Financial Conduct Authority

Regulator Assessment: Qualifying Regulatory Provisions

Title of proposal: PS14/9: Review of the client assets regime for investment business

Lead regulator: FCA

Date of assessment: January 2017

Commencement date: 1 June 2015

Origin: Domestic

Does this include implementation of a Cutting Red Tape review? No

Which areas of the UK will be affected? UK firms that are subject to the Client Assets sourcebook (CASS) because they conduct investment business and hold client money, custody assets, collateral and/or mandates in relation to that investment business (or rely on an exemption contained within CASS).

Brief outline of proposed new or amended regulatory activity

In CP13/5 we proposed changes to the rules in CASS to address specific risks, clarify the requirements firms must comply with and enhance our client assets regime to achieve better results for consumers and increase confidence in financial markets. In PS14/9, we published feedback to CP13/5, our response and final rules. The final rules in PS14/9 had a staggered implementation: some rules came into force on 1 July 2014, some in 1 December 2014 and the remaining on 1 June 2015. Although the changes constituted a complete overhaul of the CASS regime, the changes with greatest impact were implemented first.

For the purposes of this impact assessment, we are only focusing on the changes that came into force on 1 June 2015, as the Enterprise Act requirements apply to changes after 1 May 2015. These changes affected the custody rules (CASS 6), client money rules (CASS 7), mandate rules (CASS 8) and information to clients rules (CASS 9).

On CASS 6 and 7, we reordered the rules to improve readability and clarified existing provisions on record-keeping processes, depositing custody assets with third party custodians, money ceasing to be client money, cleared funds and treatment of physical receipts. We also updated record-keeping provisions to: accommodate firms that use integrated systems to maintain records for custody assets; prescribe a minimum frequency for reconciliations and other record checks; set out more detailed notifications requirements; and tighten requirements on registering firm assets. The changes were reported to have minimal impact because they provided flexibility for firms to use different methods and were in line with existing practices (save for the one-off cost explained on page 2).

On CASS 7, we enhanced due diligence requirements on banks and third parties holding client money, provided flexibility for clearing firms in certain situations to receive client money into a firm account and prescribed a procedure for firms that choose to prudently segregate money in a client account. No material impact was reported for these changes. We also limited the application of the 'delivery versus payment' exemption for collective investment schemes from a three-day to one-day window (see page 2 on the impact of this change).

On CASS 8, we clarified the form and content of records to be retained around mandates. On CASS 9, we clarified requirements on providing reports to clients on their client asset holdings and required firms to honour client requests for this information. No material impact was reported for these changes.

Consequential changes were made to the CASS Resolution Pack (CASS 10) and Client Money and Asset Return (CMAR) to reflect the above changes. No material impact was reported on the basis that it increased clarity for firms on these rules in relation to the above changes.

See pages 11 to 17 of PS14/9 (*PS14/9 'Review of the client assets regime for investment business'* (June 2014): https://www.fca.org.uk/publication/policy/ps14-09.pdf) for a full summary of the changes (the changes applicable to this assessment are denoted under the 'CASS Rule References at 1 June 2015').

Which type of business will be affected? How many are estimated to be affected?

The types of businesses affected and estimated to be affected by the relevant changes were:
- brokerage and other market intermediary firms (320 firms);
- asset managers and advisers (548 firms);
- custody firms (14 firms); and
- other firms that, in the course of investment business, hold client money and assets which are subject to the CASS regime (36 firms).

For further information, see page 84 of CP13/5 (*CP13/5 'Review of the client assets regime for investment business'* (July 2013): https://www.fca.org.uk/publication/consultation/cp13-05.pdf).

Price base year	**Implementation date**	**Duration of policy (years)**	**Business Net Present Value**	**Net cost to business (EANDCB)**	**BIT score**
2015	2015	10	-0.46	0.1	0.5

Please set out the impact to business clearly with a breakdown of costs and benefits

In developing this proposal we collected cost information from firms, via a survey, and reported this in the consultation paper (see CP13/5). Respondents indicated that total impact of measures (in scope of this assessment) had minimal impact either because they were clarificatory or reported to have minimal costs. This analysis was not challenged following consultation or, where there were challenges, we addressed these in PS14/9.

The only changes that had quantifiable costs (based on survey data in CP13/5 and PS14/9) were the following:

1. Custody recordkeeping, record checks and reconciliations[1]. Respondents to the 2013 pre-consultation costs survey estimated one-off costs of up to £100,000 for CASS large firms

[1] See page 12 of PS14/9 for summary of this change.

and up to £500 for CASS medium and small firms. There were no on-going costs reported. These estimates were not challenged during consultation or changed following PS14/9.

From internal data, we understand there were approximately 26 CASS large firms and 396 CASS small and medium firms in 2013. On this basis, we estimate this rule change resulted in a total one-off cost to industry of approximately £458,000 ((26 * 100,000) + (396 * 500)).

The principal benefit from the introduction of a new method of custody reconciliation was that firms could, in compliance with the rules, use integrated systems to maintain their records for custody assets, which a number of firms already had in place, if they were unable to maintain records for the traditional internal custody reconciliation method.

2. Limiting 'delivery versus payment' (**DvP**) exemption for collective investment schemes[2]. In CP13/5, we consulted on removing the DvP exemption (which allows fund managers to cease to treat money as client money under CASS for a period whilst carrying out a DvP transaction. The CASS rules cross refer to the collective investment scheme rules in this context.). Respondents to the 2013 pre-consultation costs survey estimated a median one-off cost of £4,000 and a median on-going cost of up to £21,000 if the DvP exemption was removed entirely, although we felt these figures were high.

   Following feedback to CP13/5, we decided to retain the DvP exemption but reduce it from a three-day to a one-day window. We noted in PS14/9 that the costs to firms to comply with the revised requirement is likely to be no more, if not considerably less, than the costs associated with removing DvP exemption in CP13/5[3]. We also consider there were no 'new' costs associated with the final proposal given that firms were still able to utilise the DvP window for some time and were already required to segregate any client money they held outside the DvP window under the CASS rules.

   Firms had always been required to be able to meet the requirements of CASS outside the DvP window unless they could arrange their business in such a way as to take it outside the scope of CASS; in order to make use of the DvP exemption, firms had to be subject to CASS in the first instance.

   We therefore believe that costs would only be incurred by firms that were not compliant with the CASS rules and that the high figures reported by firms in the pre-CP13/5 cost survey reflect this situation (rather than any new costs imposed by the reduction of the DvP window from three days to one day).

Please provide any additional information (if required) that may assist the RPC to validate the BIT Score.

[2] See page 14 of PS14/9 for a summary of this change.
[3] See paragraph 7.50, page 72 of CP13/5.