

Client money and unbreakable deposits

Feedback to CP17/29 and final rules

Policy Statement

PS18/2

January 2018



This relates to

This relates to Consultation Paper 17/29, which is available on our website at www.fca.org.uk/publications.

Comments or queries can be sent to:

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1 Overview

Introduction

- 1.1** Some investment firms are experiencing increasing difficulty placing client money with banks. Industry feedback suggests that this is partly due to the combined effects of a rule in the Client Assets sourcebook (CASS) and the liquidity rules that apply to banks.
- 1.2** The client money rules (CASS 7) prevent firms from placing client money in bank accounts with unbreakable terms of longer than 30 days (30-Day Rule).¹ Banks have cited the cost of liquidity requirements associated with such 30-day money as one of the main reasons for their reduced appetite for client money. Industry feedback suggests the issue has been exacerbated by significantly increased amounts of client money and general liquidity in the banking system and low interest rates.
- 1.3** In our consultation paper CP17/29: Client money and unbreakable deposits² (CP) we proposed changes to the 30-Day Rule designed to ensure consumers continue to be appropriately protected by firms holding their client money.
- 1.4** This policy statement (PS) summarises the feedback we received to the CP and our responses and includes final rules.

Who does this affect?

- 1.5** This PS is relevant to regulated firms that hold client money in relation to investment business. The changes do not apply to client money received by a firm in its capacity as a trustee firm.
- 1.6** This PS will interest banks with whom firms deposit client money. It may also interest auditors who provide client assets audit reports.

Is this of interest to consumers?

- 1.7** The new rules will affect the protections afforded to consumers by those firms to which the rules apply and will enable consumers to make better informed decisions by receiving greater disclosures.

Context

- 1.8** CASS 7 applies to money received or held by a firm for, or on behalf of, a client in the course of, or in connection with, its MiFID business, designated investment business

¹ CASS 7.13.3R(3)

² <https://www.fca.org.uk/publication/consultation/cp17-29.pdf>



or relevant ISA business.³ Firms are required to deposit client money in an account opened with an authorised bank, a central bank or in a qualifying money market fund.⁴

1.9 In 2012, we conducted a survey in which firms reported client money holdings in three to four year unbreakable deposits (UDs). We subsequently issued a letter⁵ to firms stating our concerns and expectations on the use of lengthy UD.

1.10 To address our concerns, in July 2014⁶ we introduced the 30-Day Rule to ensure that:

- firms carry out risk assessments on the banks with which they deposit client money and are able to react to that risk assessment by withdrawing and re-locating client money if necessary, and
- client money is readily available for distribution back to clients as soon as is reasonably practicable in the event of the failure of a firm

1.11 The July paper set out our view that the use of UD with lengthy terms to hold client money is incompatible with the purpose of the client money regime.

1.12 After the 30-Day Rule came into force, we received feedback that firms are experiencing increasing difficulty depositing client money at banks, with banks citing the cost of the Liquidity Coverage Ratio (LCR) as their main reason for refusing to accept client money from firms. The LCR requires banks to have highly liquid assets to cover 100% of their potential net cash outflows over 30 days.⁷

1.13 There may be harm to consumers if a firm reaches a point where it is unable to deposit client money at a bank. This could result in client money being returned to clients rather than invested in line with the clients' instructions, including subscriptions in ISAs, or client money being deposited with banks that do not meet firms' due diligence requirements.

1.14 In the lead up to the publication of CP17/29, the FCA formed a technical working group to investigate the issue in greater detail. The group comprised a small number of firms, with each representing an industry association. Firms, banks and industry associations also independently provided us with further information. Feedback consistently suggested that permitting firms to place client money on deposits with unbreakable terms of longer than 30 days would ease the situation, as banks would regain some of their appetite to hold client money.

1.15 We worked with the Prudential Regulation Authority (PRA) on considering changes to the 30-Day Rule. In CP13/17⁸, the PRA outlined its view that a 90-day horizon is essential for properly monitoring firms' liquidity risks. The PRA proposed to monitor credit institutions' contractually due cash flows on a daily basis up to 92 days, on a monthly basis in a six-month period thereafter and more aggregated beyond that.

3 CASS 7.10.1R

4 CASS 7.13.3R

5 <https://www.fca.org.uk/publication/archive/fsa-unbreakable-term-deposits.pdf>

6 See PS14/9: Review of the Client Assets Regime for investment business, paragraphs 7.98–7.106

7 The LCR is a component of the Basel III reforms, which are global regulatory standards on bank capital adequacy and liquidity. The LCR standard has been implemented in the EU through the Commission Delegated Regulation (EU) 2015/61.

8 CP13/17 Pillar 2 liquidity (July 2017): <http://www.bankofengland.co.uk/prd/Documents/publications/cp/2017/cp1317.pdf>

1.16 As noted above, our policy position is that the use of UD's with excessively lengthy terms is not compatible with the client money regime. However, in light of the market conditions, industry feedback and our objectives of protecting consumers and ensuring market integrity, we considered a rule amendment to ensure a proportionate balance was struck between ensuring client money could be held in banks in the first place, while respecting our overall policy aims.

1.17 In CP17/29 we, therefore, proposed changes to the 30-Day Rule to allow a firm to deposit an appropriate proportion of client money in a UD of up to 90 days (90-Day UD) subject to certain conditions. Some firms have also been granted an individual modification of the 30-Day Rule to permit them to hold a proportion of client money in a UD of longer than 30 days.

Summary of feedback and our response

1.18 We received 31 written responses to the CP, including submissions from banks, firms, auditors and trade bodies. Overall, respondents were supportive of the proposals. Therefore, we have finalised the rules as consulted on, with some amendments to reflect the feedback. Descriptions of the feedback are included in this PS and the final rules that we are making are published in Appendix 1.

1.19 We would like to thank all respondents for their feedback.

Equality and diversity considerations

1.20 We have considered the equality and diversity issues that may arise from the changes in this PS.

1.21 Overall, we do not consider that the changes in this PS 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.

Next steps

What do you need to do next?

1.22 The rules set out in Appendix 1 will come into force on 22 January 2018. The rules enable firms to hold a proportion of client money in a UD longer than 30 days, subject to certain conditions.



2 Amendments affecting unbreakable deposits

- 2.1** In this chapter we summarise and respond to the feedback received to our proposed changes to CASS.

Length of unbreakable deposit

- 2.2** We consulted on permitting a firm to deposit an appropriate proportion of client money in client bank accounts with unbreakable terms or notice periods of between 31 and a maximum of 90 days.

In CP17/29 we asked:

Q1: *Do you agree with our proposal to permit firms to deposit client money in UD's of up to 90 days? If not, why not? Please provide specific examples.*

- 2.3** Nearly all respondents agreed with permitting firms to deposit client money in UD's of longer than 30 days. However, the majority requested that we permit firms to deposit client money in UD's of up to 95 days (95-Day UD's), as it would encourage a wider selection of banks and building societies to accept client money. One reason given for this was that banks and building societies' own internal policies are more stringent for 90-day deposits, making these more expensive for them to hold. Other reasons given were: 95 days aligns with banks' existing product offerings; 95-day terms allow banks to better manage deposits expiring on weekends and bank holidays; and ensuring parity with firms that have been granted an individual rule modification to permit them to hold client money in a 95-Day UD. Some respondents questioned the status of existing individual rule modifications and whether these would be superseded by the new rules.
- 2.4** A few respondents were concerned that where an operator of a self-investment personal pension (SIPP) holds client money in a UD of longer than 30 days, the firm may have to reclassify all of its assets in the SIPP under the Interim Prudential sourcebook for Investment Businesses (IPRU-INV) and be subject to higher capital requirements.⁹
- 2.5** Some respondents felt that amending the 30-Day Rule would not improve banks' appetite to take on client money in the long term because of ongoing capacity restraints and regulatory pressures. They suggested alternative solutions including using collateralised deposits, greater use of qualifying money market funds (QMMFs) and permitting client money to be deposited at the Bank of England.

⁹ Note 1 in IPRU-INV 5.9.1R states that an asset is 'standard' if it readily realised within 30 days.

Our response

We are persuaded that allowing 95-Day UD will result in a greater range of banks and building societies accepting more client money from more firms and reduce the likelihood of harm to consumers materialising. We acknowledge the benefits of ensuring 90-Day UD deposits fall within the PRA's proposed daily monitoring window for credit institutions. However, based on the feedback, we are convinced of the benefits of 95-Day UD and we understand that such deposits will still be captured in the PRA's proposed monthly reporting requirement. We have, therefore, amended the rules to permit a firm to deposit an appropriate proportion of client money in 95-Day UD.

The final rules provide a transitional provision to enable existing rule modifications on the 30-Day Rule to continue until the relevant modification ceases to have effect. Firms can also choose to terminate their modifications earlier if they wish to comply with the new rules.

The rules allow (but do not require) firms to place client money in a UD of longer than 30 days. It is therefore up to firms, including SIPPs, to ensure that they can comply with the final CASS rules and other rules, such as IPRU-INV, to which they are subject.

We note the suggested solutions on improving banks' appetite to take on client money in the longer term. The placement of client money pursuant to CASS 7 is constrained by MiFID II (and previously MiFID) requirements (see paragraph 1.8). Therefore, the ability to place client money in an arrangement outside these methods is not possible within the parameters of MiFID II. A firm is permitted to place client money in a QMMF providing it has the relevant permissions to invest in a QMMF and complies with the applicable rules. The Bank of England offers accounts to institutions that fall within a certain eligibility criteria¹⁰ and does not have any current plans to expand the criteria or the range of firms which can apply for an account.

Overall we believe our final rules strike the right balance and we are not expecting to do any further work in this area in the foreseeable future.

- 2.6** We consulted on making it clear that firms will not be in breach of the rules if the unbreakable term expires on a day the relevant bank is not open for business, provided that the firm can make the withdrawal of client money on the next day the bank is open for business.

In CP17/29 we asked:

Q2: *Do you agree with our proposal that where the expiry of a notice period falls on a day the bank is closed, provided that the firm is able to make the withdrawal on the next day that*

¹⁰ The Bank of England offers several types of accounts to various types of institutions in order to meet its objectives. This includes: reserves accounts to the firms defined in the Sterling Monetary Framework Eligibility Criteria; settlement accounts to the firms defined in the Settlement Account Policy Eligibility Criteria; and customer accounts to the UK Government, overseas central banks and certain firms where there are financial stability reasons to do so.



bank is open for business, this is not a breach of CASS 7. If not, why not? Please provide specific examples.

2.7 Most respondents agreed with this proposal, with a few noting that this was market convention. One stated that banks typically arrange their deposits to expire on a working day. However, a number suggested the proposal would be unnecessary if firms could use a 95-Day UD.

Our response

We are no longer proceeding with this proposal given the feedback that it would not be necessary if we amend the rules to permit 95-Day UDs (which we are doing). We have also introduced guidance to clarify that a firm will be in breach of the final rules if its UD expires on a weekend or bank holiday and the firm is not able to make a withdrawal until the next day the bank is open for business.

Conditions on UDs of over 30 days

2.8 We proposed that where a firm deposits client money in a UD of longer than 30 days, it must comply with certain conditions. These conditions included:

- producing a written policy setting out the maximum proportion of client money that would be appropriate for the firm to deposit in a UD longer of 30 days and the measures it will take to manage the risk of being unable to access client money when required
- taking appropriate measures to manage the risk of the firm being unable to access client money when required
- providing each client with a written explanation of the risks that arise as a result of the longer notice period for withdrawals and in a medium in accordance with the firm's disclosure obligations under COBS 6¹¹, and
- for CASS medium and large firms, reporting UDs of longer than 30 days in their client money and asset return (CMAR)¹²

In CP17/29 we asked:

Q3: ***Do you agree with our proposed conditions for firms that deposit client money in UDs of greater than 30 days? If not, why not?***

11 COBS 6.1.13R or COBS 6.1ZA.19EU as applicable to the firm in respect of its obligations to provide information to its clients. These obligations require a firm to provide the information in a durable medium or via a website (where it does not constitute a durable medium) where the website conditions are satisfied.

12 SUP 16.14

- 2.9** Most respondents agreed with this proposal.
- 2.10** Some respondents requested guidance on the proposed written explanation to clients. This included whether the explanation could be incorporated into existing client disclosures and whether the FCA could provide suggested wording for a standard notification or amendments to client agreements. A few respondents were concerned that the written explanation may unnecessarily alarm clients, with one suggesting it should also incorporate the benefits of using a UD longer than 30 days and another requesting that the FCA provide an industry-wide communication on the wider context and risks to consumers. One respondent commented that the written explanation should not be provided to clients who do not have their client money in a UD of longer than 30 days or whose accounts have no cash.
- 2.11** One respondent felt that the conditions relating to obligations under COBS 6 (medium of written explanation to clients) and SUP 16.14 (CMAR reporting) should be removed from the proposed rules in CASS 7. They felt that the inclusion of these references would increase the scope of the client assets audit report (CASS audit).
- 2.12** A few respondents queried the FCA's expectations if a firm cannot meet its written policy on using a UD longer than 30 days. One noted that it might be difficult for firms with dynamic client money balances to follow their policy.

Our response

We are introducing these provisions with some minor amendments.

The final rules require that:

- prior to a firm depositing client money in 95-Day UDs, it must provide each client with a written explanation of the risks that arise as a result of the longer notice periods for withdrawals, and
- whilst a firm uses 95-Day UDs, before receiving or holding client money from new clients, the firm must provide them with a written explanation of the risks of the longer notice periods for withdrawals

In the event of a firm failure, all client money held by the firm is pooled¹³ (including client monies held in designated client accounts) and either distributed to clients or transferred to another service provider.¹⁴ However, where client money is 'stuck' in a UD this process cannot start, potentially to the detriment of all clients expecting to share in the client money pool. This is why we believe it is important that clients understand these risks.

Firms can provide the written explanation as a standalone notification or as part of their existing disclosures, providing the explanation complies with the final rules. This includes being clear, fair and not misleading. We are not considering an industry-wide communication on the wider context and risks to consumers at this time.

¹³ This includes client money which is in a general client bank account, a designated client bank account or a designated client fund account (CASS 7A.2.4R(1)(b)(i)).

¹⁴ CASS 7A.2.4R



We have retained the condition on providing the written explanation in accordance with the firm's disclosure obligations under COBS 6, on the basis that assessing compliance with this condition is limited to the requirement to provide the written explanation itself. The scope of the CASS audit is only increased to that limited extent. We have moved the requirement to report UD's of longer than 30 days in the CMAR to the Handbook chapter containing other rules on CMAR reporting (SUP 16.14).

We note the comments on firms with dynamic client money balances and their ability to comply with their written policy. Firms should set realistic policies reflecting their circumstances and that they can adhere to. The final rules also require firms to keep their written policy under review, amending it where necessary. We remind firms that they are required to establish, implement and maintain adequate policies and procedures sufficient to ensure compliance with their regulatory obligations.¹⁵

Compliance with requirement to take 'appropriate measures'

2.13 We consulted on an evidential provision setting out how a firm can demonstrate compliance with the requirement to take appropriate measures to manage the risk of being unable to access client money when required.

In CP17/29 we asked:

Q4: *Are the provisions setting out how a firm can demonstrate compliance with the requirement to take 'appropriate measures to manage the risk of the firm being unable to access client money when required' understandable and achievable? Would it be helpful to set out more detailed requirements and guidance such as for example those found in BIPRU 12.4 for considering stress scenarios or developing a contingency funding plan?*

2.14 The majority of respondents agreed with this proposal, with a number noting that it was clear, understandable and achievable. A few respondents commented that the proposal would not be burdensome because firms already follow certain governance procedures before placing client money in a UD, manage their own liquidity risks and make sure that they maintain sufficient liquidity to meet client instructions.

2.15 A few respondents were concerned about a firm having to include a variety of 'severe yet plausible liquidity shocks' in its analysis of stress scenarios. The respondents felt this may include analysis of stress scenarios both of the banks used for client money and the firm itself, and consequently make it difficult to use UD's of longer than 30 days. They also commented that it would be hard to argue that any liquidity shock is 'implausible'.

2.16 Responses were divided on whether more detailed requirements and guidance would be helpful. There was no support for including guidance such as that found in BIRPU 12.4. However, a few respondents requested further guidance to assist audit

15 SYSC 6.1.1R

firms on assessing compliance and ensuring consistent standards. In contrast, some respondents suggested that more detailed requirements and guidance would limit a firm's flexibility to do its own analysis. They also argued firms would be best placed to undertake the analysis, as the scale of client money holdings and diversification policies vary between firms. One respondent suggested that the FCA can assess compliance of a firm managing its liquidity risks through receiving CMAR data on UDs and more detailed requirements and guidance would confuse obligations between CASS and BIPRU.

Our response

We are introducing the provisions as consulted on.

We consider it is appropriate for a firm to consider a variety of severe yet plausible liquidity shocks to manage the liquidity risks associated with using an extended UD. Many CASS investment firms are already likely to undertake similar analysis in their broader obligations under BIPRU.¹⁶ See paragraphs 2.24 to 2.27 for further details on an investment firm's general liquidity requirements. While a firm is likely to have obligations under BIPRU, the CASS rules require a firm to manage liquidity specifically when using UDs for client money and include specific measures in its UD written policy.

Written policy in CASS resolution pack

2.17 We consulted on requiring a firm to include the written policy referred to in paragraph 2.8 in its CASS resolution pack (CASS RP).

In CP17/29 we asked:

Q5: *Do you agree with our policy to require a firm to include the written policy in its CASS RP? If not, why not?*

2.18 Many respondents agreed with this proposal on the basis that it would be helpful for an insolvency practitioner (IP) and for completeness. One also noted that it would not be burdensome given they already include other policies in the CASS RP.

2.19 On the other hand, some respondents questioned whether this proposal would help the IP. One also noted that any policy on the use of UDs, if material, would form part of a firm's manual on 'procedures for the management, recording and transfer of client money' and therefore will be included in the CASS RP under CASS 10.2.1R(9).

Our response

We are introducing the provisions as consulted on.

Including the written policy in the CASS RP will enable an IP to immediately identify whether the firm places client money in UDs of longer than 30 days. Introducing this as a separate requirement will

¹⁶ BIPRU 12.1.1R(1) requires a firm to maintain adequate liquidity resources to ensure that there is no significant risk that its liabilities cannot be met as they fall due. BIPRU 12.4 also sets out requirements on analysing stress scenarios.



ensure the rules are explicit that this policy must be included in the CASS RP.

CMAR reporting

2.20 We consulted on requiring CASS medium and large firms which use UD of longer than 30 days to report these in their CMARs under section 3, data field 13. We also proposed amending the guidance to the CMAR¹⁷ (CMAR Guidance) on how these UDs should be reported by firms.

In CP17/29 we asked:

Q6: *Do you agree with our proposal to require CASS medium and large firms to report UDs in this way? If not, why not.*

2.21 Nearly all respondents supported this proposal. Although no respondents were against the proposal, some raised suggestions and concerns.

2.22 One concern was that the proposed amendments to the CMAR Guidance could be interpreted as requiring double counting of client money balances when client money was moved between banks during the reporting period. They also indicated that such reporting would conflict with the current CMAR Guidance on firms accurately reporting the amount of client money they have held in a reporting period.¹⁸

2.23 Some respondents queried whether they should report the unexpired, initial or full term of the UD in the CMAR. They also suggested that where the remaining term was less than 30 days, this did not need to be reported in the CMAR (in line with UDs permitted under the 30-Day Rule).

Our response

We are introducing these provisions with some minor amendments.

We have amended the CMAR Guidance to make it clear that firms should report any UD in use at the end of the reporting period.

We have amended the rules to make it clear that firms should report the unexpired term of a UD, where the remaining term is longer than 30 days. We believe this information will help us to supervise the use of these deposits, the term lengths and adherence to UD written policies. This data will also be useful in the event of a firm's failure.

We have also amended the CMAR Guidance on how these UDs should be reported by firms and have included a worked example as an illustration of how firms should complete data field 13.

¹⁷ SUP 16 Annex 29A

¹⁸ SUP 16 Annex 29G (13C)

BIPRU liquidity requirements for investment firms

- 2.24** Where investment firms use extended term UD's they retain an obligation to satisfy customer cash withdrawals and investment redemptions promptly (in line with the applicable contractual obligations and CASS). This involves maturity transformation, which in turn gives rise to additional liquidity risk. Maturity transformation arises from timing differences between the cash flows that represent a firm's payment obligations and the liquid resources required to meet those obligations. Liquidity, either provided from within the client money funds or from the firm's own liquid resources, may be required to meet payment obligations to clients before the term deposit resources are available to fund them.
- 2.25** We remind all firms holding client money that fall under the IFPRU regime of their liquidity risk management obligations under the BIPRU 12 liquidity rules. When assessing potential liquidity resources required from maturity transformation exposure, the amount of liquidity resources would be based on that exposure. It would not be based on the amount of client money placed on deposit within the 95-Day UD.
- 2.26** All firms to which BIPRU 12 applies must demonstrate compliance with the 'Liquidity Adequacy Rule'¹⁹. This rule calls for firms to have access to adequate liquidity resources (on their balance sheet) at all times. This is to ensure that there is no significant risk that their liabilities cannot be met as they come due. In demonstrating compliance with this rule, firms would need to have developed and implemented an appropriate and proportionate liquidity risk management framework.²⁰ This includes a firm specific liquidity risk tolerance²¹ based on its own liquidity stress testing scenarios relevant to the business model.²²
- 2.27** Further, all firms subject to BIPRU 12 are required to have a 'Contingency Funding Plan'²³ that establishes their procedures for identifying and managing a liquidity stress event, the sources of liquidity the firm has access to and how these sources will be used to meet the stressed liquidity outflows. It is for each firm subject to BIPRU 12 to be fully aware of its liquidity risk management requirements²⁴ and ensure that they are met. Firms must be able to demonstrate compliance at all times.

19 BIPRU 12.2.1R

20 BIPRU 12.3.4R, 12.3.10R

21 BIPRU 12.3.8R, 12.3.11R

22 BIPRU 12.4.-1R, 12.4.1R, 12.4.2R

23 BIPRU 12.4.10R, 12.4.11R, 12.4.13R

24 BIPRU 12.1.4R, 12.2.8R, 12.5, 12.7, and 12.9 where relevant and appropriate



3 Feedback on cost benefit analysis and compatibility statement

Cost benefit analysis

- 3.1** In CP17/29 we set out a cost benefit analysis (CBA) of our proposed rules, as required by section 138I(2)(a) of the Financial Services and Markets Act 2000. The CBA assessed the costs and benefits of each proposal and explained why we expect the incremental costs of the proposals to be of minimal significance.

In CP17/29 we asked:

Q7: *Do you have any comments on our cost benefit analysis? Please provide explanations and quantitative evidence to support your response where appropriate.*

- 3.2** We received a number of comments on the CBA. Some respondents confirmed that the CBA was realistic and plausible. However, some respondents argued that we had underestimated the cost of client disclosures in terms of postage costs and number of clients and underestimated the cost of producing the written policy in terms of governance procedures. A couple of respondents noted that the 50% client money deposit in a UD of longer than 30 days was unrealistic because client money represents inflight balances. They suggested 10% to 15% would be more realistic.
- 3.3** A few respondents noted that the reference to a firm passing 10% of interest earned on a 90-Day UD to clients was not quantified and may be considered guidance. One respondent argued that additional interest should be given either to clients or charity, because requiring interest to be allocated to clients can be expensive.

Our response

We acknowledge the feedback that the estimated cost of the client disclosures may be higher for some firms than others, given that each firm's costs are dependent on the number of clients and the type of disclosure made to each client. Our CBA reflected median costs. The final rules require a firm to provide this disclosure to clients in a durable medium²⁵ or via a website, providing certain conditions under COBS are met.²⁶ In other words, a firm is able to make the client disclosure in any form providing it meets the relevant COBS requirements. We consider this client disclosure is necessary to make all clients aware of the risks of client money being in a 95-Day UD.

25 Generally speaking, durable medium means on paper or any instrument which enables the recipient to store information addressed personally to him in a way accessible for future reference for a period of time adequate for the purposes of the information and which allows unchanged reproduction of the information stored.

26 COBS 6.1.13R or COBS 6.1ZA.19EU as applicable to the firm in respect of its obligations to provide information to clients.

We are not revising our CBA for the estimated costs for producing a written policy. This is because we had considered governance procedures as part of the original CBA and have not received significant feedback to warrant a change in this respect.

We note the feedback that firms are more likely to place 10% to 15% of client money in a UD of longer than 30 days. We are also aware of firms that place more than this amount in such deposits. We have therefore revised our CBA to reflect expected interest earnings of a firm placing between 10% to 50% of client money in a UD of longer than 30 days. We estimate the interest earnings to be between £75 to £525 for a CASS small firm; £18,000 to £126,000 for a CASS medium firm and £750,000 to £5,250,000 for a CASS large firm. See Table 1 below for further details.

In relation to any interest earned on client money, the rules are clear that where a firm is not going to pay all the interest on the client money to clients, clients must be notified of this in writing.²⁷

The changes that we have made to the instrument do not significantly differ from the consultative draft. On that basis we have not made any further amendments to our CBA as consulted on.

Table 1: Revised estimated increased interest earnings for industry

	Number of firms ²⁷	Average client money holdings (£) ²⁸	Estimated interest earnings for a firm (25-35 basis points) (£) ²⁹	Estimated interest earnings of proposal for industry as a whole (£)
CASS small	124	300,000	75-525	9,300 – 65,100
CASS medium	443	72,000,000	18,000 – 126,000	7,974,000 – 55,818,000
CASS large	29	3,000,000,000	750,000 – 5,250,000	21,750,000 – 152,250,000
Total	596	3,072,300,000	768,075 – 5,376,525	29,733,300 – 208,133,100

Compatibility statement

3.4

We consider that the compatibility statement set out in the CP still applies. We did not receive any feedback that requires us to revise the compatibility statement. Also, we consider the amendments being introduced in this PS do not require it to be revised.

²⁷ CASS 7.11.32R to CASS 7.11.33G

²⁸ Figures as at 7 June 2017 of firms holding client money.

²⁹ Figures as at 7 June 2017 of firms holding client money.

³⁰ This reflects a range between a firm depositing 10% of its client money in a UD earning interest on 25 basis points (0.25% x (10% of client money holdings)) and a firm depositing 50% of its client money in a UD earning interest on 35 basis points (0.35% x (50% of client money holdings)).



Annex 1

List of non-confidential respondents

AJ Bell Securities Limited

Association of Member-Directed Pension Schemes (AMPS)

Aviva UK Life

Brewin Dolphin Limited

Building Societies Association

Charles Stanley & Co. Limited

Elevate Portfolio Services Limited

Equiniti Financial Services Limited

IG Markets Limited

Integrated Financial Arrangements Ltd

Interactive Investor Trading Limited

LGT Vestra LLP

Lloyds Banking Group Plc

Pershing Securities Limited

PricewaterhouseCoopers LLP

Rosediem Consulting Limited

Sarasin & Partners LLP

Standard Life Savings Limited

Tax Incentivised Savings Association (TISA)

UK Platform Group

Annex 2

Abbreviations used in this paper

BIPRU	Prudential sourcebook for Banks, Building Societies and Investment Firms
CASS	Client Assets sourcebook
CASS RP	CASS resolution pack
CBA	Cost benefit analysis
CMAR	Client money and asset return
CP	Consultation Paper
FCA	Financial Conduct Authority
IFPRU	Prudential sourcebook for Investment Firms
IPRU-INV	Interim Prudential sourcebook for Investment Businesses
ISA	Individual savings account
MiFID	European Parliament and Council Directive on markets in financial instrument (No. 2004/39/EC), commonly referred to as the 'Markets in Financial Instruments Directive'
MiFID II	European Parliament and Council Directive on markets in financial instruments (No. 2014/65/EU), commonly referred to as the 'Markets in Financial Instruments Directive II'
PRA	Prudential Regulation Authority
PS	Policy Statement
QMMF	Qualifying money market fund
UD	Unbreakable deposit



We have developed the policy in this Policy Statement in the context of the existing UK and EU regulatory framework. The Government has made clear that it will continue to implement and apply EU law until the UK has left the EU. We will keep the proposals under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

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Appendix 1

Made rules (legal instrument)

CLIENT ASSETS (TERM DEPOSITS) INSTRUMENT 2018

Powers exercised

- A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137A (The FCA’s general rules);
 - (2) section 137B (FCA general rules: clients’ money, right to rescind etc);
 - (3) section 137T (General supplementary powers);
 - (4) section 138C (Evidential provisions); and
 - (5) section 139A (Power of the FCA to give guidance).
- B. The rule-making provisions listed above are specified for the purposes of section 138G(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 22 January 2018.

Amendments to the Handbook

- D. The Client Assets sourcebook (CASS) is amended in accordance with Annex A to this instrument.
- E. The Supervision manual (SUP) is amended in accordance with Annex B to this instrument.

Citation

- F. This instrument may be cited as the Client Assets (Term Deposits) Instrument 2018.

By order of the Board
18 January 2018

Annex A

Amendments to the Client Assets sourcebook (CASS)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

7 Client money rules

...

7.13 Segregation of client money

...

7.13.13 R (1) An account which the *firm* uses to deposit *client money* under CASS 7.13.3R(1) to CASS 7.13.3R(3) must be a *client bank account*.

(2) ~~Each~~ In respect of each *client bank account* used by a *firm* must be held on terms under which to satisfy its obligation under CASS 7.13.3R(1) to (3):

(a) the relevant bank's contractual counterparty ~~is~~ must be the *firm* itself that is subject to the requirement under CASS 7.13.3R; and

(b) ~~unless the *firm* has agreed terms that comply with CASS 7.13.13R(3) subject to paragraph (3A), the *firm* is~~ must be able to make withdrawals of *client money* promptly and, in any event, within one *business day* of a request for withdrawal.

Transitional provision CASS TP 1.1.10AR applies to (2).

(3) ~~*Firms* may use *client bank accounts* held on terms under which withdrawals are, without exception, prohibited until the expiry of a fixed term or a notice period of a maximum of 30 days. [deleted]~~

(3A) Where the requirement under sub-paragraph (2)(b) is not satisfied and provided that the *client bank account* is not included in a *sub-pool*, a *firm* may use a *client bank account* from which it will be unable to make a withdrawal of *client money* until the expiry of a period lasting:

(a) up to 30 days; or

(b) provided the *firm* complies with CASS 7.13.14AR, from 31 to 95 days.

(4) Paragraphs (2)(b) and ~~(3)~~ (3A) do not apply in respect of *client money* received by a *firm* in its capacity as a *trustee firm*.

7.13.14 G CASS 7.13.13R(2)(b) and CASS 7.13.13R~~(3)~~(3A) do not prevent a *firm* from depositing *client money* on terms under which a withdrawal may be made before the expiry of a fixed term or a notice period (whatever the duration), including where such withdrawal would incur a penalty charge to the *firm*.

7.13.14 R A *firm* may only use one or more *client bank accounts* under CASS
A 7.13.13R(3A)(b) if:

(1) prior to using any such *client bank accounts*, it:

(a) produces a written policy that sets out:

(i) for each of its business lines, the maximum proportion of the *client money* held by the *firm* that the *firm* considers would be appropriate to hold in such *client bank accounts* having regard to the need to manage the risk of the *firm* being unable to access *client money* when required;

(ii) the *firm*'s rationale for reaching its conclusion(s) under (i); and

(iii) the measures that it will put into place to comply with sub-paragraph (2)(a) of this *rule*, having regard to CASS 7.13.14CE; and

(b) provides each of its *clients* with a written explanation of the risks that arise as a result of the longer notice period for withdrawals that:

(i) is clear, fair and not misleading; and

(ii) in respect of the medium of the explanation, satisfies whichever of COBS 6.1.13R (Medium of disclosure) or COBS 6.1ZA.19EU (Medium of disclosure) applies to the *firm* in respect of its obligations to provide information to the *client*; and

(2) while the *firm* uses any such *client bank accounts*, it:

(a) takes appropriate measures to manage the risk of the *firm* being unable to access *client money* when required;

(b) keeps its written policy under sub-paragraph (1)(a) under review, amending it where necessary; and

(c) provides any of its *clients* to whom it has not previously provided the explanation under sub-paragraph (1)(b) with

such a written explanation before it starts to hold or receive client money for them.

- 7.13.14 R (1) A firm must make and retain a written record of:
- B
- (a) the written policy it produces under CASS 7.13.14AR(1)(a); and
 - (b) each subsequent version of the written policy it produces as a result of CASS 7.13.14AR(2)(b).
- (2) The firm must make the record:
- (a) under sub-paragraph (1)(a) on the date it produces the written policy; and
 - (b) under sub-paragraph (1)(b) on the date it produces the new version of the written policy.
- (3) The firm must keep each record under this rule for a period of five years after the earlier of:
- (a) the date on which the version of the policy to which the record relates was superseded; and
 - (b) the date on which the firm ceased to use client bank accounts under CASS 7.13.13R(3A)(b).
- 7.13.14 E (1) Appropriate measures under CASS 7.13.14AR(2)(a) include the firm considering the need to make, and making where appropriate, quarterly or more frequent adjustments to the amount of client money held in client bank accounts under CASS 7.13.13R(3A)(b), taking into consideration the following factors:
- C
- (a) historic and expected future client money receipts and payments;
 - (b) the firm's own analysis of its exposure to the risk of being unable to meet instructions from its clients in relation to client money that it holds, applying an appropriate set of time horizons and stress scenarios; and
 - (c) the content of the firm's written policy under CASS 7.13.14AR(1)(a)(i) and (ii).
- (2) Compliance with (1) may be relied on as tending to establish compliance with CASS 7.13.14AR(2)(a).
- (3) Contravention of (1) may be relied on as tending to establish contravention of CASS 7.13.14AR(2)(a).

- 7.13.14 D G (1) Under CASS 7.13.14AR(2)(b) a firm should consider whether amendments to its written policy under CASS 7.13.14AR(1)(a) are needed for any reason, including in light of the firm's analysis in the course of its measures under CASS 7.13.14AR(2)(a).
- (2) Each time a firm amends its written policy under CASS 7.13.14AR(1)(a), it should also update the rationale for the amended policy under CASS 7.13.14AR(1)(a)(ii).
- (3) The stress scenarios under CASS 7.13.14CE(1)(b) should include a variety of severe yet plausible institution-specific and market-wide liquidity shocks.
- 7.13.14E G (1) If a fixed term or notice period for a withdrawal from a client bank account is scheduled to expire on a day on which a firm would expect to be unable to make the withdrawal, and the result is that the total period for which the withdrawal is prevented is longer than that permitted under CASS 7.13.13R(3A)(a) or (b), then the firm would be in breach of that rule.
- (2) Such a situation could arise because the fixed term or notice period expires on a day which is not a business day for the relevant bank.
- (3) Firms should therefore schedule their withdrawals from client bank accounts under CASS 7.13.13R(3A)(a) and (b) to avoid such breaches.
- 7.13.14F G Firms that hold client money using a client bank account under CASS 7.13.13R(3A)(b) and to which SUP 16.14 (Client money and asset return) applies may need to fill in their CMARs in the way set out at SUP 16.14.7R (Reporting of 'unbreakable' client money deposits).

...

10 CASS resolution pack

...

10.3 Existing records forming part of the CASS resolution pack

- 10.3.1 R A firm must include, as applicable, within its CASS resolution pack the records required under:

...

- (5B) CASS 7.13.14BR (policy for use of client bank accounts under CASS 7.13.13R(3A)(b));

...

...

TP 1.1 Transitional Provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...					
<u>10E</u> <u>A</u>	<u>The changes to CASS in Annex A of the Client Assets (Term Deposits) Instrument 2018</u>	<u>R</u>	<u>The changes effected by the provisions in the Annex listed in column (2) do not apply to any <i>firm</i> in respect of which:</u> <u>(1) prior to 22 January 2018 the <i>FCA</i> has directed under s.138A of the <i>Act</i> that CASS 7.13.13R(3) be applied with modifications; and</u> <u>(2) such a direction is in effect on 22 January 2018.</u>	<u>From 22 January 2018 to the date on which the relevant direction referred to in column (4) ceases to have effect.</u>	<u>22 January 2018</u>

Insert the following new row in the appropriate numerical position in Schedule 1 (Record keeping requirements). The text is not underlined.

Sch 1.3G

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...				
CASS 7.13.14BR	The <i>firm's</i> written policy produced under CASS 7.13.14AR(1)(a) in respect of the <i>firm's</i> use of <i>client bank accounts</i> under CASS 7.13.13R(3A)(b),	(i) For each of the <i>firm's</i> business lines, the maximum proportion of the <i>client money</i> held by the <i>firm</i> under CASS 7.13.3R(1) to (3) in respect of the business line that	On the date it creates the version of the policy	Five years after the earlier of: (1) the date on which the version of the policy was superseded; and (2) the date on which the <i>firm</i> ceased to use <i>client bank accounts</i> under

	and subsequent versions of it	<p>the <i>firm</i> considers would be appropriate to hold in such accounts;</p> <p>(ii) the <i>firm's</i> rationale for reaching its conclusion(s) under (i); and</p> <p>(iii) the means by which the <i>firm</i> will comply with CASS 7.13.14AR(2)(a), having regard to CASS 7.13.14CE.</p>		CASS 7.13.13R(3A)(b).
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Annex B

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text.

16 Reporting requirements

...

16.14 Client money and asset return

...

Reporting of ‘unbreakable’ client money deposits

- 16.14.7 R (1) This rule applies to a firm in respect of a CMAR required under SUP 16.14.3R where, at the end of the reporting period for the CMAR:
- (a) the firm holds client money using a client bank account under CASS 7.13.13R(3A)(b) (Segregation of client money); and
 - (b) the firm is unable to make a withdrawal from that client bank account until the expiry of a period lasting between 31 and 95 days.
- (2) A firm must use a separate row in data field 13 of its CMAR to report on any aggregate positive balance of client money held with a particular bank which, as at the end of the reporting period for the CMAR:
- (a) the firm is able to withdraw within a period of up to 30 days;
 - (b) the firm is unable to withdraw for a period of 31 to 60 days; and
 - (c) the firm is unable to withdraw for a period of 61 to 95 days.
- (3) (a) A firm must denote a balance falling under (2)(b) by using the words “unbreakable 31-60” in data field 13B of the CMAR.
- (b) A firm must denote a balance falling under (2)(c) by using the words “unbreakable 61-95” in data field 13B of the CMAR.
- 16.14.8 G (1) Because of SUP 16.14.7R(1)(b), SUP 16.14.7R would not apply to a firm where, for example:
- (a) it was using a client bank account under CASS 7.13.13R(3A)(b) that had a fixed term of over 30 days, but by the end of the reporting period for the CMAR there were fewer than 31 days remaining before the firm could withdraw

all the money in that account; or

- (b) it was using a client bank account under CASS 7.13.13R(3A)(b) that had a notice period of over 30 days for withdrawals, but by the end of the reporting period for the CMAR the firm had already served notice for withdrawal for all the money in that account and there were fewer than 31 days remaining before the end of the notice period.

- (2) Further guidance is available in SUP 16 Annex 29AG on completing data field 13 of the CMAR in cases where SUP 16.14.7R applies.

...

16 **Guidance notes for the data item in SUP 16 Annex 29R**
Annex
29AG

...

Section 3 **Segregation of client money**

...

13C *Client money* balances

...

The balance shown in that row may also include any balance that is included in data field 17.

If SUP 16.14.7R applies to a firm:

it should use a separate row to report:

- the total balance of client money held at that institution which the firm is able to withdraw within a period of up to 30 days;
- the total balance of client money held at that institution which the firm is unable to withdraw for a period of 31 to 60 days (using the marker “[Bank Name] unbreakable 31-60” in data field 13B); and
- the total balance of client money held at that institution which the firm is unable to withdraw for a period of 61 to 95 days (using the marker “[Bank Name] unbreakable 61-95” in data field 13B);

the firm does not need to report a nil balance row if there is no client money held at that institution that falls within a particular category above; and

if the firm has given notice for a withdrawal from a client bank account under CASS 7.13.13R(3A), it should take account of the amount and date of that withdrawal when completing this data field.

Table 13C shows an example of how a firm that was using client bank accounts under CASS 7.13.13R(3A)(b) at the end of the reporting period should complete data field 13. In this example:

- the first row shows the firm to hold £230,000 of client money at Bank A Ltd that, at the end of the reporting period, the firm is able to withdraw within a period of up to 30 days;
- the second row shows the firm to hold £60,000 of client money at Bank A Ltd that, at the end of the reporting period, the firm is unable to withdraw for a period of 31 to 60 days;
- the third row shows the firm to hold £11,000 of client money at Bank A Ltd that, at the end of the reporting period, the firm is unable to withdraw for a period of 61 to 95 days; and
- the fourth row shows the firm to hold £50,000 of client money at Bank B Ltd that, at the end of the reporting period, the firm is unable to withdraw for a period of 61 to 95 days.

Depending on circumstances at the end of the reporting period, the total client money balance reported in each row could reflect the individual balances held in a range of client bank accounts and the periods for withdrawal for all or part of those individual balances. For example, the reported £230,000 in the first row of Table 13C could be made up of £200,000 in an instant access account, £20,000 in a fixed term deposit of 95 days (for which 10 days remain before client money can be withdrawn) and £10,000 in a notice account (for which 20 days remain before client money can be withdrawn). There may also be additional amounts in the notice account for which mandatory notice of over 30 days has not yet been given; these would be included in the balance reported in the second or third row, depending on the mandatory period of notice.

Table 13C

<u>A</u>	<u>B</u>	<u>C</u>	<u>D</u>	<u>E</u>
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<u>Type</u>	<u>Institution</u>	<u>Client money balances (£k)</u>	<u>Country of incorporation of the institution</u>	<u>Is this a group entity?</u>
<u>CRD Credit Institution</u>	<u>Bank A Ltd</u>	<u>230</u>	<u>GB</u>	<u>No</u>
<u>CRD Credit Institution</u>	<u>Bank A Ltd unbreakable 31-60</u>	<u>60</u>	<u>GB</u>	<u>No</u>
<u>CRD Credit Institution</u>	<u>Bank A Ltd unbreakable 61-95</u>	<u>11</u>	<u>GB</u>	<u>No</u>
<u>CRD Credit Institution</u>	<u>Bank B Ltd unbreakable 61-95</u>	<u>50</u>	<u>GB</u>	<u>No</u>

...

TP 1.2 Transitional Provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...					
<u>12Z A</u>	<u>The changes to SUP in Annex B of the Client Assets (Term Deposits) Instrument 2018</u>	<u>G</u>	<u>As a result of CASS TP 1.1.10AAR the changes effected by the provisions in the Annex listed in column (2) would not apply to any firm in respect of which: (1) prior to 22 January 2018 the FCA has directed under s.138A of the Act that CASS 7.13.13R(3) be applied with</u>	<u>From 22 January 2018 to the date on which the relevant direction referred to in column (4) ceases to have effect</u>	<u>22 January 2018</u>

			<u>modifications; and</u> <u>(2) such a direction is in effect on 22 January 2018.</u>		
...					

