MONTHLY REGULATORY UPDATE
OCTOBER 2019
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Overview:
The FCA is consulting on plans to ban commission models that give motor finance brokers/dealers an incentive to raise customers’ interest rates. It is also consulting on minor changes to some of their rules and guidance to ensure that many types of credit broker give consumers more relevant information about commission.

The FCA’s extensive research into this sector has found that discretionary commission models have led to higher finance costs for consumers. Firms are also often failing to give customers timely, relevant information. This paper consults on proposals to:

- ban commission models that can give brokers and motor dealers an incentive to increase a customer’s interest rate; and
- amend parts of the rules and guidance relating to the disclosure of commission arrangements with lenders.

Applicable to:
- motor finance providers; and
- motor finance credit brokers, including motor dealers.

Chapter 4 is directly relevant to many types of brokers of regulated credit and consumer hire agreements.

This consultation will also be of interest to trade bodies representing consumer credit lenders, consumers and consumer organisations.

Next steps:
Send comments to the FCA by 15 January 2020.
Email your responses to cp19-28@fca.org.uk.
Overview:
The FCA will be the anti-money laundering and counter terrorist financing (AML/CTF) supervisor for cryptoasset businesses, from 10 January 2020. This consultation sets out its proposals for recovering the costs of this new role.

The Treasury has announced, in the Economic Crime Plan (ECP), that the FCA will be the anti-money laundering and counter terrorist financing (AML/CTF) supervisor of UK cryptoassets businesses under the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs).

Evidence of increased risks from growing use of cryptoassets for illicit activity, as well as risks to consumers and markets has resulted in the Government and financial regulators moving to minimize those risks.

The EU is addressing these through the Fifth Money Laundering Directive (5MLD). The UK is doing so through amendment to the MLRs.

Applicable to:
This applies to any business which undertakes or expects to undertake the cryptoasset activities identified in the Treasury 2019 consultation paper.

Next steps:
Consider the proposals and send comments to the FCA by 11 November 2019 regarding Question 1, and 10 December 2019 regarding Question 2.

Email your responses to cp19-29@fca.org.uk.
Policy Statement

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<th>PS19/25</th>
<th>Overdraft Pricing and Competition Remedies</th>
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Overview:
As part of the High-Cost Credit review, the FCA published the Overdraft Pricing Policy Statement (PS19/16). They made rules to change the way banks and building societies charge for overdrafts. Their rules are designed to fundamentally reform the overdraft market and to address the harm they found which was high prices for unarranged overdrafts, complex pricing structures, low consumer awareness and the repeat use of overdrafts. This policy statement completes the FCA's package of remedies designed to reduce harm in the overdraft market and improve competition.

Applicable to:
This PS is applicable to banks and building societies that offer overdrafts. Their trade bodies should also read this document. This will also be of interest to consumers who use overdrafts and to consumer groups and digital comparison services.

Next steps:
The new rules on the publication of pricing information will come in to force on 6 April 2020, in line with the overdraft pricing rules set out in PS19/16.

|---------|--------------------------------------------------------------------------------|

Overview:
Policy statement PS19/26 confirms the regulatory technical standards for strong customer authentication and common and secure open standards of communication, which will apply in the UK, in the event of a no-deal exit by the UK from the EU.

The UK regulatory technical standards are substantially the same as EU technical standards designed to make electronic payments safer and more secure. Making the UK regulatory technical standards in this way will provide certainty for firms and maintain consumer protections.

In December 2018, as part of the FCA’s Brexit contingency plan it consulted on making regulatory technical standards for strong customer authentication and common and secure open standards of communication (CP18/44). These standards would apply in the event of the UK’s withdrawal from the European Union (EU) without a ratified withdrawal agreement, “a no-deal exit”.

In the consultation paper, the FCA proposed to make these standards substantially the same as EU regulatory technical standards (EU-RTS) after a no-deal exit. This policy statement summarises the feedback the FCA received from the consultation and publishes the UK regulatory technical standards (UK-RTS), together with handbook changes, which they will make in the event of a no-deal exit.
Applicable to:
This policy statement will primarily be of interest to payment service providers, including:

- banks;
- building societies;
- e-money issuers;
- payment institutions;
- registered account information service providers; and
- payment initiation service providers.

It will also be of interest to consumer bodies and relevant trade bodies, retailers, consumers, micro-enterprises and those involved in open banking initiatives.

Next steps:
Payment service providers must comply with the provisions of the UK-RTS in the event of a no-deal exit.

Overview:
This policy statement sets out the FCA's changes that it is making to its responsible mortgage lending rules based on the proposals and the feedback that it received via CP19/14.

The CP set out the FCA’s concerns that some consumers cannot switch to a more affordable mortgage, despite being up to date with their mortgage payments. This includes those who cannot switch because of changes to lending practices during and after the 2008 financial crisis, and subsequent regulation that tightened lending standards – often referred to ‘mortgage prisoners’. The FCA concluded that consumers in this position, or those who could be in this position in the future, are suffering harm, as they are paying higher than necessary mortgage payments.

The CP proposed to remove barriers to consumers switching to a more affordable mortgage. The FCA proposed changes to responsible lending rules to allow lenders to use a more proportionate affordability assessment for consumers who are up to date with their existing mortgage and who want to switch to a more affordable mortgage without borrowing more. The proposals also aimed to reduce the time and costs of switching for all consumers meeting this definition.
Changes to the mortgage responsible lending rules and guidance - feedback on CP19/14 and final rules

Applicable to:
This policy statement will be directly relevant to:

- mortgage lenders;
- mortgage administrators;
- mortgage intermediaries;
- unregulated entities that own mortgage books; and
- mortgage customers.

It will also be relevant to stakeholders with an interest in the mortgage market, including trade bodies representing mortgage firms, charities and other organisations and consumer organisations.

Next steps:
All the rules outlined in this policy statement come into force immediately.

Press Release

- **FCA sets out potential remedies to tackle concerns about general insurance pricing** – The FCA has published the interim report of its market study into the pricing of home and motor insurance. The FCA found that competition is not working well for all consumers in these markets. It sets out concerns about how pricing in these markets leads to consumers who do not switch or negotiate with their provider paying high prices for their insurance.

  The FCA estimates that around 6 million policyholders pay high prices and are not getting a good deal on their insurance. If those customers paying high premiums paid the average premium for their risk they could save around £1.2 billion a year. This affects all types of customers. The FCA estimates this includes 1 in 3 people who are potentially vulnerable.

- **FCA urges victims to come forward after getting confiscation order against three individuals** – Southwark Crown Court has made confiscation orders against Samrat Bhandari, Muhammad Mirza and Paul Moore, following their earlier convictions and prison sentences for running an illegal investment scheme that lost investors over £1.4 million.

  Between 2009 and 2014, they systematically misled investors, many of whom were retired and vulnerable, by giving them wholly misleading information about the value and prospects of Symbiosis Healthcare Plc.

- **FCA announces future work on climate change and green finance** – The FCA has published a feedback statement setting out its proposals to improve climate change disclosures by issuers and information to consumers on green financial products and services.

  The statement identifies a number of priorities, which will provide a foundation for the FCA’s future work on climate change and green finance. These include issuers’ climate change disclosures, regulated firms’ integration of climate change risk and opportunities into their decision-making and consumers’ access to green financial products and services.
FCA data shows 4.29m complaints for first half of 2019 - The FCA has published the complaints figures for regulated firms for the first half (H1) of 2019. The data shows an increase in complaints from 3.91m in the second half (H2) of 2018 to 4.29m in the first half of 2019.

The increase in complaints was mainly driven by a 34% increase in the volume of PPI complaints received, from 1.58m to 2.12m. PPI complaints made up 49% of all complaints received during this period, continuing to be the most complained about product.

While PPI complaints increased in the first half of 2019, there was a 6% drop in the number of non-PPI complaints, from 2.32m in 2018 H2 to 2.18m in 2019 H1. When PPI is taken out, the figures today are the lowest volume of complaints firms have received since new reporting rules came into effect in 2016.

Excluding PPI complaints, the most complained about products remain current accounts (14% of reported complaints), credit cards (8%) and motor and transport insurance (6%). The average volume of complaints received per 1,000 accounts for banking and credit cards has decreased to 4.2, compared to 4.6 in 2018 H2. This was also the case for home finance, which decreased from 9.6 to 8.7 complaints per 1,000 mortgage accounts.

Overall, excluding PPI, the average redress per complaint upheld increased from £175 to £200 between 2018 H2 and 2019 H1.
Overview:
In this consultation paper (CP), the Prudential Regulation Authority (PRA) proposes to amend its expectation on the treatment of restricted Tier 1 own funds (rT1) instruments in the light of recent information from HMRC. The proposals would make amendments to Supervisory Statement (SS) 3/15 ‘Solvency II: the quality of capital instruments.’

The SS currently sets out the PRA’s expectation that insurers will deduct the maximum tax charge generated on write down, when including externally issued rT1 instruments in their own funds. This consultation proposes expanding this expectation to reflect the maximum tax charge that could be generated on conversion of such items into ordinary shares. To reflect any changes to SS3/15 following this consultation the PRA would also update the reporting clarification published as Appendix 2 to Policy Statement (PS) 4/19 ‘Solvency II: Adjusting for the reduction of loss absorbency where own fund instruments are taxed on write down’.

The purpose of the proposals in this consultation is to maintain the existing regulatory policy of only recognising rT1 items to the extent that they provide loss absorbency on trigger, and to prevent the amount of loss-absorbency provided by rT1 instruments that convert into ordinary shares on trigger from being overstated.

Applicable to:
The CP is relevant to UK insurance firms within the scope of Solvency II, the Society of Lloyd’s, and firms that are part of a Solvency II group that will determine and classify capital instruments under the Solvency II own funds regime, together with their advisors.

Next steps:
This consultation closes on Monday 13 January 2020. The PRA invites feedback on the proposals set out in this consultation. Please address any comments or enquiries to CP26_19@bankofengland.co.uk.

The proposals set out in this CP have been designed in the context of the current UK and EU regulatory framework. The PRA will keep the policy under review to assess whether any changes would be required due to changes in the UK regulatory framework, including those arising once any new arrangements with the European Union take effect.

In the event that the UK leaves the EU with no implementation period in place, the PRA has assessed that the proposals would not need to be amended under the EU (Withdrawal) Act 2018 (EUWA)
CP27/19  Liquidity: The PRA’s approach to supervising liquidity and funding risks

Date Published – 17 October 2019

Overview:
In this Consultation Paper (CP), the Prudential Regulation Authority (PRA) sets out proposals to update Supervisory Statement (SS) 24/15 ‘The PRA’s approach to supervising liquidity and funding risk’ to reflect relevant updates to the Bank of England’s Market Operations Guide and to reiterate relevant expectations set out in SS9/17 ‘Recovery Planning’.

The PRA considers that a consultation period of one month is justified given the relatively minor impact of the proposed updates and the benefit of providing clarity to firms by aligning SS24/15 with the Market Operations Guide as soon as possible.

The proposals set out in this CP have been designed in the context of the current UK and EU regulatory framework. The PRA has assessed that the proposals will not be affected in the event that the UK leaves the EU with no implementation period in place.

Applicable to:
This CP is relevant to PRA-authorised UK banks, building societies, and PRA-designated UK investment firms, referred to collectively as ‘firms’.

Next steps:
This consultation has closed.
Policy Statement

Enforcement: Changes to the PRA’s settlement policy

Date Published – 4 October 2019

Overview:
This Prudential Regulation Authority (PRA) Policy Statement (PS) provides the final Statement of Policy (SoP) ‘The PRA’s approach to enforcement: Statutory statements of policy and procedure’ (Appendix), as consulted in Consultation Paper (CP) 10/19 ‘Enforcement: Changes to the PRA’s settlement policy’. The PRA received no responses to the CP and has decided to make the changes to the SoP as consulted.

The PRA proposed, by way of amendment to the SoP, to:
- simplify the PRA’s settlement discount scheme (by retaining a 30% penalty discount for early settlement and removing the 20% and 10% discounts available for settlement in later stages of an enforcement action); and
- clarify and make more transparent the PRA’s procedures for settlement.

Applicable to:
This PS is relevant to PRA-authorised persons, qualifying parent undertakings, persons who are or have been auditors or actuaries of a PRA-authorised person, senior managers and certified employees at firms, and all individuals involved in providing financial services to PRA-authorised persons.

Next steps:
The SoP takes effect from Friday 4 October 2019, with one exception: in relation to cases where the PRA has already concluded ‘Stage 1’ settlement discussions with the subject, without reaching a settlement, prior to Friday 4 October 2019, the existing scheme as set out in the March 2019 SoP ‘The PRA’s approach to enforcement: Statutory statements of policy and procedure’, will continue to apply.
Large Exposures: Reciprocation of French Measure

Overview:
This Prudential Regulation Authority (PRA) Policy Statement (PS) provides the PRA’s final rule following Consultation Paper (CP) 15/19 ‘Large exposures: Reciprocation of French measure’. The PRA received no responses to the consultation.

In CP15/19 the PRA proposed to tighten the large exposure limit in CRR Article 395(1) to 5% of eligible capital, in respect of the exposures of UK G-SIs and O-SIs to French non-financial corporations, meeting the definition of ‘highly indebted’.* This reciprocates the same measure imposed by the Haut Conseil de stabilité financière (HCSF) in France in July 2018.

The PRA has made one minor change to the draft rule-making instrument (Rule 5.1) to remove possible ambiguity on the scope of application. The PRA considers this will have no impact on firms, and specifically, mutuals.

The policy presented in this PS will take effect on Wednesday 1 January 2020.

The policy set out in this PS has been designed in the context of the current UK and EU regulatory framework. The PRA will keep the policy under review to assess whether any changes would be required due to changes in the UK regulatory framework, including those arising once any new arrangements with the European Union take effect.

Applicable to:
The measure described in this PS applies on a consolidated basis to firms identified by the PRA as global systemically important institutions (G-SIs) and other systemically important institutions (O-SIs), under the Capital Requirements Directive (2013/36/EU) (CRD) as implemented in the Capital Requirements (Capital Buffers and Macro-prudential measures) Regulations 2014. This PS is therefore relevant to such firms and their subsidiaries.

Next steps:
The policy presented in this PS will take effect on Wednesday 1 January 2020.
Working Paper

- **Predicting bank distress in the UK with machine learning** – Using novel data and machine learning techniques, the PRA has developed an early warning system for bank distress. The main input variables come from confidential regulatory returns, and their measure of distress is derived from supervisory assessments of bank riskiness from 2006 through to 2012. They contribute to a nascent academic literature utilising new methodologies to anticipate negative firm outcomes, comparing and contrasting classic linear regression techniques with modern machine learning approaches that are able to capture complex non-linearities and interactions. They find the random forest algorithm significantly and substantively outperforms other models when utilising the AUC and Brier Score as performance metrics.

The PRA go on to vary the relative cost of false negatives (missing actual cases of distress) and false positives (wrongly predicting distress) for discrete decision thresholds, finding that the random forest again outperforms the other models. They also contribute to the literature examining drivers of bank distress, using state of the art machine learning interpretability techniques, and demonstrate the benefits of assembling techniques in gaining additional performance benefits. Overall, this paper makes important contributions, not least of which is practical: bank supervisors can utilise the findings to anticipate firm weaknesses and take appropriate mitigating action ahead of time.

Bank Overground

- **How are semi-autonomous features on vehicles affecting the UK motor insurance sector?** – New vehicles are fitted with increasingly advanced technology. The PRA has highlighted three trends and consider whether new sources of data will be required to monitor the changing risks arising from autonomous technology on vehicles.

The UK might still be many years away from a fully autonomous vehicle, but preparations are underway. For example, the UK’s first autonomous vehicle test track launched recently. Against this backdrop, the PRA look at three different data sets (Department for Transport, Society of Motor Manufacturers and Traders, and Solvency II) and examine whether they provide insights to enable monitoring and forecasting of the changing risk landscape.

In 2017, the PRA projected a potential reduction in the size of the motor insurance market over the next two decades as autonomous vehicles take to the road. They also highlighted likely increased losses arising from product liability, cyber-attacks, litigation and disruption caused by the technological failure of autonomous vehicles.

Data from the Department for Transport indicate a sharp rise in technology-attributed recalls (Chart A), suggesting the potential for these risks is increasing.
UK FINANCE (UKF)

Report

- **2019 Total Tax Contribution of the UK Banking Sector** - This year’s Total Tax Contribution Study for the UK banking sector, commissioned by UK Finance, found that the UK banking sector paid £39.7 billion in taxes in the financial year to March 2019, with banks seeing a 50 per cent rise in taxes borne over the past five years.

  The report found that the banking sector’s tax contribution accounted for 5.5 per cent of total UK tax receipts. Half of this contribution was paid by foreign-headquartered banks and the other half by UK-headquartered banks. Employment taxes accounted for £21.8 bn of the total taxes paid by the sector, equivalent to 7.3 per cent of all UK employment tax receipts, reflecting the large number of highly skilled workers employed in the banking industry.

  The report also includes analysis of the UK’s tax competitiveness for banking relative to other leading global financial centres. London continues to have the highest total tax rate for a typical corporate and investment bank out of the three major financial services centres surveyed. The rate in London is 47.1 per cent, 13.6 percentage points higher than New York City (33.5 per cent) and 2.4 percentage points higher than in Frankfurt (44.7 per cent).

BANK OF ENGLAND (BOE)

Speech

- **Remarks by Mark Carney (Governor of the Bank of England) given during the UN Secretary General’s Climate Action Summit 2019** – Ultimately, the speed with which the new sustainable finance develops will be decided by the coherence and credibility of countries’ climate policies. Finance will complement - and potentially amplify these initiatives— but it will never substitute for climate policy action.

  The policy frameworks with the greatest impact will be: time consistent; transparent; target-based; and committed, through treaties, Nationally Determined Contributions (NDCs), domestic legislation and consensus. The 20 countries – including the UK – that have plans to legislate for net zero show what can be done.

  If countries build their track records, their credibility will grow, and the market will allocate capital to deliver the necessary innovation and growth and pull forward the adjustment to a low carbon future.

  The more prolific the reporting, the more robust the risk management and the more widespread the return optimisation, the more rapidly the insurance sector can build resilience while promoting the transition that citizens demand.
Blog

- **Enabling access, erasure, and rectification rights in AI systems** – In this blog, Reuben Binns, the ICO’s Research Fellow in Artificial Intelligence (AI), discusses the challenges organisations may face in implementing mechanisms in AI systems that allow data subjects to exercise their rights of access, rectification and erasure.

This post is part of the ICO’s ongoing Call for Input on developing the ICO framework for auditing AI. They encourage consumers to share their views by emailing the ICO at AIAuditingFramework@ico.org.uk.

Under the General Data Protection Regulation (GDPR) individuals have a number of rights relating to their personal data. These rights apply to personal data used at the various points in the development and deployment lifecycle of an AI system, including personal data:

- contained in the training data;
- used to make a prediction during deployment; or
- that might be contained in the model itself.

This blog post describes the considerations organisations may encounter when attempting to comply with three specific rights – access, rectification and erasure - in relation to AI systems, and where exemptions may apply.

- **Data Protection Impact Assessments and AI** – Simon Reader, Senior Policy Officer, discusses some of the key considerations for organisations undertaking data protection impact assessments for Artificial Intelligence (AI) Systems.

This blog post is part of the ICO’s ongoing Call for Input on developing the ICO framework for auditing AI. The ICO encourage consumers to share their views by emailing them at AIAuditingFramework@ico.org.uk.

Several of the blogs in this series have referred to the importance of carrying out a Data Protection Impact Assessment (DPIA) for AI systems that will process personal data. DPIAs offer organisations an opportunity to consider how and why they are using AI systems to process personal data and what the potential risks could be.

The ICO has produced detailed guidance on DPIAs that explains when they are required and how to complete them. This blog sets out some of the things organisations should think about when carrying out a DPIA for the processing of personal data in AI systems.

**DPIAs under the General Data Protection Regulation (GDPR)**

The GDPR states that, DPIAs are required (at least):

- before the deployment of innovative technological solutions;
- for the processing of special category personal data at large scale; or
- for automated decision-making, profiling, or for the expected denial of a service to an individual.

The use of AI for processing personal data will therefore usually meet the legal requirement for completing a DPIA. If the result of an assessment indicates residual high risk to individuals that cannot be reduced, data controllers must consult with the ICO.
What should be assessed in a DPIA

A DPIA needs to describe the nature, scope, context and purpose of any processing of personal data. It needs to make clear how and why AI is going to be used to process the data. It will need to detail:

- how data will be collected, stored and used;
- the volume, variety and sensitivity of the input data;
- the nature of the data controller’s relationship with data subjects; and
- the intended outcomes for individuals, wider society and for the data controller.

BUILDING SOCIETIES ASSOCIATION (BSA)

Press Release

- BSA responds to FCA updated responsible lending rules – The Financial Conduct Authority has set out the finalised changes to its responsible mortgage lending rules.

Paul Broadhead, BSA Head of Mortgages and Housing comments:

“The BSA welcomes FCA’s updated responsible lending rules. BSA members actively participated in the implementation group, and we thank the FCA for their collaborative approach to this consultation.

“For customers who are currently on reversion rates with inactive or unregulated mortgage owners and have demonstrated a good payment history, the new rules could give them the opportunity to remortgage to a new lender.

“However the BSA, and now the FCA, recognise that those borrowers with unregulated lenders have fewer safeguards, and we would support the call for an extension to the regulatory perimeter.

“Now that the final shape of the rules has been established, lenders can begin to analyse how they fit with their respective lending policies.

“We will continue to work with our members and the FCA to support these changes, but it is important to recognise that this intervention will only help a proportion of the customers identified by the FCA in the Mortgage Market Study.”
FOR FURTHER INFORMATION CONTACT

Jonathan Pepper
RSM Risk Assurance Services LLP

Fifth Floor, Central Square, 29 Wellington Street, Leeds, LS1 4DL
Jonathan.Pepper@rsmuk.com
Tel: +44 (0)113 285 5000
Mob: +44 (0)7940 050221

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