Thought Leadership:
What's next on the Regulatory Horizon: GDPR and CSDR

Introduction

After MiFID II came into force on the 3rd January 2018, you may have been forgiven for thinking that the 'regulatory goal posts' may have been set in place for a good while, and regulatory change programmes could be put on a back burner and project teams disbanded.

However, within financial services it would be safe to say that regulatory change has become one of the only constants since the financial crisis; and it is our opinion, and experience, that 2018 is looking set to continue this trend.

So what's next?

2018 is set to see the implementation of several new significant regulations, including the General Data Protection Regulation ("GDPR"), the continuation of the Central Securities Depositories Regulation ("CSDR") and elements of the extention of the Senior Manager and Certification Regime ("SMCR") going live.

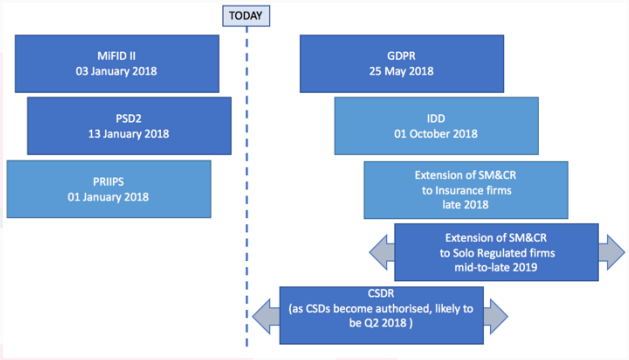

Figure 1: *Following MiFID II, firms are now getting ready for GPDR, CSDR, IDD (deadline moved from 23 February 2018 to 01 October 2018) and the extension of the SMCR.*

The Challenge of GDPR in a CASS context

The General Data Protection Regulation ("GDPR") is going to change how all companies handle their customers' data.

Within Financial services the scope of the regultions will be limited to records related to individuals who are resident in a European state, which in turn will translate in most cases to the retail client base of financial services firms. Consequently, the effects of GDPR are going to be felt most by functions within firms charged with handling retail client records, such as

transfer agencies, client services teams and investment/wealth managers.

The regulations focus particularly on digital records stored on computer systems, however, paper records which are stored in an organised and accessible manner also fall in scope and so must also be included in any prepatory exercises.

Whilst global firms, such as the big investment banking groups, will no doubt have significant project teams about complete ahead of the 25th of May deadline, this regulation becomes active for all companies simultaneously. Therefore, no matter the size of your firm, it is critical that you are aware of what measures are, and more importantly should, be in the pipeline.

In relation to CASS, the trickiest interaction with GDPR will be the right of data subjects to be forgotten. This will undoubtedly cause conflict with CASS's record keeping requirements - which mandate that firms must retain a wide remit of data for 5 years post activity.

Where a direct contradiction occurs, the rules in CASS will overrule GDPR requirements and data will be able to be retained. However, new requirements will need to be built into firms' governance arrangements to ensure, and be able to evidence, that this hierarchy is not being used as a blanket measure to restrict data subjects who wish for their data to be deleted where the firm has no due cause not to do so.

Also, from our work with clients we have become aware that many firms' meet the data retention aspect of CASS by holding all records indefinitely. This avoids having to worry about the time since last use or the date at which relationships with key third parties ended. Going forward this approach will not be compliant with GDPR and as such firms wll need to invest in smarter ways of storing client data.

Preparing for CSDR

The Central Securities Depositories Regulation ("CSDR") introduces new measures for the authorisation and supervision of EU Central Security Depositories ("CSDs"). However, it also set to have a substantial impact upon participants.

From the date that a CSD becomes authorised by their national competent authorities (e.g. FCA, BAFIN etc.) participants will have to make sure they are able to meet the stipulations of CSDRs associated Regulatory Technical Standards ("RTS"). Consequently, preparations should be well in place by now to hit the likely May 2018 deadline.

Most notable of these RTS, from a client money and assets perspective, is article 38 paragraphs 5 and 6, wherein participants of CSDs will be required to offer their clients' a choice between (i) Omnibus Segregated Accounts ("OSAs"), where all the participant clients' accounts appear undifferentiated from the CSD's perspective; and (2) Individual Segregated Accounts ("ISAs") where clients have their own bespoke arrangements.

Given the obvious cost implications of having to operate ISAs for clients, the rules allow for the passing on of reasonable charges to clients opting to use ISA to house their trading activity. The regulation also insists that CSD participants need to ensure that in their agreements with

clients, the associated costs and risks of the two structures are clearly explained to allow clients to make an informed choice between the two options.

The European trade body, the Association for Financial Markets in Europe and several of the bulge bracket investment banks and magic circle law firms have now published their responses to these requirements on their public websites and have consequently set the standard that other CSD participants should strive for to ensure full compliance with these new rules.

The disclosures have typically been drafted in the style of a side letter to be appended to a general terms and conditions, or product specific agreement. For firms with a global footprint, individual side letters have been drafted for each relevant European jurisdiction.

For each jurisdiction the letters cover the cost and risk of OSAs and ISAs to the clients' assets whilst the CSD participant's is a going concern (i.e. how the occurrence of shortfall will be treated during BAU operations) and should the CSD participant become insolvent, how assets will be repatriated to their benifical owners.

What will 2019 bring?

From 1 January 2019, the largest UK banks must separate core retail banking from their investment banking activities. This will involve both the creation of new entites and transfers of business between exisiting entities which are both areas prone to suffering from poor regulatory oversight.

Brexit will also be realised, and as articulated in the FCA's recently published Business Plan, will be upmost in many organisations thinking and strategic planning for the next year into early 2019.

From figure 1 you can also see that the SMCR will be extended to solo regulated firms from mid to late 2019 completing the migration from the approved persons regime started by banks in 2016.

Contact us

If you would like to discuss any of the issues raised in this paper further, or would like to discuss any area of the FCA's conduct rules or your own operational model, please get in touch directly by email or by leaving a message on our website.

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