



London Update

UK Financial Services Regulatory Developments

August 2007

FSA Reverses Proposed Amendments to UK Listing Rules

On June 29, the Financial Services Authority (FSA) announced the results of its feedback and further consultation on the Listing Review for Investment Entities in consultation paper CP07/12. The details of the proposal for the revised Listing Rules for Investment Entities comprised a withdrawal of a prior proposal that would have permitted close ended funds incorporated outside the UK to obtain a London listing by complying with lower level requirements than for UK investment funds.

The FSA has announced that it will amend the section of its listing rules applicable to investment funds to make London listings more attractive to alternative investment funds. Proposed changes include: (i) permitting listing of feeder funds, (ii) relaxing requirements for investment manager experience and (iii) modifying requirements for an independent board of directors.

http://www.fsa.gov.uk/pubs/cp/cp07_12.pdf

JMLSG Consults on Changes to Anti-Money Laundering Guidance

On June 29, the Joint Money Laundering Steering Group (JMLSG) announced that it is consulting on proposed amendments to its risk-based anti-money laundering guidance to reflect the UK Money Laundering Regulations 2007. The amendments, once confirmed and approved by HM Treasury, will update the JMLSG's guidance to include the 2007 Regulations which will implement the EU Third Money Laundering Directive.

Comments are invited by September 7.

<http://www.jmlsg.org.uk/bba/jsp/polopoly.jsp?d=751&a=9852>

FSA Announces New Market Abuse Strategy

The FSA announced its new Market Abuse Strategy on July 2. The Regulator first emphasised the need to prevent misuse of inside information and other forms of market abuse, focusing on the need for firms' senior management to take an active role in achieving this and the FSA's enforcement strategy against errant firms.

In speeches by Margaret Cole, the current FSA director of enforcement, on June 29 and John Tiner, the departing FSA chief executive on July 2, both mentioned the importance of the FSA being granted the power to offer immunity or plea bargains in exchange for agreements to give evidence.

The FSA called on all firms, whether regulated or not, to strengthen their controls. The FSA's markets division is drawing up a statement of good practice to improve standards among non-FSA regulated firms. The FSA has approached the Solicitors Regulation Authority about possible changes to the new Solicitors Code of Conduct as part of its drive to clamp down on insider trading.

The remainder of the new strategy was announced in one of the FSA's newsletters, its *Markets Division Market Watch*, on market conduct which detailed good practices and appropriate high level policies and procedures for regulated firms. These included:

- firms being less complacent about the effectiveness of their existing internal procedures;
- documented policies understood by all relevant staff;

- effective information barriers; and
- IT controls to limit access to inside information.

Significantly, in light of a number of other recent reports, there was no focus on particular market participants: hedge funds, private equity funds and prime brokers were not specifically mentioned or targeted.

http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2007/0629_mc.shtml

http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2007/0702_jt.shtml

http://www.fsa.gov.uk/pubs/newsletters/mw_newsletter21.pdf

FSA Launches Discussion on MTF Trading Oversight

Following proposals by HM Treasury in February 2007 to modernize stamp duty relief on the trading of shares, the FSA published a discussion paper on July 5 to consider potential issues raised by FSA's oversight of markets for multilateral trading facilities (MTFs).

HM Treasury is extending tax relief available for intermediaries trading shares admitted to a regulated market, including over-the-counter (OTC) trades. The tax relief aims to ensure a single sale is not subject to multiple charges. HM Treasury is also considering extending the relief beyond regulated markets to shares trading on MTFs.

The discussion paper invites comments by September 7.

http://www.fsa.gov.uk/pubs/discussion/dpo7_o3.pdf

FSA Publishes Quarterly Consultation

On July 6, the FSA published its 13th quarterly consultation (CP07/13) with various proposals to amend the FSA Handbook's glossary of definitions, Insurance Prudential sourcebooks, Fees Manual, Market Conduct sourcebook and New Collective Investment Schemes sourcebook.

The quarterly consultation includes proposed clarifications on the application of FSA's Code of Market Conduct to block trades and proposals to allow non-UCITS retail schemes (i.e., funds outside the EU undertakings for collective investments in transferable securities directives) to hold real estate assets through a special purpose vehicle and clarifications on payments to third parties out of scheme property.

http://www.fsa.gov.uk/pubs/cp/cpo7_13.pdf

Principles for Distribution of Retail Structured Products Published

On July 10, the International Capital Market Association (ICMA), International Swaps and Derivatives Association (ISDA), London Investment Banking Association (LIBA), Securities Industry and Financial Markets Association (SIFMA) and the European Securitisation Forum (ESF) jointly published a set of non-binding principles relating to the distribution of retail structured products (the "Retail Structured Products Principles").

Structured products are described in the Retail Structured Products Principles as including "a variety of financial instruments that combine various cash assets and/or derivatives to provide a particular risk-reward profile that would not otherwise be available in the market".

The Principles focus on the management of the relationship between providers and intermediary distributor banks of structured products, and seek to address issues that firms should consider when delivering structured products to retail investors.

<http://www.isda.org/press/RSP-Principles071007.pdf>

Reform of FSA's Procedures for Regulatory Guidance

Following a consultation issued in May 2006, HM Treasury has amended the way in which the FSA consults on and makes guidance. A Regulatory Reform Order (RRO) was laid before Parliament in May 2007 to pass the changes and the RRO took effect on July 12.

The RRO has abolished the requirements contained in the Financial Services and Markets Act 2000 for the FSA, as part of any consultation on proposed guidance, to publish: (i) a cost benefit analysis, (ii) an explanation of the guidance's

purpose, (iii) an explanation of why FSA believes the proposed guidance is compatible with their general duties, (iv) an account of representations made and any responses and (v) an account of any difference between the proposed guidance and the actual guidance made. Until the RRO, only the FSA Board could exercise the legislative function of issuing general guidance. The RRO now allows a committee or sub-committee of the FSA Board to issue general guidance.

Taken together these procedures should simplify the process of consulting on guidance and facilitate its issuance.

http://www.fsa.gov.uk/pubs/policy/ps07_10.pdf

LSE Launches Specialist Fund Market

On July 13, the London Stock Exchange (LSE) announced the launch of a new Specialist Fund Market (SFM) for alternative investment funds which target non-retail investors. The SFM will be subject to a “light touch” regulatory regime and is targeted at specialist funds that are seeking a quotation on a regulated market. The SFM will be a “regulated market” for the purposes of EU law. Funds admitted to the SFM will therefore be required to prepare a prospectus meeting the requirements of the EU Prospectus Directive – the so-called directive minimum requirement.

This development dovetails with the FSA’s revised proposals for the listing of investment entities covered in the July 20, 2007 edition of the *Corporate and Financial Weekly Digest*. The requirements of the SFM regime will be similar to the Listing Rules chapter 14 proposal withdrawn by the Financial Services Authority. The FSA’s withdrawn proposal would have applied to funds directed at retail investors unlike the SFM which will target professional investor funds only.

The SFM regime will be lighter touch than the chapter 15 Listing Rules regime which will apply to funds aimed at retail investors.

<http://www.londonstockexchange.com/NR/exeres/CAF85279-3285-47B4-A5A6-E66269AoE8E2.htm>

Hector Sants Appointed Chief Executive of FSA

Hector Sants, FSA’s managing director of wholesale and institutional markets was appointed chief executive of the FSA on July 13th. The appointment was effective when current chief executive John Tiner stepped down after FSA’s Annual Public Meeting on July 20th.

Mr Sants joined the FSA in May 2004 and was chief executive of Credit Suisse First Boston’s Europe, Middle East and Africa operations prior to joining the FSA. John Tiner had been chief executive of the FSA since September 2003.

<http://www.fsa.gov.uk/pages/Library/Communication/PR/2007/086.shtml>

BVCA Working Group Publishes Private Equity Consultation

On July 17, a British Private Equity and Venture Capital Association (BVCA) high-level industry working group issued a consultative document that makes recommendations about the need for self-regulation by the private equity industry. The working group, chaired by Sir David Walker, Senior Adviser at Morgan Stanley International (and a former Executive Director of the Bank of England and former Chairman of the Financial Services Authority’s predecessor regulator, the Securities and Investments Board) was established in March 2007.

The document proposes that private equity firms should provide: (i) identification of the management company’s leadership team, (ii) a commitment to conform to proposed guidelines, (iii) conflicts of interest and corporate social responsibility policies; (iv) indications of funds’ performance, and (v) disclosure of the limited partners in their funds, including banks and private individuals.

The document also included disclosure proposals for portfolio companies and guidelines for the collection of fund data.

The consultation period for comments on the proposals runs until October 9.

http://walkerworkinggroup.com/sites/10051/files/walker_consultation_document.pdf

FSA Publishes Further Consultation on Implementing MiFID

On July 18, the FSA published consultation paper CP07/16 *Consequential Handbook Amendments (arising from implementation of MiFID and creation of NEWCOB)*. The paper seeks views on proposed consequential amendments to the Handbook to reflect changes FSA has made in implementing the Markets in Financial Instruments Directive (MiFID) and in the new Conduct of Business Sourcebook (COBS).

The proposals include: (i) the application of the “customer principles” in the Principles for Businesses Sourcebook (PRIN) to non-designated investment business, (ii) amendments to the rules in the Senior Management Arrangements, Systems and Controls sourcebook (SYSC) relating to apportionment and oversight and senior management responsibility, (iii) amending the approved persons regime, (iv) amending MiFID transaction reporting requirements to take into account CESR guidance relating to transaction reporting and (v) revisions to the arrangements for Trade Data Monitors (TDMs).

This consultation covers changes relevant to both MiFID and non-MiFID firms and business within and outside the scope of MiFID.

The consultation period closes on September 14, except for comments on Chapter 6 (Post-trade transparency and trade data monitors) which closes on August 15.

http://www.fsa.gov.uk/pubs/cp/cpo7_16.pdf

HMRC Issues Revised Statement of Practice on IME

On July 20, HM Revenue and Customs (HMRC) issued its revised Statement of Practice (SP) 1/01 *Treatment of Investment Managers and their Overseas Clients* which deals with the Investment Manager Exemption (IME). The IME provides an exemption from UK taxation for non-UK funds with an investment manager based in the UK, provided that the manager is independent. The SP (first issued in 2001) explains HMRC practice with respect to IME’s qualifying conditions.

The general industry reaction to the revised SP is that it is an improvement on its predecessors. Indeed, HMRC has emphasized on page 1 of the revised SP that it is committed to maintaining a tax environment which enables non-residents to appoint UK based investment managers without the risk of liability to UK taxation, and to providing greater flexibility for investment managers and expanding the scope of exempt activities.

http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?_nfpb=true&_pageLabel=pageLibrary_ShowContent&id=HMCE_PROD1_o27709&propertyType=document

UK Treasury and FSA Jointly Consult on New Framework for Covered Bonds

On July 23, the UK Treasury and the FSA announced a consultation on proposals that will allow UK issued covered bonds, a class of corporate bond where interest and repayment of the principal is “guaranteed” by ring-fenced assets, to benefit from options on EU Directives.

The lack of a covered bond regime in the UK has been cited as a prime reason why the development of long-term fixed rate mortgage lending has been restricted.

The proposed framework is designed to provide the necessary underpinning for compliance with the EU’s Undertakings for Collective Investment in Transferable Securities (UCITS) Directive. For example, covered bonds that comply with the UCITS Directive benefit from higher prudential investment limits. UCITS can invest up to 25 % (rather than 5%) of their assets in the compliant covered bonds of one issuer.

In summary, the proposals would require that: (i) the issuer must be a credit institution with a UK registered office, (ii) UK recognized covered bonds will be regulated by the FSA, (iii) bonds must be supported by an asset pool, (iv) the asset pool must have sufficient collateral to cover bondholder claims throughout the whole term of the bond, and (v) bondholders must have a priority claim on the asset pool in the event of insolvency.

The consultation period ends on October 15.

http://www.fsa.gov.uk/pubs/cp/cp_bonds_hmt.pdf

FSA Sets Out Good Practice for Managing Compliance Risk

On July 25, the FSA published its observations on good practices for managing compliance risk in major investment banks. FSA is promoting an integrated approach to the effective management of compliance risk that takes into account the size and complexity of a firm’s business and is based upon senior management engagement. FSA will refer to these good practices when engaging with FSA regulated entities.

The good practices are grouped into six areas: (i) having a clear understanding of what is meant by compliance risk, (ii) establishing a compliance culture, (iii) involving senior management, (iv) establishing a compliance risk assessment methodology, (v) compliance monitoring, and (vi) evaluating the effectiveness of compliance performance.

http://www.fsa.gov.uk/pubs/ceo/compliance_risk.pdf

UK Money Laundering Regulations Published

HM Treasury announced on July 25 the new Money Laundering Regulations 2007 will come into effect on December 15, 2007. The Money Laundering Regulations build on responses to the UK Government's consultation on the draft Regulations, published in January 2006. The new Regulations are effective across a wider spread of businesses than the previous regulations including the financial sector, professionals such as lawyers and accountants, casinos, trust and company service providers and estate agents.

http://www.hm-treasury.gov.uk/consultations_and_legislation/money_laundering_directive/consult_moneylaundering_2007.cfm

<http://www.opsi.gov.uk/si/si2007/20072157.htm>

FSA Publishes Further Information on Listing Issues

On July 25, the FSA published issue 16 of its *List!* newsletter. The latest issue includes feedback on (a) common issues with prospectuses; (b) the application of the convertible bond exemption in the Prospectus Directive; (c) retail debt cascades; (d) summary content requirements for a prospectus; (e) debt issuance programmes; (f) comfort letters for schemes of arrangement and (g) issues with references to the Companies Act.

http://www.fsa.gov.uk/pubs/ukla/list_julo7.pdf

FSA Issues New Enforcement Rule Book

On July 27 the FSA issued policy statement PS07/12 and announced the results of its review of its Enforcement and Decision Making Manuals. This review formed part of the FSA's work to simplify its Handbook of Rules and promotion of "better regulation." Specifically the FSA's goal has been to make the material with respect to enforcement clearer and easier to navigate. It has deleted the current ENF (enforcement) and DEC (decision making) manuals and replaced them with a new "Decision Procedure and Penalties Manual" (DEPP) and a new "Enforcement Guide" (EG) which will not form part of the Handbook. The changes include modifications of policy and procedure and consequent developments in enforcement policy will obviously be of great interest to all regulated firms.

http://www.fsa.gov.uk/pages/Library/Policy/Policy/2007/07_12.shtml

FSA Publishes Latest Asset Management Sector Newsletter

On July 30 the FSA published issue 7 of its Asset Management Sector Newsletter.

http://www.fsa.gov.uk/pubs/newsletters/am_newsletter7.pdf

FSA Publishes Its Transaction Reporting User Pack

On July 30 the FSA published its Transaction Reporting User Pack (TRUP).

The aim of the TRUP is to give detailed instructions and guidelines to help firms prepare for the new transaction reporting requirements contained in Chapter 17 of its SUP sourcebook following the implementation of the EU Markets in Financial Instruments Directive (MiFID) on November 1, 2007.

<http://www.fsa.gov.uk/pubs/other/trup.pdf>

FSA Confirms Position on Soft Commissions

In PS07/14 released on July 30 the FSA confirmed that, although its current rules on the use of dealing commission by investment managers are more stringent than the provisions on inducements contained in MiFID, its rules (currently at COB 7.18 of the FSA's Handbook) will be carried forward into the new FSA rulebook at COBS 11.6 substantially unchanged.

http://www.fsa.gov.uk/pubs/policy/ps07_14.pdf

EU Developments

Undertakings for Collective Investment in Transferable Securities Amending Directive Announced

An amending directive was published on July 10, dealing with consequential amendments as a result of the EU's adoption of a new "comitology" procedure in 2006. The new procedure increases the European Parliament's rights of oversight of implementing measures and gives the European Parliament the right to exercise scrutiny of draft implementing measures, and also extends the grounds on which the European Parliament may oppose a draft measure or may propose amendments.

<http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P6-TA-2007-0299+o+DOC+XML+Vo//EN&language=EN>

Questionnaire on Rating of Structured Finance Instruments Published

On June 22, the European Committee of European Securities Regulators (CESR) published a questionnaire on the rating of structured finance instruments as part of CESR's review of the extent that credit ratings agencies are applying the International Organization of Securities Commissions (IOSCO) Code of Conduct Fundamentals for Credit Rating Agencies. CESR has previously advised the European Commission not to formally regulate credit rating agencies.

The deadline for comments is July 31.

<http://www.cesr-eu.org/popup2.php?id=4675>

Commission Steps Up Pressure on Member States to Implement MiFID

On June 27, the European Commission formally requested 24 EU Member States to write MiFID into national law within two months. The deadline for this was January 31, 2007, but only the UK met that date and only Ireland and Romania have joined the UK since January in fully transposing MiFID into national law. The transposition deadline was intended to give the EU financial services firms affected by MiFID provisions nine months prior to November 1, 2007, when MiFID comes into effect, to make the necessary changes to systems, documents and procedures.

The European Commission has previously sent letters to these Member States seeking explanations for the delays in MiFID implementation. The formal requests are part of the second stage of the EU's infringement procedure. If there is no satisfactory reply within two months, the European Commission can refer the matter to the European Court of Justice.

<http://www.europa.eu/rapid/pressReleasesAction.do?reference=IP/07/911&format=HTML&aged=o&language=EN&guiLanguage=en>

CESR Gives Guidance on Implementing MAD

On July 16, CESR published more guidance on the EU Market Abuse Directive (MAD). The guidance includes clarifications on what constitutes inside information, where delays to disclosure of inside information are permissible, insider lists and in what circumstances information relating to a pending orders may constitute inside information.

http://www.cesr-eu.org/index.php?page=home_details&id=225

CEBS Approves International Financial Reporting Amendments

On July 25, the Committee of European Banking Supervisors (CEBS) approved amendments to its Guidelines on Financial Reporting, which provides guidance on international financial reporting standards.

The current Guidelines were released in December 2006 and are part of CEBS's ongoing efforts to streamline financial reporting requirements in the European Union.

<http://www.c-eps.org/press/24072007CPo6rev.htm1.htm>

CESR Produces Guidelines on Use of Hedge Fund Indices by UCITS Funds

On July 18, CESR adopted its final guidelines for the classification of hedge fund indices for the purposes of the EU UCITS III Directive (the Third EU Directive on Undertakings for Collective Investment in Transferable Securities).

CESR have now confirmed that hedge fund indices are eligible to be included in UCITS portfolios, subject to certain conditions. The guidelines were a response to uncertainty over whether hedge fund indices could be classified as "financial indices", as defined in UCITS III, which sets out what financial instruments a UCITS fund may invest in.

The guidelines require funds to perform additional due diligence before investing in a hedge fund index. In particular, when assessing an index's quality, the fund must take into account, as a minimum of matters addressed in the guidelines.

http://www.cesr-eu.org/index.php?page=home_details&id=227

CESR Sets out Market Abuse Priorities

On July 26, the Committee of European Securities Regulators (CESR) published its work programme for further work in the area of differing sanctions that apply across Europe under the EU Market Abuse Directive (MAD). As part of a raft of work on the MAD, CESR has identified a number of areas that could facilitate the convergent application of the directive.

CESR intends to look at such areas as the harmonisation of insider lists and the definition of inside information, including further guidance on the definition of insider information with particular regard to commodity derivatives, as well as issues surrounding suspicious transaction reports.

http://www.cesr-eu.org/index.php?page=home_details&id=229

Offshore Developments

BVI Announces Bearer Share Transition Relief

On July 3, the British Virgin Islands (BVI) Business Companies Act was changed by Executive Order to exempt BVI companies, incorporated before 2005, which still have the power to issue bearer shares in their Memorandum & Articles of Association, from payment of higher government fees.

The Executive Order giving effect to the change provides that the Memorandum & Articles of Association of every International Business Company (IBC) formed prior to 2005 shall be deemed to prohibit the issuance of bearer shares from December 31, 2009 unless the company elects that the deeming provision should not apply to it.

http://www.offshore-inc.com/content/attachment/NA_117_Press%20Release.pdf

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