pwc

Yujin Baskett and Philippe Marie, Markets
Financial Conduct Authority
25 The North Colonnade
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London E14 5HS

2 April 2015

Dear Yujin and Philippe

Response to chapter 2 of CP 15/8: Quarterly Consultation no 8

Thank you for the opportunity to respond to this consultation paper. This letter outlines the view of PricewaterhouseCoopers LLP, the UK member firm of the PwC network. It covers those matters which are most relevant to us.

We have extensive experience in interpreting and applying the CASS rules, both as auditor and adviser. We believe that clarity and consistency are key to enabling firms to comply with the rules and to providing a level playing field for both regulated firms and auditors. Historically we have been aware of many instances where regulatory or industry interpretations of the CASS rules have not been aligned with the rules as they are written. So we very much welcome the proposed change to the DvP exemption for regulated collective investment schemes. This would bring the rules in line with the policy intent, set out in PS 14/9, that "the final rules do not prohibit AFMs from transferring client money from a client bank account and into a firm account before making a payment to a third party".

The proposed changes to CONC 12.1.4R extend the scope of CASS, the CMAR and CF10A to loan-based crowdfunding firms with interim permission. We are aware that you have already advised some firms with interim permissions that they are required to apply CASS and SUP in this way. So, in principle, we agree that these supervisory expectations should be communicated as rules which are available to and apply to all relevant firms. But many investment firms find compliance with these rules to be burdensome and costly. We do not agree that firms will not incur additional costs as a result of having to apply these rules before full authorisation.

Finally, we find the policy thinking behind exempting firms who delegate custody from applying CASS 6.2.3R to be unclear. We feel that such an exclusion is likely to have undesirable outcomes and could be used as a means of avoidance.

We have given further comment on these matters in the attached appendix. If you would like to discuss our comments and views, please contact either Mike Newman on 020 7212 5201 or Laura Cox on 020 7212 1579.

Yours faithfully

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Appendix 1: Answers to specific questions

Q2:2: Do you agree with our proposal relating to registration and recording of legal title to client assets?

No. We do not believe that firms which delegate custody should benefit from a blanket exclusion from CASS 6.2.3.R.

We recognise that the chain of custody can be complex and firms can find it hard to identify what name securities are ultimately registered in. But we note that:

- CASS 6.3.4BG requires written custody agreements to note the arrangements for registration or recording of assets
- CMAR field 25 requires CASS medium and large firms to disclose the way in which assets are registered
- CASS 6.2.3R (2)(d) specifically applies to firms depositing safe custody assets with custodians.

You have not proposed any amendments to these requirements in the consultation.

If your intent is to recognise that firms may struggle to obtain clear data around registration where custody is delegated, we believe that principle 10 would be better served in this context if the rules:

- specifically required firms to exercise all due skill, care and diligence to ensure that delegated custodians register assets in accordance with CASS 6.2.3R
- required firms to obtain evidence that custodians have complied with this requirement as part of their annual due diligence.

Q2:4: Do you agree with our proposal relating to the DvP rules for regulated collective investment schemes?

Yes. We agree that the rules should be aligned to the policy intent set out in PS 14/9.

We believe that the proposed rules, as drafted, are capable of differing interpretations. We suggest that you clarify the final rules to define an "immediate payment". Given industry practice and the practical constraints around banking systems, we suggest that the rules require firms to make an onward payment from the corporate account to a third party on the same business day as the transfer from the client money account takes place.

We note that firms face similar difficulties in complying with the DvP exemption for commercial settlement systems. CASS 7.2.8AAR (2) states that firms must stop using this exemption *for the transaction* if it does not settle by the third business day after the firm starts using the exemption. A strict reading of this would mean that firms would not be able to re-use the DvP exemption when the transaction finally settles – so in practice, this would mean firms were not able to route the money in respect of the transaction through an account held at a commercial settlement system (which is typically a house account). We expect that this would be burdensome and difficult to comply with. So we suggest that you amend CASS 7.2.8AAR / CASS 7.11.14R with similar wording to that proposed relating to the amendment for regulated collective investment schemes.

Finally, we believe that there continues to be a great deal of technical concern and cost incurred in the fund management industry in interpreting the 'new' DvP exemption for regulated collective investment schemes. In general, our clients have interpreted the new rules as requiring segregation of client money from at least T+1 until fund settlement – generally but not always on the settlement date. In many cases, this interpretation has necessitated major system changes and significant investment by firms, and may potentially result in a loss of liquidity. We understand that whether or not funds are due and payable to the AFM (and therefore not client money) is ultimately down to the business model of each firm. In our experience, authorised fund manager business models are largely homogenous and settlement cycles and practices are mainly operated by the major transfer agents. We believe it would be beneficial to the fund management industry if you articulated your expectations around how client money should be segregated under CASS 7.11.21R, given the generally homogenous business model for authorised fund managers and given typical practice around, for example, when clients are entered into the fund's register.

Q2.6: Do you agree with our proposals to ensure that CASS applies as stated in PS 14/4

Yes. We agree that the rules should be clear and consistent with your supervisory expectations. We are aware that some loan-based crowdfunding firms have received written guidance from FCA staff advising them that CASS, CF10A and CMAR applies. So we believe that codifying this will provide consistency and a level playing field for crowdfunding firms as a whole and their clients.

However, we note that in your cost-benefit analysis you state that you do not expect firms to incur additional costs as a result of applying these rules before full authorisation. We do not concur with this analysis. In our experience, investment firms incurred costs in implementing the CF10A and CMAR requirements and for larger and more complex firms there are significant on-going costs around the reporting framework. Bringing loan-based crowdfunding firms under SUP may also bring them into the scope of the CASS assurance report to the FCA, and therefore the costs of appointing a CASS auditor, although we note that currently there is no category under SUP 3.1.2R into which most loan-based crowdfunding firms would fall.