

Insights

FCA CONSULTS ON CHANGES TO INVESTMENT RESEARCH AND BEST EXECUTION REPORTING

May 20, 2021

SUMMARY

On 28 April 2021 the Financial Conduct Authority (FCA) published a consultation paper ([CP 21/9](#)) on proposed changes to its investment research rules and best execution reporting requirements. We discuss these proposed changes, their context and EU / MiFID II counterparts in this alert.

BACKGROUND: A NEW UK LEGISLATIVE FRAMEWORK POST-BREXIT

The FCA's consultation is part of the capital markets review it is conducting alongside HM Treasury in light of Brexit and the resultant ability to depart from EU rules. This review will focus on what the FCA describes as "priority areas", many of which stem from the UK's onshored MiFID II requirements. These priority areas include: market structures, pre- and post-trade transparency for shares, bonds and derivatives; the cost and distribution of market data; and commodity derivatives markets.

The first part of the review is the FCA's proposed changes to the investment research and best execution reporting rules.

THE MIFID II POSITION

The investment research rules which are set out in MiFID II and were essentially the brainchild of the FCA, have been the subject of much debate and consternation in the industry. MiFID II required research to be "unbundled" from transaction costs. Firms receiving research were required to either pay for research themselves or pass the cost on to clients as a separate charge, to ensure that clients had better price transparency. The FCA's review of the market, undertaken after MiFID II's commencement, found that firms now absorb the costs rather than pass them onto clients. However, concerns about the impact on research coverage and quality have led the FCA to propose the relatively limited changes described further below.

In addition, the FCA has found that the best execution related reporting requirements that were introduced by RTS 27 and 28 in MiFID II, are not helpful to market participants or investors when it comes to assessing best execution quality. Accordingly, the FCA is proposing to remove the RTS 27 and 28 obligations.

FCA'S PROPOSED CHANGES

At the EU level, changes to the investment research and best execution reporting rules have recently been implemented via what is known as the MiFID "Quick Fix". The FCA has spoken to UK market participants and considered similar issues to those dealt with by the "Quick Fix". The table below provides a summary comparison of the "Quick Fix" changes versus the changes the FCA is currently proposing under this consultation paper (CP 21/9):

FCA changes	EU "Quick Fix" changes
Research into SMEs below a market capitalisation of £200 million (for the 36 months preceding the research) exempt from the inducement / investment research rules	Research into SMEs below a market capitalisation of €1 billion (for the 36 months preceding the research) exempt from the inducement / investment research rules
Fixed Income, Currencies and Commodities research exempt from the inducement / investment research rules	No equivalent
Research provided by independent research firms (not engaged in execution services or part of a group that offers execution or brokerage services) exempt from the inducement / investment research rules	No equivalent
Research made openly available (e.g. not requiring a log-in, sign up or submission of user information) exempt from the inducement / investment research rules	No equivalent
Removal of obligation for execution venues to make RTS 27 reports (quarterly execution quality metrics)	Obligation to make RTS 27 reports suspended for two years from the end of February 2021
Removal of obligation for firms executing and transmitting client orders to make RTS 28 reports (annual report listing the top five execution venues where they have sent client orders in the preceding years, and a summary of the execution outcomes achieved)	No equivalent

While it is unsurprising that the FCA has chosen to divert from the EU's proposals and tailor the changes to the needs of the UK market, it does represent further regulatory fragmentation for firms operating across the UK and EU jurisdictions. It remains to be seen how many firms will take advantage of the FCA exemptions or whether they will find it administratively easier (and cheaper) to maintain one approach across both the EU and UK.

The consultation closes on 23 June 2021.

RELATED CAPABILITIES

- Financial Regulation Compliance & Investigations
- Investigations

MEET THE TEAM



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