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Implementation of the new Overseas Fund Regime ("OFR") is an important piece of the jigsaw for the UK market place. With the FCA's publication *of Consultation Paper 23/26* in December, we have some, but only some, of the answers on outstanding aspects of the new regime.

In the Consultation, the FCA set out their proposals for the operational aspects of how the regime will work – the information the FCA will need to obtain from scheme operators to inform their recognition decisions, and proposals for notification requirements for overseas recognised schemes, and measures so consumers have a clear explanation that the UK Financial Ombudsman Service and Financial Services Compensation Scheme do not apply.

However, we are still awaiting the critical piece of the jigsaw from HM Treasury, and notably it making its equivalence regulations under Section 271A in relation to collective investment schemes in any overseas jurisdiction. The key issue for many firms is whether EU UCITS which are currently promoted in under the TMPR will need to apply for recognition under the OFR regime by the end of the statutory period for TMPR in order to continue marketing in the UK, which is expected if the Government makes equivalence regulations under Section 271A: we have yet to hear from the Treasury on this.

New terminology

Before explaining the FCA's proposals for the OFR, it is important to note the terminology now being used as we move into the post Brexit world and the OFR regime:

The Glossary term "recognised scheme" previously stood for overseas schemes recognised under several sections of FSMA – and most recently, Sections 264 and 272. This approach will continue, with the FCA applying the term "**recognised scheme**" both to

- **OFR recognised schemes.** Schemes recognised under Section 271A will be referred to as "OFR recognised schemes".

and

- **Schemes that are individually recognised under Section 272.** The FCA plan to review the rules on UK facilities for Section 272 recognised schemes (COLL 9.4) in due course, to consider whether to bring them into line with the proposals for the OFR recognised schemes set out in this Consultation Paper.

Text will be added to COLL 9 to explain the different kinds of recognised scheme which exist and to clarify which sections of the chapter apply to which kinds of scheme.

Guidance rules will be reinserted in Section 9.1 of PERG to direct operators of overseas open-ended investment companies by way of explanatory guidance.

Applying for recognition

If we assume that the Government makes a positive equivalence determination, the FCA now set out in this Consultation Paper the data they propose to request. They mention their favourite phrase again about taking a proportionate approach, in this instance given that any future equivalence assessment and acknowledging the scheme will have been approved by the relevant regulator in the home jurisdiction of the fund.

- **Information required**

  The FCA emphasise that, in assessing applications, they are going to focus on matters most relevant to protecting UK investors' interests, and the information intended to be requested will be that which is relatively available to funds and information that would normally be disclosed. Overall, it is clear that their emphasis is to be in a position for the FCA to act quickly to identify and prevent practices that could harm UK investors and potential investors.

  It is interesting to note that the FCA specifically point out that they are legally required to refuse applications if they consider it desirable to do so to protect the interests of UK participants or potential participants in the scheme. Whilst that scenario might be rare, they state that the FCA will assess each individual application in the light of the data it

receives to identify potential risks of consumer harm. This gives the FCA a clear way effectively to impose consumer duty like obligations should they decide to do so, particularly in relation to disclosure matters.

Also the UK is peculiar in prohibiting promotional payments being made out of the scheme property to third parties for promotion or distribution of units/shares. The FCA indicate they will look closely at any promotional payments during the application process for OFR recognition – asking for details of any such payments to entities associated with marketing or distributing the scheme, such as payments to a sponsor. They do not though indicate whether that will be a matter which will preclude recognition being given.

- **Financial promotions**

  As part of the information provided in an application, information will be required about marketing and distribution.

  Financial promotions relating to units in an OFR recognised scheme will need to be communicated or approved by a UK authorised firm, unless a financial promotion exemption applies. This is different from the current position for EEA UCITS under the TMPR which are able to communicate financial promotions themselves, because they are deemed under FSMA to be authorised persons.

  The FCA are going to request the identity of the UK financial promotion approver which will allow the FCA to verify whether that firm has permission to approve financial promotions where such approval is needed.

- **Application fees**

  Applications will be charged at Category 4 in FEES 3, Annex 2: £2,500 for a stand-alone scheme and double for an umbrella scheme, currently £5,000. Periodic charges will be in line for those charged to UK UCITS, set out in FEES 4, Annex 4. It is likely these rates will be increased – and the new rate will be consulted on in April 2024 fee rates Consultation Paper to take effect from 1 July 2024.

  If the Government makes an equivalence decision before July 2024, some TMPR schemes which were allocated earlier landing slots to apply for recognition under OFR may pay lower application fees than those in later slots. The FCA are indicating that they propose to exempt schemes that are in the TMPR from the increase, so that all TMPR schemes pay the same application fee.

Changes

As you would expect, certain changes will require notification prior to their occurrence – thirty (30) days before it could take effect in the UK. Such changes will include changes to the scheme name; legal structure; suspension in dealings in units/shares; a fundamental change to a scheme's investment objective, policy or strategy; a scheme's target investors in the UK; the minimum investment amount; or matters that would likely cause significant negative effect on UK investors such as a material increase in fees or change in redemption terms. In addition, the list of changes also includes termination of a scheme or sub-fund in its home jurisdiction, or a request to derecognise the scheme or sub-fund when it remains in existence but the operator no longer wishes for it to be marketed in the UK; and supervisory sanctions imposed by the scheme's home regulator on the operator, or the scheme itself, as well as any voluntary restrictions on their activities agreed by them.

For other changes, operators will be required to notify the FCA within thirty (30) days of those changes and to confirm on an annual basis on the FCA's system that all the data held is up to date.

Enhanced disclosures given the lack of access to FSCS and FOS

The Government has decided the OFR will operate outside the scope of the FOS and FSCS. This though applies to the scheme – regulated activities by FCA authorised firms, for example, in relation to platform investment arrangements could still be covered. Nonetheless, the overall proposition essentially remains.

As a consequence, where the FOS and FSCS are not available to investors, the FCA want customers to be informed about whether or not they can access redress arrangements outside the UK.

There is to be a rule in a new section 4.15 of the Conduct of Business sourcebook (COBS) setting out rules for financial promotions relating to OFR recognised schemes and specifying the financial promotions to which the rules do not apply. The FCA's proposal is that a disclosure in a promotion should indicate as a minimum that:

- the fund is authorised overseas but not in the UK;
- the FOS will not be able to consider complaints about the operator or depositary of the fund (as they are not FCA authorised firms carrying on regulated activities from establishments in the UK) unless the firm has joined the Voluntary Jurisdiction and the relevant conditions in the FCA's rules are met;
- any claims against the non-UK authorised operator of the scheme are unlikely to be covered by the FSCS; and
- investors may wish to obtain financial advice before investing and/or ask for more information or see the fund's prospectus.

A new rule, COLL 9.5.5R(2) is proposed which will require the operator to disclose information in the fund's prospectus about redress arrangements in an English language prospectus available to UK investors. This must include a statement that a UK investor may not be able to seek redress under the UK regulatory system if the activities of the operator and depositary of the scheme are not covered by the FOS or the FSCS. The proposal is that the prospectus must explain whether or not a UK investor:

- would have the right to access an alternative dispute resolution (ADR) mechanism in the jurisdiction of the OFR recognised scheme (or of its operator or depositary, if different). If there would be access, the prospectus must indicate where further information in English about that scheme can be obtained.

and

- 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 liabilities to the investor.

Currently for UK UCITS, TMPR funds and EEA UCITS recognised under Section 272 there is a requirement for a Key Investor Information Document (KIID). The intention is to extend a similar UK disclosure requirement to OFR recognised schemes through secondary legislation to be laid before the end of 2023.

The FCA though plan to require firms to provide information on redress arrangements in a supplementary document – as currently set out in COBS 13.3.1R(2). This information will be similar to the statements mentioned above to appear in the prospectus under a new COBS 14.2.1-BR provision.

Once the Government replaces existing point of sale disclosure requirements with a new consumer disclosure regime, the FCA will have powers to make rules applying to all regulated schemes marketed to retail customers, including those recognised under the OFR and under section 272. The FCA will then have their own consultation on proposals for the new regime in 2024. The position may therefore change pursuant to that new consultation.

It seems likely that the FCA will consider additional clarifications depending on how the Future Disclosure Framework is introduced. They think there is a case of mandating further disclosure about the scope of UK redress arrangements as part of the sales process, especially where customers carry out execution only transactions through an intermediary such as a platform provider. For example, the FCA could require UK platforms to provide an enhanced digital disclosure (e.g. a pop-up risk warning) about the lack of UK coverage, in similar terms to the warnings that are required for high risk investments. At this point though, they are only asking for views.

Access to a UK representative of the operator

As the FCA feel it is important that UK investors are able to contact a scheme operator without facing undue barriers, get information, give instructions or ask questions, the FCA intends to require operators of OFR recognised schemes to continue providing facilities of this kind to UK investors. So copies of essential documents (constituting instrument, prospectus, most recent reports and accounts, and key investor information document) should all be available on demand, together with

information about how to check the latest prices of units. Although most activities do not fall within regulated activities, it is likely that some (accepting instructions to buy and sell units) could fall within regulated activities such as arranging deals. Firms will need to satisfy themselves any appropriate FCA authorisation required for those activities.

The expectation, given the platform and nominee arrangements, is that it is likely that few, if any, OFR recognised schemes will have any unitholders in this situation who may require physical UK facilities to be available to them, so the need for physical office facilities may disappear. Whilst in the past the UK representative has had to maintain an office in the UK which investors could visit or to which they could apply, the FCA thinks it reasonable to allow OFR recognised schemes to adopt a policy which allows facilities to be provided within the EEA without a physical presence in the host state (following the amended Article 92(2) of the UCITS Directive), at least in cases where the terms and conditions of investment anticipate that all interactions will take place via electronic media, or where the customer has individually consented to such arrangements. The requirement for a physical address will only remain where direct investors have not previously used electronic means of communication and do not consent to do so.

Mergers and amalgamations

On the assumption that a UCITS could merge with a UCITS pre Brexit, COLL 7.6.2R(2) allowed a UK UCITS scheme to be merged with an EEA UCITS scheme which is recognised under Section 264 of FSMA, and this continues to be the case for recognised schemes that can be marketed under the TMPR.

In future, the FCA's view of this is that it would be inappropriate to continue treating all EEA UCITS as meeting the required standard of comparable investor protection unless there has been a determination based on an equivalence assessment. If the Government decides to designate that some or all EEA UCITS are under the OFR process, the FCA would maintain the ability of UK AFMs to propose a scheme of arrangement between a UK UCITS and a recognised EEA UCITS. Amendments are proposed to COLL 7.6.2R(2) on the basis that such a determination may be made (but they might reconsult on an alternative approach if EEA UCITS are not able to be recognised schemes under the OFR).

Note that the FCA think it inappropriate to extend the rule to cover any other categories of overseas funds that might in future be recognised under the OFR although they may consider the matter again if and when a non-EEA jurisdiction is designated by the Government under Section 271A FSMA. The FCA do however propose to modify the rule to include any EEA UCITS recognised under Section 272.

Where the provision applies, COLL 7.6.2R(7) will be amended so that, in any merger proposal, the documents must set out the consequence that they will be outside the scope of the FOS or the FSCS.

As indicated at the beginning of this Briefing Paper, the FCA's Consultation Paper CP23/26 provides only part of the jigsaw for the new OFR regime.

Critical to the effectiveness of the OFR is the still awaited publication by the HM Treasury regarding their decision on the equivalence regulations under Section 271A in relation to collective investment schemes in any overseas jurisdiction and their decision on the key issue of whether EU UCITS which are currently promoted under the TMPR can apply for recognition under the OFR regime by the end of the statutory period for TMPR.

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