FCA FINANCIAL CONDUCT AUTHORITY

12 Endeavour Square
London
E20 1JN

Tel: +44 (0)20 7066 1000
Fax: +44 (0)20 7066 1099
www.fca.org.uk

Harriett Baldwin MP
Chair
Treasury Sub-Committee on Financial Services Regulations
House of Commons
Committee Office
London
SW1A 0AA

07 February 2024

Dear Harriett,

Re: CP23/26, Implementing the Overseas Funds Regime (OFR)

Thank you for your letter of 10 January 2024 regarding our policy proposals on the implementation of the Overseas Funds Regime (OFR).[1]

On 30 January 2024, the Government announced that it found EU and EEA member states to be equivalent under the UK's Overseas Funds Regime.[2] The decision applies to funds authorised in EU and EEA member states as Undertakings for Collective Investment in Transferable Securities (UCITS), except for those which are also authorised as Money Market Funds.

This decision will allow EU and EEA UCITS to be promoted to UK retail investors once their application for recognition has been approved by the FCA and subject to complying with financial promotion requirements.

The Government has also announced it is considering whether to extend the UK's sustainable disclosure regime to funds recognised under the Overseas Funds Regime. We have been providing technical assistance to HM Treasury with its assessment and will continue to do so at their request.

Please see replies to the Sub-Committee's questions below.

1. *What input [will] you as a regulator will have into any decision by the Government to grant equivalence to an overseas regulatory regime?*

HM Treasury may make regulations approving a country or territory for the purposes of the OFR if it is satisfied that the equivalent protection test is met.

To meet that test, a country or territory must provide protection to investors or potential investors that is at least equivalent to that afforded by comparable UK-authorised schemes, as set out in section 271B of the Financial Services and Markets Act 2000 (the Act). HM Treasury must also be satisfied that there exist or will exist adequate arrangements for co-operation between the overseas regulator and the FCA.

As set out in section 271D of the Act, while the Government will make any equivalence decision when considering whether to approve a jurisdiction for the purposes of the OFR, HM Treasury may ask us to help by preparing a report that covers:

[1] https://www.fca.org.uk/publication/consultation/cp23-26.pdf
[2] https://questions-statements.parliament.uk/written-statements/detail/2024-01-30/hcws220

- The law and practice of the country or territory under which such schemes are authorised and supervised, or particular aspects of such law and practice; and
- Any existing or proposed arrangements for co-operation between the overseas regulator and ourselves.

In September 2023, we submitted a report to HM Treasury on the law and practice of six specified jurisdictions, including those representing the largest number of funds at the point of assessment - but not covering the EU as a whole – and on existing or proposed co-operation arrangements in those jurisdictions. HM Treasury is not legally bound by the FCA's findings in the report. It is for HM Treasury to be satisfied that the equivalent protection test is met and that adequate co-operation arrangements exist or will exist.

2. *How [would you] respond to the Government granting equivalence to an overseas regulatory regime which in your view was not an equivalent regime?*

Parliament has made the Government responsible for decisions on equivalence. We will provide advice as detailed above where it is requested of us. The Treasury Committee may wish to discuss with HM Treasury what advice it has requested from us and whether it would share any advice we provide to it on jurisdictions' equivalence.

In relation to the OFR, in September 2023 we submitted a report to HM Treasury on the law and practice of the specified jurisdictions and on existing or proposed co-operation arrangements, in response to a request made in accordance with section 271D of the Act. HM Treasury is not bound by the FCA's findings in the report, and it is for HM Treasury to be satisfied that the equivalent protection test is met and that adequate cooperation arrangements exist or will exist.

When the Government makes an equivalence decision, it may decide to impose additional requirements on recognised schemes which could be applied through the FCA Handbook, following consultation.

Once the Government is satisfied that the conditions for approving a jurisdiction in relation to the overseas funds regime are met, specified categories of funds from that jurisdiction can apply to the FCA for recognition in order to market to UK retail investors.

Under section 271G of the Act, the FCA can grant an application for recognition under the OFR only if it is satisfied that:

- The scheme is authorised in a country or territory which is approved by HM Treasury in regulations under section 271A of the Act;
- The scheme is of a description of scheme specified in the regulations;
- Adequate arrangements exist for co-operation between the FCA and the overseas regulator; and
- Where requirements imposed by regulations under section 271E of the Act would apply to the scheme or its operator if the application were granted, each such requirement would be satisfied.

The FCA has a duty to refuse applications for recognition if we consider it desirable to do so to protect the interest of UK participants or potential participants in a scheme.

The FCA is currently consulting on categories of information that it will collect from individual funds as part of the recognition and registration process that individual funds will need to go through for any jurisdictions that the Government deems equivalent. This information will aid us in assessing whether an individual scheme may represent a risk of harm to our objectives.

Our consultation was published before the Government announced an equivalence decision for the EU.[3] In it, we said that if the Government makes an equivalence decision in future for individual jurisdictions, further Handbook rules and guidance specific to any equivalence decision might also be needed if appropriate to address any consumer protection issues that fall within our powers as an independent regulator. If so, we would similarly consult on any such proposed rules or guidance.

3. *How [will you] make sure that UK investors are fully aware that they may not have access to any UK based redress as a result of misconduct from an overseas domiciled fund?*

As explained above, we are currently consulting on how we will operate a future registration regime for any overseas funds domiciled in jurisdictions that HM Treasury may designate as equivalent. Our consultation includes proposals to ensure that consumers receive information about whether or not they can access the Financial Ombudsman Service (FOS) and the Financial Services Compensation Scheme (FSCS) in respect to investments made in an OFR recognised scheme.

We are proposing that in instances where a UK financial promotion for an OFR recognised scheme falls under our rules, the promotion must include information about the availability of redress arrangements. Under this rule, a firm must not communicate or approve a financial promotion relating to an OFR recognised scheme unless the financial promotion clearly states that:

- The fund is authorised overseas, but not in the UK.
- The FOS is unlikely to be able to consider complaints related to the scheme, its manager, or its depositary.
- Any claims for losses relating to the manager and the depositary of the scheme are unlikely to be covered under the compensation scheme.
- A prospective investor should consider getting financial advice before deciding to invest and should see the prospectus of the scheme for more information.

We are also proposing a new rule which will require the operator to state explicitly in the fund's prospectus that an investor may not be able to seek redress under the UK regulatory system if the scheme operator and depositary's activities are not covered by the FOS and FSCS.

We currently require firms to provide redress information to investors, including information on their complaints process and whether their investment is covered by the FSCS.[4] Under our proposed draft rules for any overseas funds under the OFR, firms would have to provide information to retail clients explaining the arrangements for handling complaints about a product. Firms must also explain whether a right to cancel or withdraw exists, and if it does exist, the terms and conditions associated with that right. In addition, firms must also provide to retail clients present in the UK information that clearly explains:

- Whether the FOS is likely to be able to consider complaints against the scheme, its operator or its depositary.
- What arrangements, if any, exist that would enable investors in the UK to have a complaint against the scheme, its operator, or its depositary considered by an alternative dispute resolution mechanism in the relevant home state.
- That the activities of the scheme's operator and its depositary are unlikely to be covered by the compensation scheme and investors might not be protected under the regulatory system if either person should become unable to meet its liabilities to them.

[3] https://questions-statements.parliament.uk/written-statements/detail/2024-01-30/hcws220
[4] https://www.handbook.fca.org.uk/handbook/COBS/13/3.html

- What arrangements, if any, exist in the home state(s) of the scheme's operator or its depositary for the payment of compensation in the UK if they become unable to meet their liabilities to investors.

Our consultation is open until 12 February 2024. We will consider all feedback that we receive from the consultation but do believe it important that consumers are provided with sufficient information to inform them about the redress and complaints mechanisms that exist, or do not exist, when making decisions on whether to invest.

4. *How [will you] make sure that UK investors are fully aware of the redress available to them in the country in which the scheme they are investing in is domiciled?*

Under the FCA's power to make rules about prospectus contents, we are proposing a new rule which will require operators of OFR schemes to disclose information about redress arrangements. The operator must explain whether or not a UK investor:

- Would have the right to access an Alternative Dispute Resolution (ADR) scheme in the jurisdiction of the OFR recognised scheme (or of the operator or depositary, if different).

- Would be able to claim compensation in the jurisdiction of the scheme, its operator or its depositary, if any of those entities were unable to meet its obligations to return money to an investor.

Investors in overseas schemes may have the right to access ADR schemes and investor compensation schemes in the jurisdictions in which the fund is domiciled. However, the exact scope and terms of these arrangements will depend on the national law and regulation of the country of domicile and is likely to be different from the UK's Financial Services Compensation Scheme (FSCS) arrangements, including the amounts protected. It is worth noting that the access to redress investors have may be comparable to previous access under passporting but may be less comprehensive than is available in the UK domestically.

If investors have access to an overseas ADR scheme or compensation scheme, the prospectus will also have to indicate where further information about the relevant scheme can be obtained in English. As part of the recognition process for OFR schemes, we will ask for the scheme prospectus.

I hope the above information is helpful.

Yours sincerely

Sarah Pritchard
Executive Director of Markets and Executive Director of International