


Handbook Notice No.51

January 2018

Contents

1.	<u>Overview</u>	<u>2</u>
2.	<u>Summary of changes</u>	<u>4</u>
3.	<u>Consultation feedback</u>	<u>6</u>
4.	<u>Additional information</u>	<u>10</u>

How to navigate this document onscreen

 returns you to the contents list



1 Overview

Legislative changes

- 1.1 On 7 December 2017, the Board of the Financial Conduct Authority pre-approved the making and amending of voluntary jurisdiction rules and the fixing and variation of standard terms as proposed by the Financial Ombudsman Service in the below instruments. The Board of the Financial Ombudsman Service made these changes on 12 December 2017.

CP	Title of instrument	Instrument No.	Changes effective
<u>CP</u>	Dispute Resolution: MiFID 2 Complaints (Voluntary Jurisdiction) (Financial Ombudsman Service) Instrument 2017	FOS 2017/6	3.1.18
<u>CP</u>	Advising on Investments (Article 53(1) of the Regulated Activities Order) (Consequential Amendments) (Financial Ombudsman Service) Instrument 2017	FOS 2017/7	3.1.18

- 1.2 On 7 December 2017, the FCA board made the relevant changes to the Handbook as set out in the below instrument and also pre-approved the changes proposed by the Financial Ombudsman Service. On 12 December 2017, the Board of the Financial Ombudsman Service Ltd made the relevant changes to the Handbook in the instrument listed below.

CP	Title of instrument	Instrument No.	Changes effective
<u>16/34;</u> <u>17/3</u>	Risk Transformation Regulations 2017 (Consequential Amendments) Instrument 2017	FCA 2017/81; FOS 2017/8	13.12.17; (3.1.18 for SYSC 1 Annex 1 3.2ER)

- 1.3 On 3 January 2018, the Board of the Financial Conduct Authority made changes to the Handbook in the instrument listed below.

CP	Title of instrument	Instrument No.	Changes effective
<u>17/32</u>	Enforcement (Packaged Retail and Insurance-based Investment Products Regulations 2017) Instrument 2018	2018/1	4.1.18

- 1.4 On 18 January 2018, the Board of the Financial Conduct Authority made the relevant changes to the Handbook as set out in the instruments listed below.



CP	Title of instrument	Instrument No.	Changes effective
17/32	Conduct of Business Sourcebook (Projections) (Amendment No 2) Instrument 2018	2018/2	6.4.19
17/29	Client Assets (Term Deposits) Instrument 2018	2018/3	22.1.18

Summary of changes

- 1.5 The legislative changes referred to above are listed and briefly described in Chapter 2 of this Notice.

Feedback on responses to consultations

- 1.6 Consultation feedback is published in Chapter 3 of this Notice or in a separate Policy Statement.

FCA Board dates for 2018

- 1.7 The table below lists forthcoming FCA board meetings. These dates are subject to change without prior notice.

February	22
March	22
April	26
May	24
June	28
July	26
September	27
October	25
November	15
December	13



2 Summary of changes

- 2.1 This Handbook Notice describes the changes to the Handbook and other material made by the Financial Conduct Authority (FCA) Board under its legislative and other statutory powers on 7 December 2017, 3 January 2018 and 18 January 2018. It additionally describes changes made by the Board of the Financial Ombudsman Service to its rules, guidance and standard terms for VJ participants on 12 December 2017. Where relevant, it also refers to the development stages of that material, enabling readers to look back at developmental documents if they wish. For information on changes made by the Prudential Regulation Authority (PRA) please see www.bankofengland.co.uk/pru/Pages/publications/default.aspx

Risk Transformation Regulations 2017 (Consequential Amendments) Instrument 2017 (FCA 2017/81)(FOS 2017/8)

- 2.2 Following consultation in CP16/34¹ and CP17/3², the FCA Board has made changes to the FCA Handbook sections listed below:

Glossary
PRIN 1 and 3
SYSC 1, 3, 12 and 14
FEES 3 and 4
SUP 11
DEPP 2
DISP 2

- 2.3 It also adds a new section to COBS, **COBS 18.6A**.
- 2.4 In summary this instrument makes changes to the Handbook required to incorporate the new regulated activity of insurance risk transformation.
- 2.5 This instrument came into force on **13 December 2017**, except for SYSC 1 Annex 1 3.2ER which came into force on **3 January 2018**. Feedback was published in PS17/24³.

Enforcement (Packaged Retail and Insurance-based Investment Products Regulations 2017) Instrument 2018 (FCA 2018/1)

1 CP16/34 'Authorisation and supervision of insurance special purpose vehicles' (November 2016)
2 CP17/3 'Proposed Handbook changes to reflect the new regulatory framework for Insurance Linked Securities' (January 2017)
3 PS17/24 'Handbook changes to reflect the new regulatory framework for Insurance-Linked Securities – Feedback to CP16/34 and CP17/3 near-final rules' (November 2017)



- 2.6 Following consultation in CP17/32⁴, the FCA Board has made changes to the FCA Handbook section listed below:

DEPP 2

- 2.7 It also makes changes to **EG 19**.
- 2.8 In summary this instrument provides guidance on the use of our enforcement powers and sets out a decision-making mechanism for the use of these new powers. It inserts a new section into Chapter 19 of EG to deal with how we will exercise our powers under the Packaged Retail and Insurance-based Investment Products (PRIIPs) Regulation.
- 2.9 This instrument came into force on **4 January 2018**. Feedback is published in Chapter 3 of this Notice.

Conduct of Business Sourcebook (Projections) (Amendment No 2) Instrument 2018 (FCA 2018/2)

- 2.10 Following consultation in CP17/32⁵, the FCA Board has made changes to the FCA Handbook section listed below:

COBS 13 and 19

- 2.11 In summary this instrument makes changes to the Handbook to ensure that consumers continue to receive information which reflects the current economic outlook.
- 2.12 This instrument comes into force on **6 April 2019**. Feedback is published in Chapter 3 of this Notice.

Client Assets (Term Deposits) Instrument 2018 (FCA 2018/3)

- 2.13 Following consultation in CP17/29⁶, the FCA Board has made changes to the FCA Handbook sections listed below:

**CASS 7, 10, TP 1 and Sch 1
SUP 16 and TP 1**

- 2.14 In summary this instrument makes changes to the Handbook to provide appropriate relief for investment firms who are facing decreasing appetite by UK banks for holding client money and to ensure consumers continue to be appropriately protected by firms holding their client money.

4 [CP17/32 'Quarterly Consultation Paper No 18' \(September 2017\)](#)

5 [CP17/32 'Quarterly Consultation Paper No. 18' \(September 2017\)](#)

6 [CP17/29 'Client money and unbreakable deposits' \(August 2017\)](#)



- 2.15 This instrument comes into force on **22 January 2018**. Feedback will be published in a separate Policy Statement.

3 Consultation feedback

- 3.1 This chapter provides feedback on consultations that will not have a separate Policy Statement published by the FCA.

CP17/32: Quarterly Consultation Paper No 18 – Chapter 3

Enforcement (Packaged Retail and Insurance-Based Investment Products Regulations 2017) Instrument 2018 (FCA 2018/1)

Background

- 3.2 On 5 December 2017 the regulations transposing the Packaged Retail and Insurance-based Investment Products Regulation (PRIIPs Regulation) – Packaged Retail and Insurance-based Investment Products Regulations 2017 (PRIIPs Statutory Instrument (SI)) – were laid before Parliament.
- 3.3 In Quarterly Consultation Paper (QCP) 17/32⁷ we proposed to apply our existing policy and procedure to the exercise of our enforcement powers under the PRIIPs SI and amend the Decision Procedure and Penalties manual and Enforcement Guide accordingly.
- 3.4 Our consultation was based on a non-public draft of the PRIIPs SI. The published SI does not materially change from the version we consulted on. We therefore do not need to change the instrument and we are finalising the rules as consulted on.

Feedback

- 3.5 We received no feedback.

Our response

- 3.6 No response is required as no feedback was received.

Cost benefit analysis and compatibility statement

- 3.7 The cost benefit analysis and compatibility statement in our Quarterly Consultation Paper No 18, Chapter 3, remain unchanged.

⁷ [CP17/32 Quarterly Consultation Paper No 18 \(September 2017\)](#)



Equality and diversity issues

- 3.8 We continue to believe the changes do not give rise to discrimination as stated in our Quarterly Consultation Paper No 18, Chapter 3.
- 3.9 The changes made by this instrument are listed in Chapter 2 of this Notice.

CP17/32: Quarterly Consultation Paper No 18 – Chapter 7

Conduct of Business Sourcebook (Projections)(Amendment No 2) Instrument 2018

Background

- 3.10 Our projections rules aim to protect consumers from harm by giving them illustrative, comparable information about the upside potential and downside risks of investment products by showing a range of possible returns. In conjunction with our requirements on charges disclosure, they also help show the effect of charges. Projections are not a guarantee of future returns.
- 3.11 Our COBS 13 projections regime specifies how firms should prepare investment projections for packaged products, including personal pension schemes. The rules require firms to prepare and provide a key features illustration (KFI). KFIs include 'standardised deterministic projections'. The rules in COBS 13 set out the maximum rate of return, inflation rate and relevant tax effects that firms should use when projecting investment returns. Firms also use these set economic assumptions when assessing the value of transferred safeguarded pensions benefits (COBS 19.1).
- 3.12 The FCA (and previously the Financial Services Authority) periodically reviews and updates these assumptions. In Policy Statement (PS) 16/12⁸ (April 2016) we committed to starting research during 2016 to inform a review of the assumptions that were established by the last review in 2012. But we suspended the research due to the economic uncertainty following the EU referendum and did not recommence it until early 2017.
- 3.13 In 2017, we re-assessed the historical and anticipated future returns on key asset classes and key economic variables, such as gross domestic product (GDP) growth, earnings and inflation. The summary of this assessment was published in 2017 in our Rates of return for FCA prescribed projections report⁹ (the Report) alongside our proposals to

8 [PS16/12 'Pension reforms – feedback on CP15/30 and final rules and guidance' \(April 2016\)](#)

9 [Rates of return for FCA prescribed projections \(September 2017\)](#)



update the economic assumptions that underpin the projections which firms must produce. In a departure from previous reviews, the Report was produced in-house by the FCA's Economics Department, rather than by an external provider. However, in order to preserve the rigour and impartiality of the analysis, we broadly followed the methodology developed by PricewaterhouseCoopers (PwC) for the 2012 review. Any changes to the methodology or data sources were agreed with our three independent peer reviewers, who also reviewed the final report and supported its findings.

3.14 In Quarterly Consultation Paper (QCP) 17/32,¹⁰ we consulted on updating our economic assumptions in line with the findings of the Report. We proposed to:

- keep the cap on the nominal intermediate rate of return for tax-exempt business at 5% and for all other products at 4.5% (the 50 basis points deduction simply reflects the impact of taxation)
- keep the current 'lower' and 'higher' flanking rates used to illustrate potential variability around the intermediate rate of return at + or - 3%
- base our price inflation assumption on the consumer price index (CPI), rather than the retail prices index (RPI), which will reduce the price inflation rate from 2.5% to 2%
- continue to use an RPI assumption for use by firms where contributions benefits or charges are linked to that index, and
- reduce the assumption for earnings inflation from 4% to 3.5%.

Feedback

3.15 We received responses from five firms, two professional bodies and one individual. Most respondents agreed with most of our proposals. One respondent proposed a lower RPI-based inflation rate, while another considered that the assumptions used for FCA projections and Department for Work and Pensions (DWP) Statutory Money Purchase Illustrations (SMPIs) should be consistent.

3.16 Three major investment management firms had concerns about our proposal to keep the maximum nominal intermediate rate of return, in rule 2.3 of Annex 2 to COBS 13, at 5% for tax-exempt products. Essentially, their concern was whether it is appropriate to impose a cap based on an averagely weighted portfolio, when many portfolios do not resemble an average portfolio. In particular, they argued that the proposed average cap does not allow a true demonstration of the returns that can be achieved through pure equity, or heavily equity-

¹⁰ [CP17/32 'Quarterly Consultation No 18' \(September 2017\)](#)

weighted portfolios. They suggested that we could adopt separate caps for different asset classes.

3.17 The Institute and Faculty of Actuaries (IFoA) made a different proposal in relation to the cap. It commented that the proposed cap on the nominal intermediate rate of 5% was too high because, in combination with the use of a lower inflation measure, it would effectively increase real returns. Instead, the IFoA recommended that, in view of the current financial climate, the rate should be reduced to 4.5%.

3.18 After the consultation period closed, we received a separate communication from one major insurer indicating that the proposed amendments to projection rates is likely to necessitate additional IT work. They requested that the proposals should come into force later than the proposed date of 1 August 2018 to allow more time for systems implementation.

Our response

3.19 We propose to proceed with our substantive proposals as set out in QCP 17/32, Chapter 7. The only change which we now propose is to extend the implementation date such that the rules come into force on 6 April 2019. This is to align with consistent changes to the projection rates used in the calculation of Statutory Money Purchase Illustrations which are being proposed by the Financial Reporting Council.

3.20 We note the points made in response to our consultation, to the effect that returns of individual portfolios are unlikely to mirror those of an averagely weighted portfolio. We are aware of this issue and noted this as a risk when seeking approval of the proposals for consultation. Our aim, in this consultation, however, was to update the existing cap.

3.21 Introduction of separate caps for different classes of assets would require further research – which we have not conducted – in relation to various, non-standard individual assets classes (in respect of which there is a lack of robust data). The different ways in which the flanking rates would have to be amended for those different assets would also have to be researched. We are therefore not presently in a position to consider changing the way we set the cap.

3.22 We also note the concerns raised by the IFoA that the proposed cap rates of 5% and 4.5% are too high. But we consider that these concerns arise from our proposal – supported by the IFoA – to base our price inflation assumption on the CPI, rather than the RPI. CPI is now considered to be a better measure of inflation in the economy. One key feature of CPI is that it systematically shows a lower rate of inflation than RPI. Put another way, RPI tended to overstate inflation. The apparent increase in real returns – which is supported by our research – is therefore due to the change of inflation measure and not to us taking a less prudent approach.



Cost benefit analysis and compatibility statement

- 3.23 Our view remains as set out in the QCP, namely that we consider our proposals will result in only minimal costs for firms. This is not the first time we have changed our assumptions and providers should therefore already have the capacity to change their systems and processes in response to our proposed updates.

Equality and diversity issues

- 3.24 We invited feedback on equality and diversity issues but did not receive any. We remain of the view set out in the QCP that we do not consider that the proposals adversely impact any of the groups with protected characteristics i.e. age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment.
- 3.25 The changes made by this instrument are listed in Chapter 2 of this Notice.

4 Additional information

Making corrections

- 4.1 The FCA reserves the right to make correctional or clarificatory amendments to the instruments made at the Board meeting without further consultation should this prove necessary or desirable.

Publication of Handbook material

- 4.2 This Notice is published on the FCA website and is available in hardcopy.
- 4.3 The formal legal instruments (which contain details of the changes) can be found on the FCA's website listed by date, reference number or module at www.handbook.fca.org.uk/instrument. The definitive version of the Handbook at any time is the version contained in the legal instruments.
- 4.4 The changes to the Handbook are incorporated in the consolidated Handbook text on the website as soon as practicable after the legal instruments are published.



- 4.5 The consolidated text of the Handbook can be found on the FCA's website at www.handbook.fca.org.uk/. A print version of the Handbook is available from The Stationery Office's shop at: www.tsoshop.co.uk/Financial-Conduct-Authority-FCA/.
- 4.6 Copies of the FCA's consultation papers referred to in this Notice are available on the FCA's website.

Obligation to publish feedback

- 4.7 This Notice, and the feedback to which Paragraph 1.3 refers, fulfil for the relevant text made by the Board the obligations in sections 138I(4) and (5) and similar sections of the Financial Services and Markets Act 2000 (the Act). These obligations are: to publish an account of representations received in response to consultation and the FCA's response to them; and to publish (where applicable) details of any significant differences between the provisions consulted on and the provisions made by the Board, with a cost benefit analysis and a statement under section 138K(4) of the Act if a proposed altered rule applies to authorised persons which include mutual societies.

Comments

- 4.8 We always welcome feedback on the way we present information in the Handbook Notice. If you have any suggestions, they should be sent to handbookproduction@fca.org.uk (or see contact details on the back cover).

Handbook Notice 51

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It also contains information about other publications relating to the Handbook and, if appropriate, lists minor corrections made to previous instruments made by the Board.

Contact names for the individual modules are listed in the relevant Consultation Papers and Policy Statements referred to in this Notice.

General comments and queries on the Handbook can be addressed to:

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Email: emily.how@fca.org.uk

Gabby Stephenson

Tel: 020 7066 7887

Email: gabrielle.stephenson@fca.org.uk

However, queries on specific requirements in the Handbook should be addressed first to your normal supervisory contact in the FCA. For most firms this will be the FCA's Contact Centre:

Tel: 0300 500 0597

Fax: 0207 066 0991

Email: firm.queries@fca.org.uk

Post: Contact Centre

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