



## London Update

### UK Financial Services Regulatory Developments

September/October 2007

*This edition of London Update covers UK and EU developments from July 27 through September 30.*

#### UK Developments

##### **FSA Issues New Enforcement Rule Book**

On July 27, the Financial Services Authority (FSA) issued Policy Statement PS07/12 announcing the results of its review of its Enforcement (ENF) and Decision Making (DEC) manuals. This review formed part of the FSA's work to simplify its Handbook of Rules and promote "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 and DEC 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.

[www.fsa.gov.uk/pages/Library/Policy/Policy/2007/07\\_12.shtml](http://www.fsa.gov.uk/pages/Library/Policy/Policy/2007/07_12.shtml)

##### **UK House of Commons Treasury Select Committee Reports on Private Equity**

On July 30, the Treasury Select Committee of the House of Commons published a report following its hearings on the UK private equity industry. In its report, the Committee recommended that the tax regime in respect of debt versus equity arrangements should be reviewed, particularly the treatment of carried interests and the application of residence and domicile rules. The Committee also called for a clarification from the Government on the application of the UK's Transfer of Undertakings (Protection of Employment) Regulations to take-overs and the continued monitoring of the risks posed by high leverage and the use of covenant-lite loans.

The Committee's report strongly supports the work of Sir David Walker's group on a code of conduct for the UK private equity industry (see London Update August 2007) and the work of the FSA on market abuse and the prevention of conflicts of interest.

[www.publications.parliament.uk/pa/cm200607/cmselect/cmtreasy/567/567o2.htm](http://www.publications.parliament.uk/pa/cm200607/cmselect/cmtreasy/567/567o2.htm)

##### **Tax Payers Entitled to Compound Interest When Tax Paid in Error**

In a landmark judgment handed down on July 18 (published on August 6) the UK's highest appeal court, the House of Lords, held that compound interest is recoverable in claims for restitution. The Court found that the Inland Revenue (now HM Revenue and Customs) had been unjustly enriched by the mistaken payment to it by Sempra Metals Limited (Sempra) of corporation tax when the tax had been levied prematurely. The House of Lords observed that the restrictive rule against recovery of compound interest was out of step with present day economic reality. It is expected that English courts will in future enable successful claimants to recover compound interest in a wider variety of circumstances.

[www.publications.parliament.uk/pa/ld200607/ldjudgmt/jdo70718/sempra.pdf](http://www.publications.parliament.uk/pa/ld200607/ldjudgmt/jdo70718/sempra.pdf)

##### **FSA Publishes Additional Feedback on MiFID Best Execution**

On August 8, the FSA published additional feedback on best execution issues arising under the EU Markets in Financial Instruments Directive (MiFID) that it had not addressed in its previous guidance and also on issues arising from the publication of the Committee of European Securities Regulators (CESR) questions and answer document on MiFID's best execution requirements.

The FSA document addresses such matters as requirements for client consent, establishing contractual rights in addition to the regulatory obligation to give best execution, the availability of data for over-the-counter markets, requirements for execution, and transmission policies. The feedback also clarifies the FSA's position on the application of best execution in respect of quote-driven markets, corporate finance, venture capital and securities lending.

[www.fsa.gov.uk/pubs/policy/pso7\\_15.pdf](http://www.fsa.gov.uk/pubs/policy/pso7_15.pdf)

### **LSE Specialist Fund Market Guidelines Published**

On August 8, the London Stock Exchange (LSE) published guidance for new funds which apply for admission to its recently announced Specialist Fund Market (see London Update August 2007). Among the matters covered are: the Market's regulatory status; eligibility for admission; guidance on the admission process (including material on transferring from the LSE's Main Market or from AIM and grounds for refusing admission); regulatory considerations; the trading system and powers to suspend trading.

[www.londonstockexchange.com/NR/rdonlyres/1B426275-F9FB-4D15-A5A475F9D4FEAB1E/o/SpecialistFundMarketGuidanceforadmission.pdf](http://www.londonstockexchange.com/NR/rdonlyres/1B426275-F9FB-4D15-A5A475F9D4FEAB1E/o/SpecialistFundMarketGuidanceforadmission.pdf)

### **FSA Confirms MiFID Connect Guidance on Suitability Checks and Investment Research Requirements**

On August 10 and August 21 respectively, the industry working group, MiFID Connect, announced that it had received FSA confirmation of its guidance on meeting MiFID's suitability and appropriateness provisions and on the application of MiFID's investment research requirements.

The guidelines on suitability set out considerations for assessing whether advice-based investment services are suitable for customers and whether other services provided may be appropriate under the FSA rules implementing MiFID in the UK.

The guidelines on investment research are based on existing guidance first published in February 2004 and May 2004 and seek to address only those areas relating to the regulation of investment research covered by MiFID.

[www.mifidconnect.org/content/1/c6/01/02/52/Investment\\_Research\\_Guideline.pdf](http://www.mifidconnect.org/content/1/c6/01/02/52/Investment_Research_Guideline.pdf)  
[www.mifidconnect.org/content/1/c6/01/02/00/suitability\\_guideline\\_100807.pdf](http://www.mifidconnect.org/content/1/c6/01/02/00/suitability_guideline_100807.pdf)

### **Access to Shareholder Information**

On August 22, the Association of Investment Companies (AIC) published guidance for investment companies on the issues raised by sections 116 to 119 of the Companies Act 2006, which introduce new requirements to allow public access to shareholder information.

The AIC guidance explores how shareholders' personal details can be obtained from a company, including requests to inspect or copy the register of members and for the purpose for which certain shareholder information is to be used. The AIC is the trade organisation for the closed-ended investment company industry and was formerly known as the Association of Investment Trust Companies (AITC).

[www.theaic.co.uk/files/technical/FINALPublicaccesstoshareholderinformation.pdf](http://www.theaic.co.uk/files/technical/FINALPublicaccesstoshareholderinformation.pdf)

### **Industry Guidance to Play a Key Role in FSA Regulation**

On September 4, the FSA issued Policy Statement 07/16, *FSA Confirmation of Industry Guidance*, which introduced a new framework for recognising industry guidance as part of the FSA's continued steps towards more Principles-Based Regulation.

Any guidance that is created by trade associations, professional bodies or firms can now be submitted to the FSA for formal recognition provided that such guidance conforms with certain criteria. FSA-recognised industry guidance will supplement the FSA's rules, not replace them. There is no obligation on industry bodies to provide guidance and the development of guidance is at their discretion.

The FSA has confirmed three sets of industry guidance on Outsourcing, Suitability and Appropriateness, and Investment Research prepared by the industry group MiFID Connect, which is preparing guidance on various aspects of MiFID. (See above and also London Update June 2007).

The Policy Statement confirms that the FSA will not take action against a firm which has complied with FSA-recognised guidance.

[www.fsa.gov.uk/pubs/policy/ps07\\_16.pdf](http://www.fsa.gov.uk/pubs/policy/ps07_16.pdf)

### **FSA Updates MiFID Guidance**

On September 10, the FSA published an update to its MiFID Permissions and Notifications Guide, which was first published in May 2007.

The update includes: (i) clarification on the position of financial advisers wishing to opt-out of MiFID's Article 3 exemption so as to obtain EU passporting rights; (ii) updates on the transitional provisions for client categorisation and passport notifications relating to firms that wish to passport into the UK; (iii) additional material on tied agents; (iv) client categorisation issues relating to Multilateral Trading Facilities (MTFs); and (v) issues relating to Approved Persons that arise from changes to certain FSA controlled functions.

[www.fsa.gov.uk/pubs/international/mifid\\_update.pdf](http://www.fsa.gov.uk/pubs/international/mifid_update.pdf)

### **MiFID Connect Publishes Information Memorandum on Conflicts of Interest Obligations**

On September 13, the industry group, MiFID Connect, published an information memorandum on the conflicts of interest requirements that will be imposed by the FSA from November 1. These requirements are to be created as part of the UK implementation of MiFID and the Capital Requirements Directive (CRD).

The guidance focuses on aspects of the FSA's Senior Management Arrangements, Systems and Controls sourcebook (SYSC), and includes suggested measures and commentaries to assist firms in implementing processes and procedures to enable them to identify and manage conflicts of interest.

The information memorandum has not been formally recognised by the FSA.

[www.mifidconnect.org/content/1/c6/01/06/90/conflicts\\_of\\_interest\\_memo.pdf](http://www.mifidconnect.org/content/1/c6/01/06/90/conflicts_of_interest_memo.pdf)

## EU Developments

### **CESR Publishes Advice on Non-equities Transparency and Reports on Commodity and Exotic Derivatives**

On August 9, the Committee of European Securities Regulators (CESR) published a document responding to requests from the European Commission for technical advice on non-equities transparency. CESR has concluded, in co-operation with different market participants, that it has not recognised evident market failure in relation to market transparency which would warrant mandatory transparency for bonds and that some re-distribution of the existing transparency information could be useful to help retail participants.

CESR has also published an initial fact-finding exercise on the regulation and operation of commodity and exotic derivatives in EU Member States in response to the European Commission's request for a compilation of responses from CESR.

[www.cesr-eu.org/index.php?page=home\\_details&id=231](http://www.cesr-eu.org/index.php?page=home_details&id=231)

### **CESR Publishes Industry Responses to its Request for Information on Structured Finance Instrument Ratings**

On August 24, CESR published the responses it had received to its questionnaire on the functioning of the rating of structured finance instruments, which was first published on June 22.

The questionnaire is part of CESR's initiative to gather information from credit rating agencies and other interested parties in order to investigate the scope for potential conflicts where there may not be a clear separation between the rating services provided and ancillary services that are provided by credit rating agencies.

[www.cesr-eu.org/index.php?page=home\\_details&id=232](http://www.cesr-eu.org/index.php?page=home_details&id=232)

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