length of the period of suspension or restriction to be imposed on a *person* under the *Act*:

(1) Deterrence

When determining the appropriate length of the period of suspension or restriction, the *FSA* will have regard to the principal purpose for which it imposes sanctions, namely to promote high standards of regulatory and/or market conduct by deterring *persons* who have committed *breaches* from committing further *breaches* and helping to deter other *persons* from committing similar *breaches*, as well as demonstrating generally the benefits of compliant business.

(2) The seriousness of the breach

The *FSA* will have regard to the seriousness of the breach. In assessing this, it will consider the impact and nature of the *breach*, and whether it was committed deliberately or recklessly. Where the *breach* was committed by an *authorised person*, relevant factors may include those listed in *DEPP* 6.5A.2G(6) to (9). Where the *breach* was committed by an *approved person*, relevant factors may include those listed in *DEPP* 6.5B.2G(8) to (11). There may also be other factors, not listed in these sections, that are relevant.

(3) Aggravating and mitigating factors

The *FSA* will have regard to factors that may aggravate or mitigate a *breach*. Where the *breach* was committed by an *authorised person*, relevant factors may include those listed in *DEPP* 6.5A.3G(2). Where the *breach* was committed by an *approved person*, relevant factors may include those listed in *DEPP* 6.5B.3G(2). There may also be other factors, not listed in these sections, that are relevant.

(4) The impact of suspension or restriction on the person in breach

The following considerations may be relevant to the assessment of the impact of suspension or restriction on an *authorised person*:

(a) the *authorised person's* expected lost revenue and profits from not being able to carry out the suspended or restricted activity;

(b) the cost of any measures the *authorised person* must

undertake to comply with the suspension or restriction;

(c) potential economic costs, for example, the payment of salaries to employees who will not work during the period of suspension or restriction or the payment of compensation to *consumers* who will suffer loss as a result of the suspension or restriction;

(d) the effect on other areas of the *authorised person's* business; and

(e) whether the suspension or restriction would cause the *authorised person* serious financial hardship.

The following considerations may be relevant to the assessment of the impact of suspension or restriction on an *approved person*:

(f) the *approved person's* expected lost earnings from not being able to carry out the suspended or restricted activity; and

(g) whether the suspension or restriction would cause the *approved person* serious financial hardship.

(5) The impact of suspension or restriction on persons other than the person in breach

The following considerations may be relevant to the assessment of the impact of suspension or restriction on *persons* other than the *person* in *breach*:

(a) the extent to which *consumers* may suffer loss or inconvenience as a result of the suspension or restriction. For example, if it is difficult for *consumers* to switch to a competitor, a longer period of suspension or restriction is likely to have more impact; and

(b) the impact of the suspension or restriction on markets.

6A.3.3 G The *FSA* may delay the commencement of the period of suspension or restriction. In deciding whether this is appropriate, the *FSA* will take into account all the circumstances of a case. Considerations that may be relevant in respect of an *authorised person* include:

(1) the impact of the suspension or restriction on consumers;

(2) any practical measures the *authorised person* needs to take before the period of suspension or restriction begins, for example, changes to its systems and controls to enable it to stop or limit the activity in question;

(3) the impact of the suspension or restriction on other costs incurred by the *authorised person*, for example, cancelling suppliers or

suspending employees.

6A.4 The interaction between the power to impose suspensions or restrictions and the power to impose penalties or public censures

6A.4.1 G The deterrent effect and impact on a *person* of a suspension or restriction, by itself or in combination with a financial penalty, may be greater than where only a financial penalty is imposed. The *FSA* will consider the overall impact and deterrent effect of the sanctions it imposes when determining the level of penalty and the length of suspension or restriction.

6A.4.2 G The *FSA* expects usually to take the following approach in respect of the interaction between a suspension or restriction and a financial penalty or *public censure*:

(1) The *FSA* will determine which sanction, or combination of sanctions, is appropriate for the *breach*.

(2) If the *FSA*, following the approach set out in *DEPP* 6.2, considers it appropriate to impose a financial penalty, it will calculate the appropriate level of the financial penalty, following the approach set out in *DEPP* 6.5 to *DEPP* 6.5D.

(3) If the *FSA*, following the approach set out in *DEPP* 6A.2, considers it appropriate to impose a suspension or restriction, it will calculate the appropriate length of the period of suspension or restriction, following the approach set out in *DEPP* 6A.3.

(4) Where the *FSA* considers it appropriate to impose both a financial penalty and a suspension or restriction, it will decide whether the combined impact on the *person* is likely to be disproportionate in respect to the *breach* and the deterrent effect of the sanctions.

(5) If the *FSA* considers the combined impact on the *person* is likely to be disproportionate, it will decide whether to reduce the period of suspension or restriction, the amount of the financial penalty or both, so that the combined impact of the sanctions is proportionate in relation to the *breach* and the deterrent effect of the sanctions. The *FSA* will decide which sanction to reduce after considering all the circumstances of the case.

(6) In deciding the final level of the financial penalty and the length of the period of suspension or restriction, the *FSA* will also take into account any representations by the *person* that the combined impact will cause them serious financial hardship. The *FSA* will take the approach set out in *DEPP* 6.5D in assessing this.

6A.4.3 G The *FSA* may depart from the approach set out in *DEPP* 6A.4.2G. For example, the *FSA* may at the outset consider that a financial penalty is the

only appropriate sanction for a *breach* but, having determined the appropriate level of financial penalty, may consider it appropriate to reduce the amount of the financial penalty for serious financial hardship reasons. In such a situation, the *FSA* may consider it appropriate to impose a suspension or restriction even if the *FSA* at the outset did not consider such a sanction to be appropriate. The *FSA* will take into account whether the *person* would suffer serious financial hardship in deciding the length of the period of suspension or restriction, and may decide not to impose a suspension or restriction if it considers such action would result in serious financial hardship.

…

Schedule 4 Powers Exercised

Sch 4.1	G	The following powers and related provisions in or under the *Act* have been exercised by the *FSA* to make the statements of policy in *DEPP*:
		Section 63C (Statement of policy)
		…
		Section 131J (Statement of policy)
		…

Annex C

Amendments to the Enforcement Guide (EG)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.2 In the areas set out below, the *Act* expressly requires the FSA to prepare and publish statements of policy or procedure on the exercise of its enforcement and investigation powers and in relation to the giving of *statutory notices*~~.~~:

(1) section 63C requires the FSA to publish a statement of its policy on the imposition, and amount, of financial penalties on *persons* that perform a *controlled function* without approval;

~~(1)~~ (1A) sections 69 and 210 require the FSA to publish statements of policy on the imposition~~, and amount,~~ of financial penalties, suspensions or restrictions on *firms* and *approved persons*, the amount of financial penalties imposed, and the period for which suspensions or restrictions are to have effect;

…

(3) section 124 requires the FSA to publish a statement of its policy on the imposition, and amount, of financial penalties for *market abuse*;

(3A) section 131J requires the FSA to publish a statement of its policy on the imposition, and amount, of financial penalties imposed under section 131G;

...

…

7.2 The FSA has the following powers to impose a financial penalty and to publish a *public censure*.

(1) It may publish a statement:

…

(e) where there has been *market abuse*, against a *person* under section 123 of the *Act*; ~~and~~

(ea) if a *person* has contravened any provision of *short selling rules*, or any requirement imposed on the *person* under section 131E or 131F, under section 131G of the *Act*; and

…

(2) It may impose a financial penalty:

(a) on a *person* that performs a *controlled function* without approval,

under section 63A of the Act;

~~(a)~~ on an *approved person*, under section 66 of the Act;

(aa)

…

(c) where there has been *market abuse*, on any *person*, under section 123 of the *Act*; ~~and~~

(ca) on a *person* who has contravened any provision of *short selling rules*, or any requirement imposed on the *person* under section 131E or 131F, or any *person* who was knowingly concerned in the contravention, under section 131G of the *Act*; and

…

Appendix 2

Financial Stability and Market Confidence sourcebook Instrument 2010

FINANCIAL STABILITY AND MARKET CONFIDENCE SOURCEBOOK INSTRUMENT 2010

Powers exercised

A. The Financial Services Authority makes this instrument in the exercise of:

(1) the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(a) section 119 (The code);
(b) section 121 (Codes: procedure);
(c) section 131B (Short selling rules);
(d) section 149 (Evidential provisions);
(e) section 156 (General supplementary powers);
(f) section 157(1) (Guidance); and
(g) section 165B(6) (Safeguards etc in relation to exercise of power under section 165A).

(2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.

B. The rule-making powers referred to above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on 6 August 2010.

Making the Financial Stability and Market Confidence sourcebook (FINMAR)

D. The Financial Services Authority makes the rules and gives the guidance in Annex A to this instrument.

Amendments to the Handbook

E. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Glossary of definitions	Annex B
Threshold Conditions (COND)	Annex C
Market Conduct sourcebook (MAR)	Annex D

Notes

F. In Annex A to this instrument, the "notes" (indicated by "**Note:**") are included for the convenience of the reader but do not form part of the legislative text.

Citation

G. This instrument may be cited as the Financial Stability and Market Confidence Sourcebook Instrument 2010.

H. The sourcebook in Annex A to this instrument (including its schedules) may be cited as the Financial Stability and Market Confidence sourcebook (or FINMAR).

By order of the Board
22 July 2010

Annex A

Financial Stability and Market Confidence sourcebook (FINMAR)

Insert the following new sourcebook after The Fit and Proper test for Approved Persons (FIT) in the block of the Handbook titled "High Level Standards". The text is all new and is not underlined, except where otherwise stated.

1 Gathering financial stability information

1.1 Application, purpose and scope

Application

1.1.1 G *FINMAR* 1 is relevant to *authorised persons* and *unauthorised persons*, in particular *persons* whose activities are or may be relevant to the stability of one or more aspects of a *relevant financial system*.

Purpose

1.1.2 G (1) Section 165B(6) (Statement of policy) of the *Act* requires the *FSA* to prepare and publish a statement of policy on the *financial stability information power*. The purpose of *FINMAR* 1 is to set out the *FSA's* statement of policy on the exercise of the *financial stability information power* and the *overseas financial stability information power* contained in sections 165A and 169A of the *Act*.

(2) The Treasury has approved this statement of policy in accordance with section 165B(7) of the *Act*.

1.1.3 G Determining whether to impose a *financial stability information requirement* involves different considerations from the exercise of other *FSA* powers. The *guidance* in this chapter relates only to the imposition of *financial stability information requirements*.

Scope of the powers

1.1.4 G The *financial stability information power* and the *overseas financial stability information power* are exercisable in relation to the categories of *person* set out in section 165A(2) of the *Act* (interpreted in accordance with the rest of that section).

1.1.5 Table: section 165A(2) of the Act

Section 165A of the *Act* applies to:	
(a)	a person who has a legal or beneficial interest in any of the assets of a relevant investment fund;

(b)	a person who is responsible for the management of a relevant investment fund;
(c)	a person (a "service provider") who provides any service to an authorised person;
(d)	a person prescribed by an order made by the Treasury or any person of a description prescribed by such an order (and see also section 165C);
(e)	a person who is connected with a person to whom this section applies as a result of any of the above paragraphs.

1.1.6 G The *FSA* may impose a *financial stability information requirement* on a *person* within the categories set out in *FINMAR* 1.1.5UK only to the extent that it considers that the information or document is or might be relevant to the stability of one or more aspects of the *UK financial system*. The *persons* within these categories may include:

(1) a vehicle for collective investment, whether or not it is regulated, (including vehicles often referred to as "hedge funds" and "structured investment vehicles" or off-balance sheet vehicles used for investment) and its managers;

(2) a provider of a service to an *authorised person*, such as a software supplier or the provider of a liquidity facility, where the risk to the stability of one or more aspects of the *UK financial system* relates to the provision of the service;

(3) a large scale proprietary trader or investor who trades large volumes of *financial instruments* that are traded on *UK regulated markets* or *UK MTFs*, for example *overseas* corporate entities; and

(4) a *person* who manages investments for a single family (whether or not the investments are held within a trust), for example a family office.

1.2 Financial stability information powers

Introduction

1.2.1 G The *FSA* has a *regulatory objective* of contributing to the protection and enhancement of *UK* financial stability. Section 250 of the Banking Act 2009 imposes a duty on the *FSA* to collect information that it thinks is, or may be, relevant to the stability of individual financial institutions or to one or more aspects of the *UK financial system*.

1.2.2 G Some information relevant to *UK* financial stability will be accessible to the *FSA*:

(1) through *authorised persons'* regular reports to the *FSA*; or

(2) from other *UK* or international authorities;

(3) through information gathered by the *FSA* under other information gathering powers, such as section 165 of the *Act* or section 250(2) of the Banking Act 2009.

1.2.3 G The *FSA* may use the *financial stability information power* to gather additional information relevant to *UK* financial stability. The information may relate to the exercise of the *FSA's* functions, or the *FSA* may collect the information in order to disclose it to another *person* or authority, for example the Bank of England or the Treasury. Information relevant to financial stability may be held by an *authorised person* or by an *unauthorised person*.

1.2.4 G When the *FSA* seeks additional information from an *authorised person* or an *unauthorised person* it may not in all cases be necessary to exercise statutory information-gathering powers. However, the *FSA* will use its statutory powers if it believes it is appropriate to do so and, in urgent cases, it may be appropriate for the *FSA* to exercise these powers without delay.

Financial stability information power

1.2.5 G The *FSA* may use the *financial stability information power* to require a *person* to provide:

(1) specified information or documents; or

(2) information or documents of a specified description;

that the *FSA* considers are or may be relevant to the stability of the *UK financial system*.

[**Note:** Section 165A of the *Act*]

Overseas financial stability information power

1.2.6 G The *FSA* may exercise the *overseas financial stability information power* at the request of an *overseas regulator* to require a *person* to provide:

(1) specified information or documents; or

(2) information or documents of a specified description;

that the *FSA* considers are or may be relevant to the stability of a *relevant financial system* operating in the country or territory of the *overseas regulator*.

[**Note:** Section 169A of the *Act*]

1.2.7 G If the *overseas regulator* is a *competent authority* and the request relates to an obligation of the *FSA* under *EU* law, the *FSA* will take into account whether it is necessary to exercise the *overseas financial stability information power* to comply with that obligation.

1.2.8 G In deciding whether to exercise the *overseas financial stability information power*, the *FSA* may take into account in particular:

(1) whether corresponding assistance would be given to a *UK* regulatory authority in the country or territory of the *overseas regulator*; and

(2) whether it is otherwise appropriate in the public interest to give the assistance sought.

1.2.9 G The *FSA* may decide not to exercise the *overseas financial stability information power* unless the *overseas regulator* undertakes to make such contribution towards the cost to the *FSA* of its exercise as the *FSA* considers appropriate.

1.2.10 G *FINMAR* 1.2.8G and *FINMAR* 1.2.9G do not apply if the *FSA* considers that it must use the *overseas financial stability information power* to comply with an obligation upon the *FSA* under *EU* law.

1.3 Providing notice before imposing a financial stability information requirement

Giving notice

1.3.1 G The *FSA* will give a *person* a notice in writing if it proposes to impose a *financial stability information requirement* unless the *FSA* is satisfied that information or documents are required without delay. The notice will include:

(1) the reasons why the *FSA* proposes to impose the *financial stability information requirement*; and

(2) the time period in which the *person* may make representations to the *FSA* in respect of the proposal.

Right to make representations

1.3.2 G The notice referred to in *FINMAR* 1.3.1G will specify a reasonable period in which to make representations. In determining the period for representations the *FSA* will take into account:

(1) the nature, type and number of documents likely to be required;

(2) the reasons for imposing the requirement;

(3) whether the *person* is likely to wish to seek legal advice;

(4) whether the *person* is an *authorised person*;

(5) any cost implications for the *person*.

1.3.3 G The *FSA* will generally invite the recipient of a notice to make representations in writing to the address provided in the notice. The *FSA* will consider a request by a *person* to make oral representations and will take into account:

(1) whether oral representations would be likely to:

(a) improve the *FSA's* understanding of the representations;

(b) be more convenient or less costly than written representations; and

(c) assist the *FSA* in making a decision more quickly; and

(2) as in other cases, and in accordance with the Disability Discrimination Act 1995, any reason relating to the disability of the person which would mean that they could not otherwise have a fair hearing.

1.3.4 G Once the period for making representations has expired the *FSA* will determine within a reasonable period whether to impose the *financial stability information requirement*.

1.3.5 G If the *FSA* does not receive any representations during the period specified in the notice it will determine whether to impose the *financial stability information requirement* based on the information available to it.

1.4 Imposing a financial stability information requirement without prior notice

1.4.1 G If the *FSA* proposes to impose a *financial stability information requirement* and is satisfied that it is necessary for the information or documents covered by a *financial stability information requirement* to be provided or produced without delay, the *FSA* may impose the *financial stability information requirement* on a *person* without taking the steps described in *FINMAR* 1.3 (see section 165B (4) of the *Act*).

1.4.2 G The *FSA* will determine whether to impose a *financial stability information requirement* without prior notice based on the facts of each case and after taking into account the information before it concerning:

(1) the nature of the risk to financial stability and whether the risk appears to be increasing rapidly;

(2) the extent of the risk to financial stability;

(3) whether it is fair to impose the requirement without notice; and

(4) whether the information sought may lead to prompt action by the *FSA*.

1.4.3 G A *person* who receives a *financial stability information requirement* without prior notice should consider whether to contact the *FSA* concerning the requirement. The *person* should raise any proposal to make representations with the *FSA* at the earliest opportunity.

1.5 Imposing a requirement

Deciding to impose a requirement

1.5.1 G In deciding whether to impose a *financial stability information requirement* the *FSA* will:

(1) review the material before it;

(2) consider any representations received from the proposed recipient of the requirement; and

(3) take into account:

(a) the nature and extent of the risks to financial stability;

(b) whether the information is more readily available from another source, taking into account the likely time and cost implications of seeking information from that source;

(c) whether the information may assist the *FSA* in fulfilling its functions, for example if the information relates to the exercise of the *FSA's* statutory powers.

1.5.2 G A decision to impose the *financial stability information requirement* will be taken by a member of *FSA* staff at the appropriate level of seniority.

Scope of the requirement

1.5.3 G The information and documents specified will be appropriate for each case. They may be defined broadly, for example information relating to a trading strategy and its execution, or in a more limited way, for example a contract documenting a particular trade.

Notice of a financial stability information requirement

1.5.4 G The *FSA* will give a *person* notice in writing if it decides to impose a *financial stability information requirement*. The notice will describe the

information and documents to which the requirement relates and include the *FSA's* reasons for imposing the requirement.

Requiring documents to be verified or authenticated

1.5.5 G The *FSA* may, where it is reasonable to do so, require a *person* subject to a *financial stability information requirement* to provide:

(1) verification of any information; or

(2) authentication of any document;

that the *person* provides to the *FSA* in accordance with that requirement.

1.5.6 G When deciding whether to require verification or authentication the *FSA* will take into account the circumstances of each case, including:

(1) the type of information or documents required and whether there is a particular need for the information to be exactly accurate;

(2) the likely additional cost to the *person* providing the information or documents;

(3) the extent to which verification or authentication may improve the quality or reliability of the information or documents; and

(4) the nature of any previous communications between the *person* and the *FSA*.

1.5.7 G The *FSA* may, where it is reasonable to do so, require the information or documents to be verified or authenticated in any manner. Examples of verification or authentification include:

(1) a signed declaration by an officer or employee of a *body corporate*;

(2) a declaration by a commissioner for oaths that a copy of a document is a true copy of the original; and

(3) a declaration by the *person's* accountant or auditor that the information provided appears to be accurate.

2 Short selling

2.1 Application and purpose

Application

2.1.1 R This chapter applies to all *persons* who:

(1) engage, or are intending to engage, in short selling in relation to

relevant financial instruments; or

(2) have engaged in short selling in relation to *relevant financial instruments* where the resulting short position is still open.

Purpose

2.1.2 G The purpose of this chapter is to set out *rules* and provide *guidance* in relation to short selling in order to promote the *FSA's* statutory objectives of:

(1) maintaining confidence in the *UK financial system*; and

(2) contributing to the protection and enhancement of the stability of the *UK financial system*.

2.2 Disclosure of disclosable short positions

Disclosure during a rights issue period

2.2.1 R A *person* who has a *disclosable short position* must provide *disclosure* of his position where:

(1) the position relates, directly or indirectly, to *securities* which are:

(a) the subject of a *rights issue*;

(b) admitted to trading on a *prescribed market* in the *United Kingdom*; and

(c) issued by:

(i) a *UK company*; or

(ii) a non-*UK company* for whom the *UK prescribed market* is the sole or main venue for trading the *securities*; and

(2) the *disclosable short position*:

(a) is reached or exceeded, or the position falls below a *disclosable short position*, during a *rights issue period*; or

(b) has been reached or exceeded immediately before the beginning of the *rights issue period* and has not fallen below a *disclosable short position* at the time the *rights issue period* commences.

2.2.2 G For the purposes of *FINMAR* 2.2.1R(1)(c)(ii), a *UK prescribed market* is the main venue for trading *securities* of a *company* where the volume of the *securities* traded on that market in the 12-month period immediately

preceding the beginning of the *company's rights issue period* is greater than the volume of the *securities* traded on any other market, whether in the *United Kingdom* or elsewhere.

Disclosure of a short position in a UK financial sector company

2.2.3 R A *person* who has a *disclosable short position* in a *UK financial sector company* must provide *ongoing disclosure* of his position.

2.2.4 G Where a *UK financial sector company* is in a *rights issue period*, a disclosure under *FINMAR* 2.2.3R is sufficient to satisfy the disclosure requirement in *FINMAR* 2.1.1R.

2.3 Calculation of net short position

Preliminary

2.3.1 G This section contains provisions relating to the calculation of a *net short position* for the purposes of determining whether a *person* has a *disclosable short position*.

2.3.2 R A *net short position* is the position remaining after deducting a long position (if any) that a *person* holds in relation to the issued capital of a *company* from a short position in relation to the issued capital of that *company*, where the value of the long and short positions is calculated in accordance with the provisions below.

2.3.3 R The calculation of a *net short position* must take account of any form of economic interest, whether by virtue of a long or short position, in the issued capital of the *company*.

2.3.4 R A *net short position* must be calculated on the basis of the position held at midnight at the end of each day that a person has the *net short position*.

Long and short positions

2.3.5 R A 'long position' is the total of:

(1) the number of *shares* a *person* holds in a *company*; and

(2) any exposure, calculated on a delta-adjusted basis, to the issued capital of the *company* the *person* has through his holding of *financial instruments* which will result in the *person* making a profit, whether directly or indirectly, if there is an increase in the price or value of the *shares* of the *company*.

2.3.6 R A 'short position' is the total of:

(1) the number of *shares* in a *company* that a *person* has sold where the *person* has borrowed or needs to borrow or purchase *shares* to settle

the transaction and the *shares* have not yet been returned to the lender, or borrowed and returned to the lender, or purchased, as the case may be; and

(2) any exposure, calculated on a delta-adjusted basis, to the issued capital of the *company* the *person* has through his holding of *financial instruments* which will result in the *person* making a profit, whether directly or indirectly, if there is a decrease in the price or value of the *shares*.

Calculating short positions: particular cases

2.3.7 R For the purposes of calculating a *net short position* when a *company* is in a *rights issue period*:

(1) a long position in the nil paid rights cannot be deducted from a short position in relation to the *company*; and

(2) any short position in the nil paid rights must be taken into account.

2.3.8 G Where a *person* has an economic exposure to the issued capital of a *company* by virtue of his interest in a basket, index or exchange traded fund, the value of the exposure to the *company* should be included in the calculation of his *net short position*.

2.4 Responsibility for disclosure

Discretionary and non-discretionary managers

2.4.1 R Where a *person* has appointed one or more *discretionary investment managers* to manage some or all of his investments, the *person* must make any disclosures required under *FINMAR* 2.2.1R or *FINMAR* 2.2.3R in respect of any *disclosable short position*, unless *FINMAR* 2.4.2G applies.

2.4.2 G Where a *person* ("P") has appointed:

(1) a *discretionary investment manager* to manage some or all of his investments, P may authorise that *discretionary investment manager* to make any disclosures required by *FINMAR* 2.2.1R or *FINMAR* 2.2.3R on P's behalf in relation to the investments managed by that *discretionary investment manager*;

(2) more than one *discretionary investment manager* to manage some or all of his investments, P may authorise another *person* (such as the *operator* of an *AUT, ICVC* or any other fund) to make any disclosures required by *FINMAR* 2.2.1R or *FINMAR* 2.2.3R on P's behalf.

2.4.3 R Where a *discretionary investment manager* or another *person* has been authorised by a *person* ("P") to make any disclosures required by *FINMAR*

2.2.1R or *FINMAR* 2.2.3R on P's behalf, he must:

(1) provide *disclosure* or *ongoing disclosure* as required under *FINMAR* 2.2.1R or *FINMAR* 2.2.3R of P's position; and

(2) clearly identify the *person* on whose behalf he is making the disclosure.

2.4.4 R Where a *discretionary investment manager* manages investments for more than one *person*, he must provide *disclosure* or *ongoing disclosure* under *FINMAR* 2.2.1R or *FINMAR* 2.2.3R in respect of the aggregate *net short position* of all the portfolios managed by him.

2.4.5 R Where a *person* whose investments are managed by a *non-discretionary investment manager* has a *disclosable short position*, the *person* must make any disclosures required under *FINMAR* 2.2.1R or *FINMAR* 2.2.3R in respect of his position.

2.4.6 G A *person* whose investments are managed by a *non-discretionary investment manager* and who has a *disclosable short position* may authorise his *non-discretionary investment manager* to make any disclosures required by *FINMAR* 2.2.1R or *FINMAR* 2.2.3R on his behalf in respect of his position.

2.4.7 R Where a *non-discretionary investment manager* has been authorised by a *person* to make any disclosures required by *FINMAR* 2.2.1R or *FINMAR* 2.2.3R on that *person's* behalf, he must:

(1) provide *disclosure* or *ongoing disclosure* as required under *FINMAR* 2.2.1R or *FINMAR* 2.2.3R of the *person's* position; and

(2) clearly identify the *person* on whose behalf he is making the disclosure.

Groups

2.4.8 R Where one or more *companies* in a group is required to disclose a *disclosable short position*, each *company* must make a separate disclosure of its own position unless *FINMAR* 2.4.9G applies.

2.4.9 G One *company* in a group may make a disclosure of a *disclosable short position* held by one or more *companies* in the group, provided that the disclosure clearly states the name of the *company* or of each of the *companies*, as the case may be, which holds a *disclosable short position*.

Editor's Note: The following chapter (FINMAR 3) replaces COND 3, which is deleted. Changes from the text of COND 3 are indicated by underlining (new text) and striking through (deleted text).

3 Banking Act 2009

3.1 Application and purpose

Application

3.1.1 G *FINMAR* 3 is relevant to *firms* subject to the powers in Parts 1 to 3 of the Banking Act 2009 (the Banking Act), that is, *UK* incorporated *firms* with a *Part IV permission* to carry on the *regulated activity* of *accepting deposits*, other than *credit unions*, *firms* with a *Part IV permission* to *effect* or *carry out contracts of insurance* and any other class of institution specified in secondary legislation.

Purpose

3.1.2 G The purpose of *FINMAR* 3 is to provide *guidance* on assessing Condition 2 under section 7(3) of the Banking Act.

~~3.1~~ 3.2 Assessing Condition 2 under section 7(3) of the Banking Act 2009

Introduction

~~3.1.1~~ 3.2.1 G The Banking Act ~~2009 (the Banking Act)~~ introduces new powers for HM Treasury, the Bank of England and the *FSA* to deal with failing banks. The powers, which are set out in Parts 1 to 3 of that Act, can be used to deal with *UK* incorporated *firms* with a *Part IV permission* to carry on the *regulated activity* of *accepting deposits*, other than *credit unions*, *firms* with a *Part IV permission* to *effect* or *carry out contracts of insurance* and any other class of institution specified in secondary legislation. In relation to *building societies*, the main tools in the Act are applied with modifications. In this section the term "bank" is used to refer to those *firms* that are potentially subject to the powers in Parts 1 to 3 of the Banking Act. The powers are defined in the Banking Act, and referred to in this section as the "stabilisation powers". The Banking Act contains powers to enable HM Treasury to extend the application of the stabilisation powers to *credit unions* by secondary legislation.

~~3.1.2~~ 3.2.2 G Section 7 of the Banking Act sets out the two conditions that must be met before a stabilisation power can be exercised in respect of a bank:

(1) Condition 1 is that the bank is failing, or is likely to fail, to satisfy the *threshold conditions*.

(2) Condition 2 is that, having regard to timing and other relevant circumstances, it is not reasonably likely that (ignoring the stabilisation powers) action will be taken by or in respect of the bank that will enable it to satisfy the *threshold conditions*.

~~3.1.3~~ 3.2.3 G The Banking Act provides that the *FSA* is to treat Conditions 1 and 2 as met if satisfied that they would be met but for financial assistance provided by either HM Treasury or the Bank of England (disregarding ordinary market assistance offered by the Bank on its usual terms).

Assessing Condition 1

~~3.1.4~~ 3.2.4 G The matters the *FSA* will take into account in assessing whether a bank is failing or is likely to fail to satisfy the *threshold conditions* are described in *COND* 2.1 to *COND* 2.5. The options available to the *FSA* in the case of a breach of the *threshold conditions* are outlined in Chapter 8 of the *Enforcement Guide* and *SUP* 7.2. These tools are available to the *FSA* at any time, and so may be used before or in conjunction with the stabilisation tools provided by the Banking Act.

Assessing Condition 2

~~3.1.5~~ 3.2.5 G The Banking Act provides that in considering the test in Condition 2, the *FSA* should ignore the stabilisation powers. The purpose of this limitation is to make clear that in making its assessment, the *FSA* is not considering whether the stabilisation powers could successfully resolve the situation, but is considering whether alternative measures might provide for this instead.

Timing

~~3.1.6~~ 3.2.6 G In assessing Condition 2, the *FSA* will consider the timeframe during which any actions taken by or in relation to the bank are likely to be available and to have effect. In the view of the *FSA*, the purpose of the reference to timing in Condition 2 is to require the *FSA* to consider whether a return to full compliance is likely to occur within a reasonable period of time. The following is a non-exhaustive list of factors the *FSA* may consider:

(1) the extent of any loss, or risk of loss, or other adverse effect on *consumers*. The more serious the loss or potential loss or other adverse effect, the more likely it is that the *FSA* will consider that remedial action will be needed urgently;

(2) the seriousness of any suspected breach of the requirements of the *Act* or the *rules* and the steps that need to be taken to correct that breach;

(3) the risk that the bank's conduct or business presents to the stability of the *UK financial system* and to confidence in that system;

(4) the likelihood that remedial action that could be taken by or in relation to the bank will take effect before *consumers*, ~~or~~ market

confidence or financial stability suffers significant detriment.

~~3.1.7~~ 3.2.7 G If the *FSA* is satisfied that the breach of *threshold conditions* is likely to be temporary and to be rectified within a reasonable time, the *FSA* is unlikely to conclude that Condition 2 has been met.

Other relevant circumstances

~~3.1.8~~ 3.2.8 G In general the *FSA* will be concerned to determine whether any remedial action that could be taken by or in relation to the bank will be effective. This will include an assessment of both how likely it is that the action will be taken, and if it is, the impact it will have on the bank's compliance with the *threshold conditions*. Circumstances that the *FSA* may take into account include but are not limited to:

(1) where the *FSA's* concerns relate to adequacy of liquidity:

(a) the availability of market funding to banks generally and any specific circumstances of the bank that may impact on its ability to access the market on terms which are generally available;

(b) whether the bank's current funding structure is adequate and viable; whether the primary sources of funding continue to be available, given current market sentiment, and whether they would still be viable if market sentiment was to change;

(c) the maturity profile of the bank's existing funding and the availability of funding from the market to replace maturing funding as the need arises;

(d) whether liquidity problems call into question adequacy of capital;

(e) the bank's credit rating and the likelihood and impact of any potential downgrade;

(f) the availability and terms of liquidity support from group *companies*, existing funders and central banks;

(2) where the *FSA's* concerns relate to capital:

(a) the availability of capital from the market for banks in general and any specific circumstances of the bank that may impact on its ability to access the market on terms which are generally available;

(b) potential sources of capital and the nature of and terms on which capital may be obtained;

(c) the success of any recent attempts by the bank to raise capital

on the open market;

(d) the willingness of existing significant institutional investors to provide or assist in a strategic solution to the bank;

(3) where the *FSA's* concerns relate to the adequacy of non-financial resources or suitability, the *FSA* will take into account the factors identified in *COND* 2.4 and 2.5, and other *Handbook* provisions referred to in those chapters. In assessing Condition 2, the circumstances of each case are likely to be different, but the *FSA* will be concerned to establish the likelihood of achieving a return to full compliance with the *threshold conditions*, and the timescale in which a return to compliance will be effected;

(4) the prospects of the bank securing a material and relevant transaction with a third party, for example a sale of the bank itself or of all or part of its business. In relation to any transaction, the *FSA* will have regard to factors including but not limited to:

(a) the status of any ongoing negotiations;

(b) the level of interest expressed and the credibility of potential counterparties;

(c) practical constraints related to the bank itself, for example, management engagement, availability of relevant information and severability of infrastructure;

(d) the sources, availability and firmness of financing for any transaction;

(e) the need for shareholder approval, merger clearances or other consents;

(f) the suitability of the counterparty and the stability of the relevant parties following completion of any transaction.

~~3.1.9~~ 3.2.9 G When assessing whether the bank will return to compliance with *threshold condition* 4 (adequate resources) the *FSA* will also assess the reasons behind the likely or actual failure of compliance. Serious failures of management, systems or internal controls may in themselves call into question the adequacy of the bank's non-financial resources (*threshold condition* 4) or suitability (*threshold condition* 5). Therefore, in assessing whether a bank is reasonably likely to satisfy the *threshold conditions* in the future, the *FSA* will be concerned to ensure that any such failures have been adequately addressed.

Schedule 1 Record keeping requirements

Sch 1.1 G There are no record-keeping requirements in *FINMAR*.

Schedule 2 Notification requirements

Sch 2.1 G There are no notification requirements in *FINMAR*.

Schedule 3 Fees and other required payments

Sch 3.1 G There are no requirements for fees in *FINMAR*.

Schedule 4 Powers Exercised

Sch 4.1 G

The following powers and related provisions in or under the *Act* have been exercised by the *FSA* to make the *rules*, statements of policy and guidance in *FINMAR*:	
	Section 131B (Short selling rules)
	Section 157(1) (Guidance)
	Section 165B(6) (Safeguards etc in relation to exercise of power under section 165A)

Schedule 5 Rights of action for damages

Sch 5.1 G There are no rules in *FINMAR*.

Schedule 6 Rules that can be waived

Sch 6.1 G There are no rules in *FINMAR*.

Annex B

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Insert the following new definitions in the appropriate alphabetical position. The text is not underlined.

disclosure	disclosure of a *disclosable short position* which: (a) is made on a *RIS* by no later than 3.30pm on the *business day* following the day on which the position reaches, exceeds or falls below a *disclosable short position* of 0.25% of the issued capital of a *company*; and (b) includes the name of the *person* who has the *disclosable short position*, the amount of the *disclosable short position* and the name of the *company* in relation to which the *person* has that position.
FINMAR	the Financial Stability and Market Confidence sourcebook.
financial stability information power	the *FSA's* power under section 165A of the *Act* (Authority's power to require information: financial stability) which, in summary, is a power to require a *person* to provide information or documents relevant to the stability of one or more aspects of the *UK financial system*.
financial stability information requirement	a requirement imposed on a *person* by the *FSA* using the *financial stability information power* or the *overseas financial stability information power*.
ongoing disclosure	disclosure of a *disclosable short position* which: (a) is made on a *RIS* by no later than 3.30pm on the *business day* following the day on which the position reaches, exceeds or falls below a *net short position* of 0.25%, 0.35%, 0.45% and 0.55% of the issued capital of a *company* and each 0.1% threshold thereafter; and (b) includes the name of the *person* who has the *disclosable short position*, the amount of the *disclosable short position* and the name of the *company* in relation to which the *person* has that position.
overseas financial stability information power	the *FSA's* power under section 169A of the *Act* (Support of overseas regulator with respect to financial stability) which, in summary, is a power exercisable at the request of an *overseas regulator* to require a *person* to provide information or documents relevant to the stability

	of one or more aspects of the *relevant financial system* operating in the country or territory of that regulator.
relevant financial instrument	(in accordance with sections 131C(4) and 131C(5) of the *Act*) a *financial instrument* that: (a) is admitted to trading on a *regulated market* or any other *prescribed market* in an *EEA State*; or (b) has such other connection with a market in an *EEA State* as may be specified by the *short selling rules*.
relevant financial system	(in accordance with section 169A(5) of the *Act* (Support of overseas regulator with respect to financial stability)) a financial system including: (a) financial markets and exchanges; (b) activities that would be *regulated activities* if carried on in the *United Kingdom*; and (c) other activities connected with financial markets and exchanges.
short selling rules	(in accordance with section 131B(8) of the *Act*) rules concerning the prohibition or disclosure of short selling in relation to *relevant financial instruments*.
UK financial system	(as defined in section 3 of the *Act* (Market confidence)) the financial system operating in the *United Kingdom* including: (a) financial markets and exchanges; (b) *regulated activities*; and (c) other activities connected with financial markets and exchanges.

Amend the following definitions as shown.

competent authority	(1) … (2) (in relation to the exercise of an *EEA right* and the exercise of the *overseas financial stability information power*) a competent authority for the purposes of the relevant *Single Market Directive*. …
disclosable short	a ~~net short position~~ *net short position* which represents an economic

position interest of one quarter of ~~one per cent~~ 1% or more of the issued capital of a ~~company~~ *company*, excluding any interest held in the capacity of a *market maker*.

~~In calculating whether a holder has a *disclosable short position*, the holder should take into account any form of economic interest it has in the shares of the *issuer*, excluding any interest which he holds as a market maker in that capacity~~.

discretionary investment manager (in *COBS*, *FINMAR* and (in relation to *firm type*) in *SUP* 16.10 (Confirmation of ~~*standing data*~~ standing data)) a *person* who, acting only on behalf of a *client*, manages *designated investments* in an account or portfolio on a discretionary basis under the terms of a discretionary management agreement.

~~*financial system* (as defined in section 3 of the *Act* (Market confidence)) the financial system operating in the *United Kingdom* including:~~

~~(a) financial markets and exchanges;~~

~~(b) *regulated activities*; and~~

~~(c) other activities connected with financial markets and exchanges.~~

market maker

(1) (except in *COBS* and *FINMAR*) (in relation to an *investment*) a *person* who (otherwise than in his capacity as the *operator* of a *regulated collective investment scheme*) holds himself out as able and willing to enter into transactions of sale and purchase in *investments* of that description at prices determined by him generally and continuously rather than in respect of each particular transaction.

(2) (in *COBS*) a *person* who holds himself out on the financial markets on a continuous basis as being willing to deal on own account by buying and selling *financial instruments* against his proprietary capital at prices defined by him.

[**Note:** article 4(1)(8) of *MiFID*]

(3) (in *FINMAR*) a *person* who, ordinarily as part of his business, deals as principal in *financial instruments* (whether *OTC* or exchange traded):

(a) to fulfil orders received from another *person* in response to that *person's* request to trade or to hedge positions arising out of those dealings; or

(b) in a way that ordinarily has the effect of providing liquidity on a regular basis to the financial markets on both bid and offer sides of the market in comparable size.

net short position	(1)	(except in *IPRU(INV)* 13 and *FINMAR*) a net short position which gives rise to an economic exposure to the issued *share* capital of a company. Any calculation of whether a *person* has a short position must take account of any form of economic interest in the *shares* of the company.
	…	
	(3)	(in *FINMAR*) a position which gives rise to an economic exposure to the issued capital of a *company*, calculated in accordance with *FINMAR* 2.
non-discretionary investment manager	(in *FINMAR* and in relation to *firm type* in *SUP* 16.10 (Confirmation of ~~*standing data*~~ standing data)) a *person* who, acting only on behalf of a *client*, manages *designated investments* in an account or portfolio on a non-discretionary basis under the terms of a non-discretionary management agreement.	
overseas regulator	(1)	(except in relation to the *overseas financial stability information power*) (as defined in section 195(3) of the *Act* (Exercise of power in support of overseas regulator)) an authority in a country or territory outside the *United Kingdom*:
		(a) …
		…
	(2)	(in relation to the *overseas financial stability information power*) (as defined in section 169A(2) of the *Act* (Support of overseas regulator with respect to financial stability)) an authority in a country or territory outside the *United Kingdom* which exercises functions with respect to the stability of the *relevant financial system* operating in that country or territory.
rights issue	(in *LR* and *FINMAR*) an offer to existing *security* holders to subscribe or purchase further *securities* in proportion to their holdings made by means of the issue of a renounceable letter (or other negotiable document) which may be traded (as "nil paid" rights) for a period before payment for the *securities* is due.	
rights issue period	the period that commences on the date a *company* announces a ~~rights issue~~ *rights issue* and which ends on the date that the ~~*shares*~~ *securities* issued under the ~~rights issue~~ *rights issue* are admitted to trading on a *prescribed market*.	

Annex C

Amendments to the Threshold Conditions (COND)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1.1.1 G *COND* applies to every *firm*, except that:

…

(3) *threshold conditions* 3, 4 and 5 do not apply to a *Swiss General Insurance Company*; and

(4) *COND* 2.6 (Additional conditions) is only relevant to *non-EEA insurers*~~; and~~.

(5) ~~*COND* 3.1 is only relevant to *firms* falling within the scope of the Banking Act 2009 (see *COND* 3.1.1G).~~ [deleted]

…

COND 3 is deleted in its entirety. The deleted text is not shown struck through.

3 Banking Act 2009 [deleted] This chapter has been moved to FINMAR 3

Annex D

Amendments to the Market Conduct sourcebook (MAR)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.9 Market abuse (misleading behaviour) and market abuse (distortion)

…

1.9.2A E ~~Failure by a person to give adequate disclosure that he has reached or exceeded a *disclosable short position* where:~~

~~(1) that position relates, directly or indirectly, to *securities* which are the subject of a rights issue; and~~

~~(2) the *disclosable short position* is reached or exceeded during a *rights issue period*;~~

~~is *behaviour* which, in the opinion of the *FSA*, is *market abuse (misleading behaviour).*~~ [deleted]

1.9.2B R ~~For the purposes of *MAR* 1.9.2AE, "adequate disclosure" means disclosure made on a *RIS* by no later than 3.30pm on the *business day* following the date on which the *disclosable short position* is reached or exceeded. The disclosure must include the name of the person who has the *disclosable short position*, the *disclosable short position* and the name of the *issuer* of the *qualifying instruments*.~~ [deleted]

Short selling in relation to financial sector companies

1.9.2C E …

1.9.2D E (1) ~~Failure by a person who has a *disclosable short position* in a *UK financial sector company* to provide adequate ongoing disclosure of their position is *behaviour* which, in the opinion of the *FSA*, is *market abuse (misleading behaviour).*~~ [deleted]

(2) ~~In (1), "adequate ongoing disclosure" means disclosure made on a *RIS* by no later than 3.30pm on the *business day* following the day on which the position reaches, exceeds or falls below a *disclosable short position* of 0.25%, 0.35%, 0.45% and 0.55% of the issued share capital of the company and each 0.1% threshold thereafter.~~ [deleted]

(a) [deleted]

(b) [deleted]

(2A) ~~The disclosure referred to in (1) must include the name of the person who has the position, the amount of the *disclosable short position*~~

~~and the name of the company in relation to which it has that position.~~ [deleted]

(3) ~~For the avoidance of doubt, changes in a *disclosable short position* between the thresholds referred to in (2) do not need to be disclosed under this section. For example, an increase from 0.25% to 0.31% of the issued share capital of the company does not need to be disclosed.~~ [deleted]

(4) ~~For the avoidance of doubt, (1) applies during a *rights issue period*.~~ [deleted]

(5) [deleted]

Financial Services Compensation Scheme (Financial Services Act 2010) Instrument 2010

FINANCIAL SERVICES COMPENSATION SCHEME (FINANCIAL SERVICES ACT 2010) INSTRUMENT 2010

Powers exercised

A. The Financial Services Authority makes this instrument in the exercise of:

(1) the powers and related provisions in the following sections of the Financial Services and Markets Act 2000 ("the Act"):

(a) section 138 (General rule-making power);
(b) section 156 (General supplementary powers);
(c) section 157(1) (Guidance);
(d) section 213 (The compensation scheme); and
(e) section 214 (General); and

(2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.

B. The rule-making powers referred to above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on 6 August 2010.

Amendments to the Handbook

D. The Glossary of definitions is amended in accordance with Annex A to this instrument.

E. The Fees manual (FEES) is amended in accordance with Annex B to this instrument.

Citation

F. This instrument may be cited as the Financial Services Compensation Scheme (Financial Services Act 2010) Instrument 2010.

By order of the Board
22 July 2010

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text.

compensation costs the costs incurred:

(a) in paying compensation; or

(b) as a result of making the arrangements contemplated in *COMP* 3.3.1R or taking the measures contemplated in *COMP* 3.3.3R; or

(c) in making payments or giving indemnities under *COMP* 11.2.3R; or

(d) under section 214B or section 214D of the *Act*; or

(e) by virtue of section 61 (Sources of compensation) of the Banking Act 2009.

Annex B

Amendments to the Fees manual (FEES)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

6.1.9 G Section 223 of the *Act* (Management expenses) prevents the *FSCS* from recovering, through a levy, any *management expenses* attributable to a particular period in excess of the limit set in *COMP* as applicable to that period. 'Management expenses' are defined in section 223(3) to mean expenses incurred or expected to be incurred by the *FSCS* in connection with its functions under the *Act*, except:

(1) expenses incurred in paying compensation; ~~and~~

(2) expenses incurred as a result of the *FSCS* making the arrangements to secure continuity of insurance set out in *COMP* 3.3.1R and *COMP* 3.3.2R or taking the measures set out in *COMP* 3.3.3R and *COMP* 3.3.4R when a *relevant person* is an *insurer* in financial difficulties; and

(3) expenses incurred under section 214B or section 214D of the *Act* as a result of the *FSCS* being required by HM Treasury to make payments in connection with the exercise of the stabilisation power under Part 1 of the Banking Act 2009.

…

6.1.15 G *Compensation costs* are principally the costs incurred in paying compensation. Costs incurred in securing continuity of long-term insurance in safeguarding *eligible claimants* when insurers are in financial difficulties, ~~and~~ in making payments or giving indemnities under *COMP* 11.2.3R and as a result of the *FSCS* being required by HM Treasury to make payments in connection with the exercise of the stabilisation power under Part 1 of the Banking Act 2009 are also treated as *compensation costs*. For funding purposes, these costs are allocated by the *FSCS*, and met by *participant firms*, in the same way as *specific costs* up to relevant *levy limits* and then in accordance with the allocation provisions in *FEES* 6.5.2R.

Consequential amendments (Financial Services Act 2010) Instrument 2010

CONSEQUENTIAL AMENDMENTS (FINANCIAL SERVICES ACT 2010) INSTRUMENT 2010

Powers exercised

A. The Financial Services Authority makes this instrument in the exercise of:

(1) the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(a) section 138 (General rule-making power);
(b) section 156 (General supplementary powers);
(c) section 157(1) (Guidance); and

(2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.

B. The rule-making powers referred to above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on 6 August 2010.

Amendments to the Handbook

D. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Glossary of definitions	Annex A
Principles for Businesses (PRIN)	Annex B
Senior Management Arrangements, Systems and Controls sourcebook (SYSC)	Annex C
Threshold Conditions (COND)	Annex D
Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)	Annex E
Prudential sourcebook for Insurers (INSPRU)	Annex F
Prudential sourcebook for UCITS Firms (UPRU)	Annex G
Supervision manual (SUP)	Annex H
Compensation sourcebook (COMP)	Annex I
Credit Unions sourcebook (CRED)	Annex J
Electronic Money sourcebook (ELM)	Annex K
Professional Firms sourcebook (PROF)	Annex L
Recognised Investment Exchanges and Recognised Clearing Houses sourcebook (REC)	Annex M

Citation

E. This instrument may be cited as the Consequential Amendments (Financial Services Act 2010) Instrument 2010.

By order of the Board
22 July 2010

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text.

consumer	(1) …
	(2) (in relation to the *FSA's* power to make general *rules* (section 138 of the *Act* (General rule-making power))), the approval requirements for *controllers* (section 186 of the *Act* (Objection to acquisition of control)), the publication of notices (section 391 of the *Act* (Publication)) and the exercise of *Treaty rights* (Schedule 4 to the *Act* (Treaty rights))) ~~(as defined in section 138(7) of the *Act* (General rule-making power))~~ a *person*:
	…
prudential context	in relation to activities carried on by a *firm*, the context in which the activities have, or might reasonably be regarded as likely to have, a negative effect on:
	(a) confidence in the <u>*UK* *financial system*</u>; or
	…
regulatory objectives	(as described in sections 2(2) and 3 to 6 of the *Act*)
	(a) market confidence;
	(b) public awareness;
	(c) the protection of *consumers*; ~~and~~
	(d) the reduction of *financial crime*<u>; and</u>
	<u>(e) financial stability</u>.

Annex B

Amendments to the Principles for Businesses (PRIN)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.1.6 G As set out in *PRIN* 3.3 (Where?), *Principles* 1 (Integrity), 2 (Skill, care and diligence) and 3 (Management and control) apply to world-wide activities in a *prudential context*. *Principle* 5 (Market conduct) applies to world-wide activities which might have a negative effect on confidence in the *UK financial system* ~~operating in the *United Kingdom*~~. In considering whether to take regulatory action under these *Principles* in relation to activities carried on outside the *United Kingdom*, the *FSA* will take into account the standards expected in the market in which the *firm* is operating. *Principle* 11 (Relations with regulators) applies to world-wide activities; in considering whether to take regulatory action under *Principle* 11 in relation to cooperation with an overseas regulator, the *FSA* will have regard to the extent of, and limits to, the duties owed by the *firm* to that regulator. (*Principle* 4 (Financial prudence) also applies to world-wide activities.)

…

3.3.1 R Territorial application of the Principles

Principle	Territorial application
…	
Principle 5	if the activities have, or might reasonably be regarded as likely to have, a negative effect on confidence in the *UK financial system* ~~operating in the *United Kingdom*~~, applies with respect to activities wherever they are carried on; otherwise, applies with respect to activities carried on from an establishment maintained by the *firm* (or its *appointed representative*) in the *United Kingdom*.
…	

Annex C

Amendments to the Senior Management Arrangements, Systems and Controls sourcebook (SYSC)

In this Annex, underlining indicates new text and striking through indicates deleted text.

3.2.11 G (1) …

(2) Risks of regulatory concern are those risks which relate to the fair treatment of the *firm's customers*, to the protection of *consumers*, to confidence in the *UK financial system*, ~~and~~ to the use of that system in connection with *financial crime*, and to financial stability.

…

14.1.4 G The purpose of this section is to serve the *FSA's regulatory objectives* of consumer protection, ~~and~~ market confidence and financial stability. In particular, this section aims to reduce the risk that a *firm* may pose a threat to these *regulatory objectives*, either because it is not prudently managed, or because it has inadequate systems to permit appropriate senior management oversight and control of its business.

…

14.1.51 G *SYSC* 3.2.20R requires a *firm* to take reasonable care to make and retain adequate records. The following policy on record keeping supplements *SYSC* 3.2.20R by providing some additional *rules* and *guidance* on record keeping in a *prudential context*. The purpose of this policy is to:

(1) …

(2) help the *FSA* to satisfy itself that a *firm* is operating in a prudent manner and is not prejudicing the interests of its *customers*, ~~or~~ market confidence or financial stability.

…

15.1.5 G Credit risk concerns the *FSA* in a *prudential context* because inadequate systems and controls for credit risk management can create a threat to the *regulatory objectives* of market confidence, ~~and~~ consumer protection and financial stability by:

…

…

17.1.4 G Insurance risk concerns the *FSA* in a *prudential context* because inadequate systems and controls for its management can create a threat to the *regulatory objectives* of market confidence, ~~and~~ consumer protection and financial

stability. Inadequately managed insurance risk may result in:

…

Annex D

Amendments to the Threshold Conditions (COND)

In this Annex, underlining indicates new text and striking through indicates deleted text.

2.5.7 G In determining whether a *firm* will satisfy and continue to satisfy *threshold condition* 5 in respect of having competent and prudent management and exercising due skill, care and diligence, relevant matters, as referred to in *COND* 2.5.4G(2), may include, but are not limited to whether:

…

(2) if appropriate, the *governing body* of the *firm* includes non-executive representation, at a level which is appropriate for the control of the *regulated activities* proposed, for example, as members of an audit committee ~~(see *COND* 3.2.15G (Audit Committee))~~;

…

(9) the *firm* has conducted enquiries (for example, through market research or the previous activities of the *firm*) that are sufficient to give it reasonable assurance that it will not be posing unacceptable risks to *consumers* or the *UK financial system*;

…

Annex E

Amendments to the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)

In this Annex, underlining indicates new text.

12.3.9 G As part of the *SLRP*, the *FSA* will assess the appropriateness of the *liquidity risk* tolerance adopted by an *ILAS BIPRU firm* to ensure that this risk tolerance is consistent with maintenance by the *firm* of adequate liquidity resources for the purpose of the *overall liquidity adequacy rule*. The *FSA* will expect a *firm* to provide it with an adequately reasoned explanation for the level of *liquidity risk* which that *firm's governing body* has decided it should assume. In assessing the appropriateness of the *liquidity risk* tolerance adopted by a *firm*, the *FSA* will consider whether the tolerance adopted is consistent with the *firm's* satisfaction of *threshold condition* 5 (*COND* 2.5.7G(6)). Consistent with the *FSA's* statutory objectives under the *Act*, in assessing the appropriateness of a *firm's* adopted *liquidity risk* tolerance the *FSA* will also have regard to the role and importance of a *firm* in the *UK financial system*.

…

12.4.3 G Consistent with *BIPRU* 12.3.5R, the *FSA* expects that the extent and frequency of such testing, as well as the degree of regularity of *governing body* review under *BIPRU* 12.4.2R, should be proportionate to the nature scale and complexity of a *firm's* activities, as well as to the size of its liquidity risk exposures. Consistent with the *FSA's* statutory objectives under the *Act*, in assessing the adequacy of a *firm's* stress testing arrangements (including their frequency and the regularity of *governing body* review) the *FSA* will also have regard to the role and importance of that *firm* in the *UK financial system*. The *FSA* will, however, expect stress testing and *governing body* review to be carried out no less frequently than annually. The *FSA* expects that a *firm* will build into its stress testing arrangements the capability to increase the frequency of those tests in special circumstances, such as in volatile market conditions or where requested by the *FSA*.

…

12.8.5 G This section represents merely an indication of the matters to which the *FSA* will have regard in considering an application for a *whole-firm liquidity modification* or an *intra-group liquidity modification*. In considering such an application, the *FSA* will always take into account anything that it reasonably considers to be relevant for the purposes of assessing whether the statutory tests in section 148 of the *Act* are met. In doing so, it will have regard to the role and importance of a *firm* or *UK branch* in the *UK financial system*.

…

12.8.12 G In determining the appropriate duration of an *intra-group liquidity modification*, the *FSA* will have regard to the role and importance of the *firm* in question in the *UK financial system*. In some cases, the *FSA* may take the view that an *intra-group liquidity modification* covering a *firm* whose role and importance in the *UK financial system* are significant ought to be reviewed more regularly than one granted in respect of a less systemically significant *firm*. The *FSA* will consider this issue in determining the appropriate duration of such a modification.

…

12.8.30 G In determining the appropriate duration of a *whole-firm liquidity modification*, the *FSA* will have regard to the role and importance of the *UK branch* in question in the *UK financial system*. In some cases, the *FSA* may take the view that a *whole-firm liquidity modification*, covering a *UK branch* whose role and importance in the *UK financial system* are significant, ought to be reviewed more regularly than one granted in respect of a less systemically significant *branch*. …

Annex F

Amendments to the Prudential sourcebook for Insurers (INSPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text.

5.1.4 G Operational risk concerns the *FSA* in a *prudential context* because inappropriate management of operational risk can adversely affect the solvency or business continuity of a *firm*, threatening the *regulatory objectives* of market confidence, ~~and~~ consumer protection and financial stability.

Annex G

Amendments to the Prudential sourcebook for UCITS Firms (UPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.2.1	G	(1)	The purpose of this sourcebook is to amplify *Principle* 4 (Financial prudence) which requires a *firm* to maintain adequate financial resources to meet its *designated investment business* commitments and to withstand the risks to which its business is subject. This assists in the achievement of the *regulatory objectives* of consumer protection, ~~and~~ market confidence and financial stability.

…

Annex H

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.1.3 G The design of these arrangements is shaped by the *regulatory objectives*. These are set out in section 2 of the *Act* (The Authority's general duties) and are:

(1) maintaining confidence in the *UK financial system*;

(1A) contributing to the protection and enhancement of the stability of the *UK financial system*;

(2) promoting public understanding of the *UK financial system*;

…

…

1.3.3 G The impact of a *firm* is assessed by reference to a range of factors derived from the *regulatory objectives*, including:

(1) …

(1A) the extent to which the *firm* may pose risks to the stability of the *UK financial system*;

…

…

2.1.3 G Achieving the *regulatory objectives* involves the *FSA* informing itself of developments in *firms* and in markets. The *Act* requires the *FSA* to monitor a *firm's* compliance with requirements imposed by or under the *Act* (paragraph 6 (1) of Schedule 1). The *Act* also requires the *FSA* to take certain steps to cooperate with other relevant bodies and regulators (section 354). For these purposes, the *FSA* needs to have access to a broad range of information about a *firm's* business.

…

2.1.5 G Part XI of the *Act* (Information Gathering and Investigations) gives the *FSA* statutory powers, including:

(1) to require the provision of information (see ~~section~~ sections 165, 165A, ~~and~~ *EG* 3 and *FINMAR* 1);

…

…

2.3.12 G In complying with *Principle* 11, the *FSA* considers that a *firm* should cooperate with it in providing information for other regulators. ~~Section~~ Sections 169 ~~of the *Act*~~ (Investigations etc. in support of overseas regulator) and 169A (Support of overseas regulator with respect to financial stability) of the *Act* ~~gives~~ give the *FSA* certain statutory powers to obtain information and appoint investigators for *overseas regulators* if required (see *DEPP* 7~~,~~ ~~and~~ *EG* 3 and *FINMAR* 1).

…

6.3.28 G (1) The *FSA* is required by section 41(2) of the *Act* to ensure that a *firm* applying to vary its *Part IV permission* satisfies and will continue to satisfy the *threshold conditions* in relation to all the regulated activities for which the *firm* has or will have *Part IV permission* after the variation. However, the *FSA's* duty under the *Act* does not prevent it, having regard to that duty, from taking such steps as it considers necessary in relation to a particular *firm*, to ~~secure its *consumer* protection objective~~ meet any of its *regulatory objectives*. This may include granting a *firm's* application for variation of *Part IV permission* when it wishes to wind down (run off) its business activities and cease to carry on new business as a result of no longer being able to satisfy the *threshold conditions*.

(2) In addition, the *FSA* may refuse the application if it appears that ~~the interests of *consumers*, or a group of *consumers*,~~ any of its *regulatory objectives* would be adversely affected if the application were to be granted and it is desirable ~~in the interests of *consumers*, or that group of *consumers*,~~ in order to meet any of its *regulatory objectives* for the application to be refused.

…

6.4.2 G Under section 44(3) of the *Act*, the *FSA* may refuse an application from a *firm* to cancel its *Part IV permission* if it appears that~~:~~ it is desirable for the application to be refused in order to meet any of the *FSA's regulatory objectives*.

~~(1) the interests of *consumers*, or potential *consumers*, would be adversely affected if the application were to be granted; and~~

~~(2) it is desirable in the interests of *consumers*, or potential *consumers*, for the application to be refused.~~

…

6 Annex 4.1G Additional guidance for a firm winding down (running off) its business

…	

3.	If appropriate, in the interests of ~~*consumer* protection~~ its *regulatory objectives*, the *FSA* will require details of the ~~firm's~~ *firm's* plans and will discuss them with the *firm* and monitor the winding down or transfer of the *firm's* business. During the period in which it is winding down, a *firm* will also be required to notify the *FSA* of any material changes to the information provided such as, for example, receipt of new complaints and changes to plans.
4.	…
Use of own-initiative powers	
5.	If, for example, the *FSA* has ~~*consumer* protection~~ concerns relating to any of the *regulatory objectives*, it may, however, use its *own-initiative power* under section 45 of the *Act* (Variation etc. on the Authority's own initiative) (see *SUP* 7 (Individual requirements) and *EG* 8 (Variation and cancellation of permission on the *FSA's* own initiative and intervention against incoming firms)) , to vary the *Part IV permission* of a *firm* which is winding down or transferring its *regulated activities*.
…	

…

7.1.5 G By waiving or modifying the requirements of a *rule* or imposing an additional *requirement* or *limitation*, the *FSA* can ensure that the *rules*, and any other *requirements* or *limitations* imposed on a *firm*, take full account of the *firm's* individual circumstances, and so assist the *FSA* in meeting the *regulatory objectives* (for example, to protect *consumers*, ~~and~~ maintain market confidence and contribute to financial stability).

…

7.2.2 G The circumstances in which the *FSA* may vary a *firm's Part IV permission* on its own initiative under section 45 of the *Act* include where it appears to the *FSA* that:

(1) …

(2) it is desirable to vary a *firm's permission* in order to ~~protect the interests of consumers or potential consumers~~ meet any of the *FSA's regulatory objectives*.

…

7.3.4 G The *FSA* will seek to give a *firm* reasonable notice of an intent to vary its *permission* and to agree with the *firm* an appropriate timescale. However, if the *FSA* considers that a delay may ~~be prejudicial to the interest of *consumers*~~ create a risk to any of the *FSA's regulatory objectives*, the *FSA* may need to act immediately using its powers under section 45 of the *Act* to

vary a *firm's Part IV permission* with immediate effect.

…

15.3.1 R A *firm* must notify the *FSA* immediately it becomes aware, or has information which reasonably suggests, that any of the following has occurred, may have occurred or may occur in the foreseeable future:

…

(4) any matter in respect of the *firm* which could result in serious financial consequences to the *UK financial system* or to other *firms*.

…

18.2.2 G The *FSA's regulatory objectives* include market confidence, financial stability and the protection of *consumers*. ~~Either or both~~ Any or all of these might be impaired if a transfer were approved that led to loss, or perceived loss, to *consumers* or other market participants. On the other hand a transfer that led to improved security or benefits for *consumers* would promote the *FSA's regulatory objectives*. When considering a transfer, the *FSA* needs to take into account the interests of existing *consumers* of the transferee and of *consumers* remaining with the transferor as well as of those whose contracts are being transferred. The *guidance* in this section is intended to protect *consumers*. By so doing it promotes the market confidence objective.

…

Sch 2 Notification requirements

…

Sch 2.2 G

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
…				
SUP 15.3.1R	Notifications - matters having a serious regulatory impact.	The fact of any of the trigger events occurring.	Becoming aware or having information which reasonably suggests, that any of the following has occurred, may have occurred or may occur in the foreseeable future:	Immediately.
			…	

			(4) any matter in respect of the *firm* which could result in serious financial consequences to the *UK financial system* or to other *firms*.	
…				

Annex I

Amendments to the Compensation sourcebook (COMP)

In this Annex, underlining indicates new text.

1.1.9 G This sourcebook is one of the means by which the *FSA* will meet its *regulatory objectives* of securing the appropriate degree of protection for *consumers*, contributing to the protection and enhancement of the financial stability of the *United Kingdom* and maintaining confidence in the *UK financial system*.

…

15.1.1 G When a *relevant person* is *in default* with claims against it for *protected deposits*, it may be desirable for the *FSCS* to make accelerated payments of compensation, for the protection of consumers, to contribute to financial stability and to maintain market confidence.

Annex J

Amendments to the Credit Unions sourcebook (CRED)

In this Annex, underlining indicates new text.

14.1.4 G The design of these arrangements is shaped by the *regulatory objectives*. These are set out in section 2 of the *Act* (The Authority's general duties) and are:

(1) maintaining confidence in the *UK financial system*;

(1A) contributing to the protection and enhancement of the stability of the *UK financial system*;

(2) promoting public understanding of the *UK financial system*;

…

…

14.6.4 G The *FSA* may vary a *credit union's Part IV permission* on its own initiative where:

(1) one or more of the *threshold conditions* is, or is likely to be, no longer satisfied;

(2) it is desirable in order to protect members;

(3) it is otherwise desirable in order to meet any of the *FSA's regulatory objectives*.

…

14.9.3 G *SUP* 15.3.1R states that a *credit union* must notify the *FSA* immediately it becomes aware, or has information which reasonably suggests, that any of the following has occurred, may have occurred or may occur in the foreseeable future:

…

(4) any matter in respect of the *credit union* which could result in serious financial consequences to the *UK financial system* or to other *firms*.

…

App 1.1 This is the table referred to in CRED 2.2.2G.

	Sourcebook or manual	**Reference code**
	…	

High Level Standards	The Fit and Proper test for Approved persons	*FIT*
	Financial Stability and Market Confidence sourcebook	*FINMAR*
	…	

Annex K

Amendments to the Electronic Money sourcebook (ELM)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.2.4 G The *rules* and *guidance* in *ELM* will help the *FSA* to meet the *regulatory objectives* of protecting *consumers*, ~~and~~ maintaining market confidence and protecting financial stability. They do so by setting standards about the backing of *e-money* issued by an *ELMI* with high quality liquid assets. They also do so by setting minimum capital and other risk management standards. This mitigates the risk that *ELMIs* will be unable to meet their liabilities and commitments to *consumers*. *ELM* also protects *consumers* by regulating the relationship between issuers of *e-money* and those who hold their *e-money*.

…

5.4.4 G The risks referred to in *SYSC* 7.1.4R and *SYSC* 7.1.5R relating to *e-money* include the following risks:

…

(4) use of the system referred to in (2) for *financial crime* or in a way that may harm or misuse any part of the *UK financial system*.

…

8.7.9 G The information or documents referred to in *ELM* 8.7.6G must be provided or produced before the end of the reasonable period, and at the place, specified by the *FSA*. The *FSA* may require the information to be provided in such form as it may reasonably require. The *FSA* may require the information to be verified, and the document authenticated, in such manner as it may reasonably require (see article 9G(6) of the *Regulated Activities Order* (Obtaining information from certified persons etc.) and section 165 of the *Act* (Authority's power to require information: authorised persons etc.)) ~~(Obtaining information from certified persons etc.)~~. The *FSA* may use the power to require information and documents from *small e-money issuers* in support of its enforcement functions.

Annex L

Amendments to the Professional Firms sourcebook (PROF)

In this Annex, underlining indicates new text.

1.1.6 G The *rules* and *guidance* in this sourcebook are intended to:

(1) …

(2) promote public understanding of the <u>*UK*</u> *financial system* by ensuring that the *clients* of an *exempt professional firm* are made aware that the firm is not an *authorised person*;

…

Annex M

Amendments to the Recognised Investment Exchanges and Recognised Clearing Houses sourcebook (REC)

In this Annex, underlining indicates new text and striking through indicates deleted text.

2.3.5 G In assessing whether a *UK recognised body* has sufficient financial resources in relation to counterparty and market risks, the *FSA* may have regard to:

(1) the amount and liquidity of its financial assets and the likely availability of liquid financial resources to the *UK recognised body* during periods of major market turbulence or other periods of major stress for the <u>*UK* *financial system*</u>; and

…

…

2.13.3 G In determining whether a *UK recognised body* is able and willing to promote and maintain high standards of integrity and fair dealing in the carrying on of *regulated activities*, the *FSA* may have regard to the extent to which the *UK recognised body* seeks to promote and encourage, through its rules, practices and procedures, conduct in *regulated activities* which is consistent with the *Code of Market Conduct* (see *MAR* 1) and with any other codes of conduct, rules or principles relating to behaviour in *regulated activities* which users of the <u>*UK* *financial system*</u> ~~in the *United Kingdom*~~ would normally expect to apply to the *regulated activity* and the conduct in question.

…

3.18.1 G …

(3) The information required under *REC* 3.18 is relevant to the *FSA's* supervision of the *UK recognised body's* obligations in relation to the enforceability of compliance with the *UK recognised body's* ~~*rules*~~ <u>rules</u>. It is also relevant to the *FSA's* broader responsibilities concerning market confidence <u>and financial stability</u> and, in particular, its functions in relation to *market abuse* and *financial crime*. It may also be necessary in the case of *members* based outside the *United Kingdom* to examine the implications for the enforceability of *default rules* or collateral and the settlement of transactions, and thus the ability of the *UK recognised body* to continue to meet the *recognition requirements*. It follows that the admission of a *member* from outside the *United Kingdom* who is not an *authorised person* could require notification under both *REC* 3.18.2R and *REC* 3.18.3R, although a single report from the *UK recognised body* covering both notifications would be acceptable to

the *FSA*.

…

4.6.4 G Under section 298(7) of the *Act* (Directions and revocation: procedure), the *FSA* need not follow the consultation procedure set out in the rest of section 298 (see *REC* 4.8), or may cut short that procedure, if it considers it essential to do so. The *FSA* is likely to consider it essential to cut short the procedure if, in the absence of immediate action, there would be:

…

(2) a serious threat to market confidence or to the stability of the *UK financial system*; or

…

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