

# FCA Seeks Input on How to Implement Conduct of Business and Organisational Requirements for MiFID II

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Financial Services and Regulation

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## Introduction

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On 26 March the FCA published a new Discussion Paper (DP15/3) in which it is looking to engage with stakeholders on specific areas of the recast Markets in Financial Instruments Directive (MiFID II). The FCA has said it wants to open dialogue with those firms, trade bodies and consumer groups affected by the new MiFID II requirements at the earliest possible opportunity during the legislation transposition process in the United Kingdom (UK). The Discussion Paper also flags up some of the more important changes that MiFID II is expected to bring in for firms when its provisions take effect on 3 January 2017.

The FCA cautions that the Level 2 implementing measures for MiFID II have not yet been finalised, but once completed they will almost certainly affect the FCA's decision with regard to any UK rules. However, it still feels that publishing a Discussion Paper now is a worthwhile exercise which will allow it plenty of time to consider views from the industry properly and enable it to feed them into any policy development appropriately.

## What is in the Paper?

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The Discussion Paper invites feedback on the following policy topics relating to MiFID II transposition:

- the extent to which the FCA should apply MiFID II provisions to insurance-based investment products and pensions, particularly in light of the expected Insurance Distribution Directive (IDD) requirements which are currently being formulated under the European Union legislative process. The FCA believes that since consumers and firms are likely to treat insurance-based investments and pensions as credible substitutes for investment products governed by MiFID II then they should, in principle, be governed by the same conduct of business rules;
- the FCA's three proposed options for how it may incorporate MiFID II's investor protection measures for structured deposits into the FCA Handbook. It suggests either:

- copying out the relevant MiFID II provisions into the FCA Banking Conduct of Business Sourcebook (BCOBS) and making them applicable only to firms advising on and selling structured deposits; or
  - applying relevant MiFID II requirements to structured deposits through the Conduct of Business Sourcebook (COBS), whilst making it clear that the non-relevant parts of COBS would be expressly disapplied for structured deposits; or
  - to incorporate structured deposits fully into COBS, whilst at the same time retaining the relevant BCOBS rules and existing guidance which would also apply;
- requesting feedback on whether the FCA should ban discretionary investment management firms from accepting commissions and other benefits. Specifically, the FCA is looking to find out whether consumer outcomes in this sector would be improved by putting in place similar rules to the Retail Distribution Review (RDR) and, thereby, banning the acceptance of such commissions, fees and benefits (including immediate client rebating) for discretionary investment management activities. Interestingly, the FCA also asks whether it should look to develop a regime similar to its approach to platforms, where it bans cash rebates (other than small amounts) but allows rebates to be given back to clients in units;
  - the proposed policy options for changes to the criteria for local authorities to be treated as elective professional clients;
  - how the FCA should adopt new requirements for independent advice on shares, bonds, derivatives and structured deposits, in light of MiFID II's introduction of a new European-wide standard for "independent advice" for the first time. The MiFID II requirement focuses on ensuring that firms that offer independent advice do not limit the products considered to those of the advisory firm, or firms with close links to the advisory firm, to prevent any potential conflicts of interest that may occur. In particular, the FCA requests views on whether MiFID II's standard of independent advice is different to that currently adopted by the RDR;
  - the extent to which the FCA should apply MiFID II's remuneration rules for sales staff and advisors to non-MiFID firms in light of domestic and European policy developments. MiFID II presents the FCA with an opportunity to consider whether it would be beneficial to develop "cross-cutting obligations" for non-MiFID II firms, based on MiFID II remuneration standards for sales staff and advisors, regardless of the type of business they conduct;
  - how the FCA should make changes to the existing regime for the recording of telephone conversations and electronic communications to implement a regime for firms which fall within the Article 3 exemption of MiFID II, which is "at least analogous" to the standard requirements for MiFID II firms. The sorts of firms within scope of the Article 3 exemption include independent financial advisers and corporate finance boutiques. The FCA is also considering whether to remove the current recording exemptions for discretionary investment managers in the UK;
  - the practical aspects of how the FCA should implement and align MiFID II's requirements relating to the disclosure of all costs and charges associated with an investment service and financial instrument, which are not caused by the occurrence of underlying market risk at the point of sale and, as appropriate, on an annual basis. The FCA is interested in finding out whether there are any specific technical

challenges which firms will face and whether there should be a standardised format for making such disclosures;

- the FCA's likely approach to the enhanced MiFID II requirements relating to the types of third party inducements firms may receive. The FCA is intending to copy across the more restrictive inducements regime to firms providing restricted advice so as to maintain domestic consistency in line with the current RDR advisor charging rules;
- the likely restrictions on products able to be classified as "non-complex" and the practical application of the appropriateness test to a wider range of complex products. The FCA states expressly that the types of products which it considers to be "non-complex" will be significantly limited under its new rules. In particular, non-UCITS collective investment schemes, such as NURs, are likely to be considered complex, and therefore subject to the appropriateness test.

## What's Next?

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The FCA is inviting comments and views in connection with the Discussion Paper via an on-line response form or by writing to it direct and using the address specified in the Discussion Paper until 26 May 2015. The FCA is then expected to consult on the necessary changes to its Handbook in December, once it has considered the feedback from the Discussion Paper properly and with a view to confirming its final rules ahead of the July 2016 transposition deadline. The FCA's latest timeline relating to the implementation of MiFID II in the UK may be accessed [here](#).

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Financial Services and Regulation practice group:

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