

Safeguarding

6 October 2022

Speakers:

Shermeen Kazmi
Mduduzi Mswabuki
Luke Patterson

Today's speakers

Mduduzi Mswabuki - EY

Partner, Financial Services and Partner Sponsor

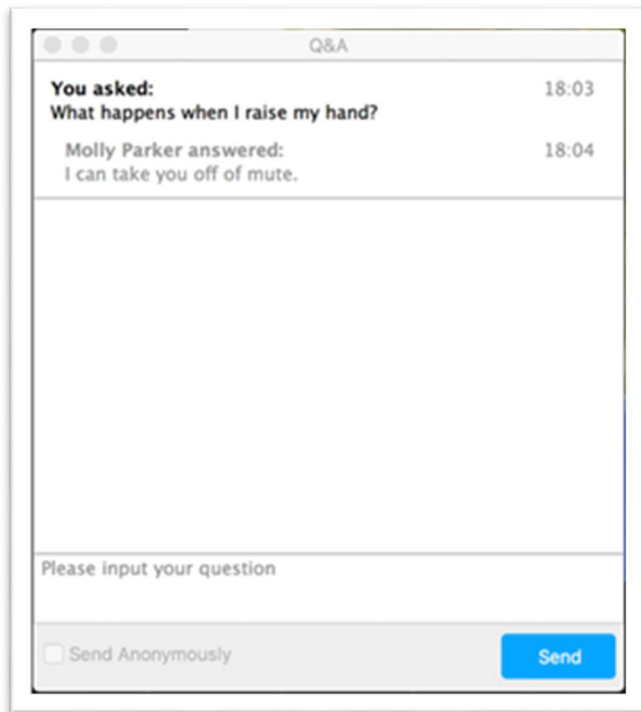
Shermeen Kazmi - Grant Thornton

Partner, Financial Services Audit

Luke Patterson - BDO

Partner, Financial Services Advisory and Safeguarding specialist.

Ask a question



The screenshot shows a Q&A interface with the following elements:

- Q&A** title bar
- You asked:** What happens when I raise my hand? 18:03
- Molly Parker answered:** I can take you off of mute. 18:04
- A large empty text input area with the placeholder text "Please input your question".
- A checkbox labeled "Send Anonymously" (unchecked).
- A blue "Send" button.

Click on the Q&A button in the bottom toolbar to open the submit question prompt.

Type in your question and click send.

Note. If you wish to ask anonymously tick the send anonymously box shown on the illustration to the left.



Payment/E Money Regulation Timeline to date

Mduduzi Mswabuki

Payment/E Money Regulation Timeline to date

Regulatory Developments

- ▶ Amendments to Payment Services and E-money Approach Document were published in November 2021 including updates on the on the following:
 - ▶ Expansion of institutions which can hold safeguarded funds
 - ▶ Disclosing information on treatment of funds on insolvency to customers
 - ▶ Due diligence
- ▶ Central Bank of Ireland (CBI) Published a Dear CEO letter in December 2021, setting out expectations for all Payments and E-money firms, and additionally the actions expected of Boards and senior managements to ensure the firm is in compliance, on an ongoing basis, with its regulatory requirements.

FCA Business Plan 2022/2023

We want make certain our 'ensuring consumer credit markets work well' and 'make payments safe and accessible' are in line with 'putting customer need first'

May 2022
Bank of England published consultation in relation to managing the failure of systemic digital settlement asset (including stablecoins) firms

December 2021
Central Bank of Ireland Dear CEO published to all payment and E-money firms

November 2021
Policy statement (PS21/19) issued on 29 November.

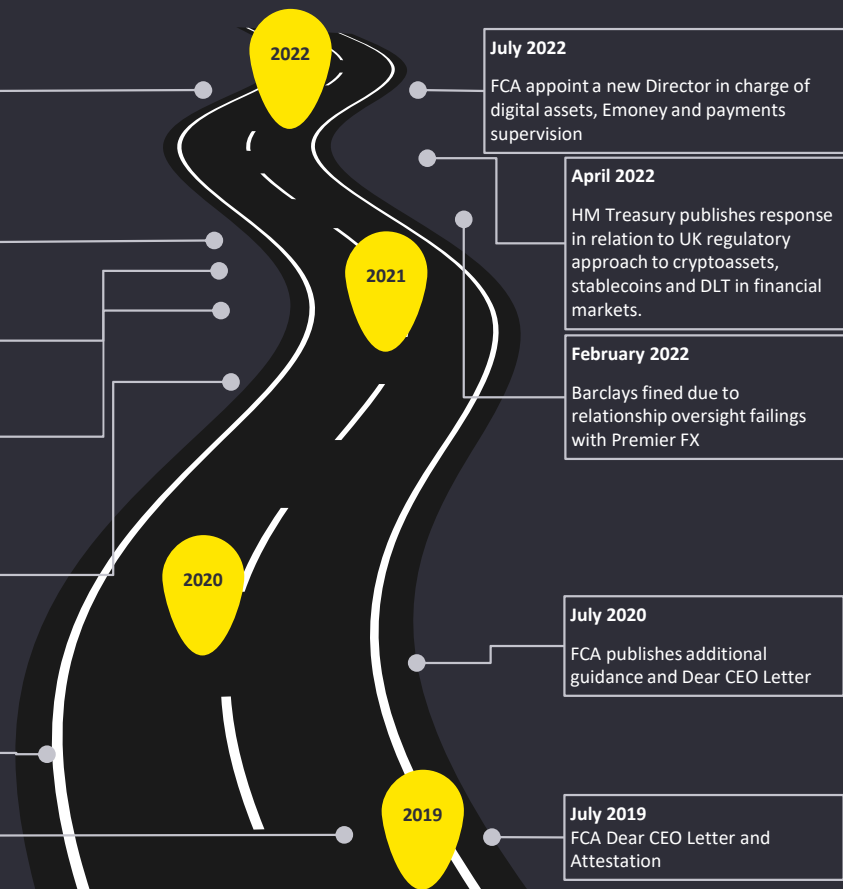
November 2021
The Payment and Electronic Money Institution Insolvency (England and Wales) Rules 2021 were released.

May 2021
the level of risk in the investment and loan activities undertaken by the third party¹

Dear CEO to all EMI firms to communicate to customers how their money is protected

May 2020
FCA publishes temporary guidance consultation

June 2019
FCA publishes updated Approach Document



July 2022
FCA appoint a new Director in charge of digital assets, E-money and payments supervision

April 2022
HM Treasury publishes response in relation to UK regulatory approach to cryptoassets, stablecoins and DLT in financial markets.

February 2022
Barclays fined due to relationship oversight failings with Premier FX

July 2020
FCA publishes additional guidance and Dear CEO Letter

July 2019
FCA Dear CEO Letter and Attestation

Safeguarding audit

Scope & requirements

Shermeen Kazmi



Applicability & Scope



Applicability of safeguarding rules

Required

- All authorised PIs
- All authorised EMIs
- Small EMIs
- A Credit Union that issue e-money
- EMIs and Credit Unions that provide unrelated payment services

Voluntary*

- Small PIs
- Small EMIs that provide unrelated payment services

***Principle 10 of the FCA' Principles for Businesses requires all firms, including small PIs to arrange adequate protection for clients' assets when they are responsible for them**

Safeguarding audit requirement



Authorised
payment
institution
(API)

A person authorised as a payment institution pursuant to the Payment Service Regulations

Electric
money
institution
(EMI)

A legal person that has been authorised to issue E-Money

Annual audit of compliance with safeguarding requirements

- The firm to arrange specific annual audits of its compliance with the safeguarding requirements under the PSRs/EMRs, if it is required to arrange an audit of its annual accounts under the Companies Act 2006
- These should be carried out by an audit firm, as referred to in regulation 24(2) of the PSRs or regulation 25(2) of the EMRs, or by another independent external firm or consultant
- Firms to exercise due skill, care and diligence in selecting and appointing auditors for this purpose. A firm should satisfy itself that its proposed auditor has, or has access to, appropriate specialist skill in auditing compliance with the safeguarding requirements under the PSRs/EMRs, taking into account the nature and scale of the firm's business

Safeguarding requirements



Overview

- Identification of Relevant funds
- Methods of safeguarding
- Systems and controls
- Reconciliations



Relevant Funds

PSR

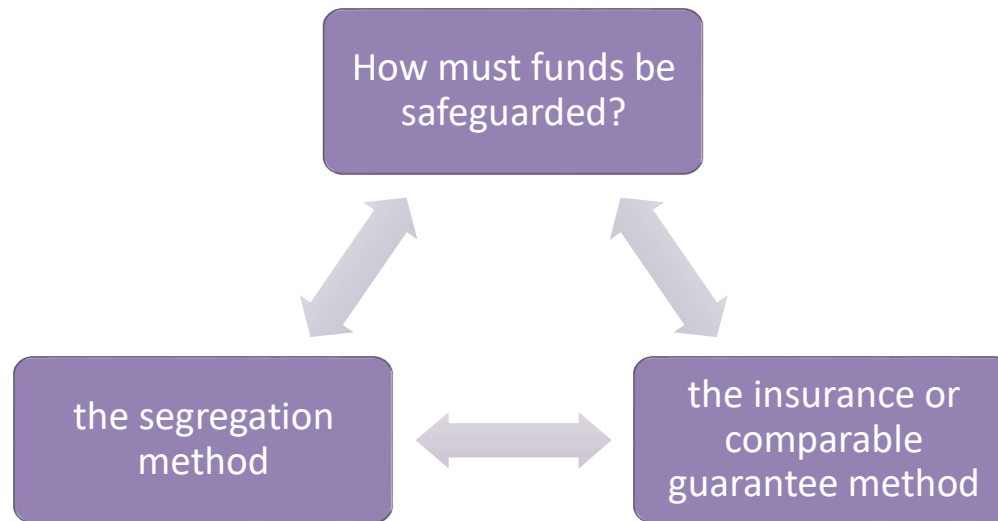
- sums **received from**, or for the benefit of, a payment service user **for the execution of a payment transaction**, and
- sums received from a payment service provider for the execution of a payment transaction **on behalf of** a payment service user

EMR

- funds that have been **received in exchange for electronic money that has been issued**
- funds received for payment services** (PS relevant funds), that are not related to the issuance of e-money, if the **EMI also provides unrelated payment services**

- Where;
 - ✓ **only a portion of the sums/funds** referred to in above paragraphs are to be used for the execution of a payment transaction (with the remainder being used for non-payment services); and
 - ✓ the precise portion attributable to the execution of the payment transaction **is variable or unknown in advance**, the relevant funds are such amount as may be **reasonably estimated, on the basis of historical data** and to the **satisfaction of the FCA/Authority**, to be representative of the portion attributable to the execution of the payment transaction (S.23.2 of PSR and S.21.3 of EMR)

Safeguarding methods



When does the obligation to safeguard start and end?

- The safeguarding obligation starts **as soon as the institution receives the funds**.
- The general principle is that the safeguarding obligation remains in place until the funds are **no longer held by the institution**, ie either paid out to the payee or the payee's PSP or other PSP (in case of chain of PSPs)

Systems and Controls

Institutions must maintain organisational arrangements that are sufficient to minimise the risk of the loss or diminution of relevant funds or assets through fraud, misuse, negligence or poor administration.

Institutions must have adequate internal control mechanisms, including sound administrative, risk management and accounting procedures, effective risk management procedures.

Institutions must take adequate measures to safeguard customer funds in addition to maintaining relevant records.

Arrangements that institutions should have in place include the following:

- **maintain clear and accurate records**
- **documenting the rationale** for every decision
- ensure an **appropriate individual** within the institution has **oversight of, and ensuring responsibility for ensuring compliance with, all procedures** relating to safeguarding and responsibility for ensuring that every aspect of the safeguarding procedure is compliant
- **exercise all due skill, care and diligence** in selecting, appointing and periodically (at least annually) reviewing credit institutions or custodians and insurers.
- Carry out both **internal and external reconciliations**.

Internal & External Reconciliations

Internal Reconciliation

An institution should carry out internal reconciliations of records and accounts of the entitlement of e-money holders/payment service users to relevant funds and assets with the records and accounts of amounts safeguarded.

External Reconciliation

An institution should regularly carry out reconciliations between its internal accounts and records and those of any third parties safeguarding relevant funds or assets. To check accuracy of its internal accounts and records against those of the third parties.

Safeguarding audit considerations



Safeguarding audit opinion

The auditor to provide an opinion addressed to the firm on:

- whether the firm has maintained organisational arrangements adequate to enable it to meet the FCA's expectations of its compliance with the safeguarding provisions of the EMRs/PSRs (as set out in chapter 10 of our Approach Document), throughout the audit period; and
- whether the firm met those expectations as at the audit period end date.

Reasonable Assurance Opinion

Key considerations

1. Auditing Standard

In the absence of a specific FRC standard, ISAE 3000 (Revised) 'Assurance Engagements Other Than Audits Or Reviews Of Historical Financial Information' could be applied.

2. Timing

Expectation is that work is completed as soon as reasonably practicable with no set timeframes defined. Firms may align the audit period with their accounts year end. Submission of report may be 4 months after the period end date

3. Nature of Opinion

"Type 2 – during the period and as at period end date report" to be issued.

4. Defining what constitutes FCA expectations

Current guidance on the safeguarding provisions of the EMRs and PSRs is set out in:

- chapter 10 of the Approach Document,
- letter dated December 2019 to firms' CEOs, and
- FCA's additional guidance published in July 2020.

Reporting by auditors and firms

Types of non-compliance audit firms should report:

Firm's auditor is required to tell the FCA if it has become aware in its capacity as an auditor, of a breach of any requirements imposed by or under the PSRs or EMRs that is of material significance to the FCA (regulation 25 of the EMRs and regulation 24 of the PSRs 2017)

Examples of the type of non-compliance requiring notification are:

- not keeping up to date records of relevant funds and safeguarding accounts
- where a firm cannot comply because a safeguarding credit institution has decided to close a safeguarding account

Types of non-compliance regulated firms should report:

The firm should notify the FCA in writing without delay if in any material respect it has not complied with or is unable to comply with the requirements in regulation 20 of the EMRs or regulation 23 of the PSRs

- Failure to keep up to date records of relevant funds & safeguarding accounts
- Inability to resolve reconciliation discrepancies
- The decision by an authorised credit institution or custodian to close a safeguarding account
- Failure to carry out reconciliation as frequently as appropriate

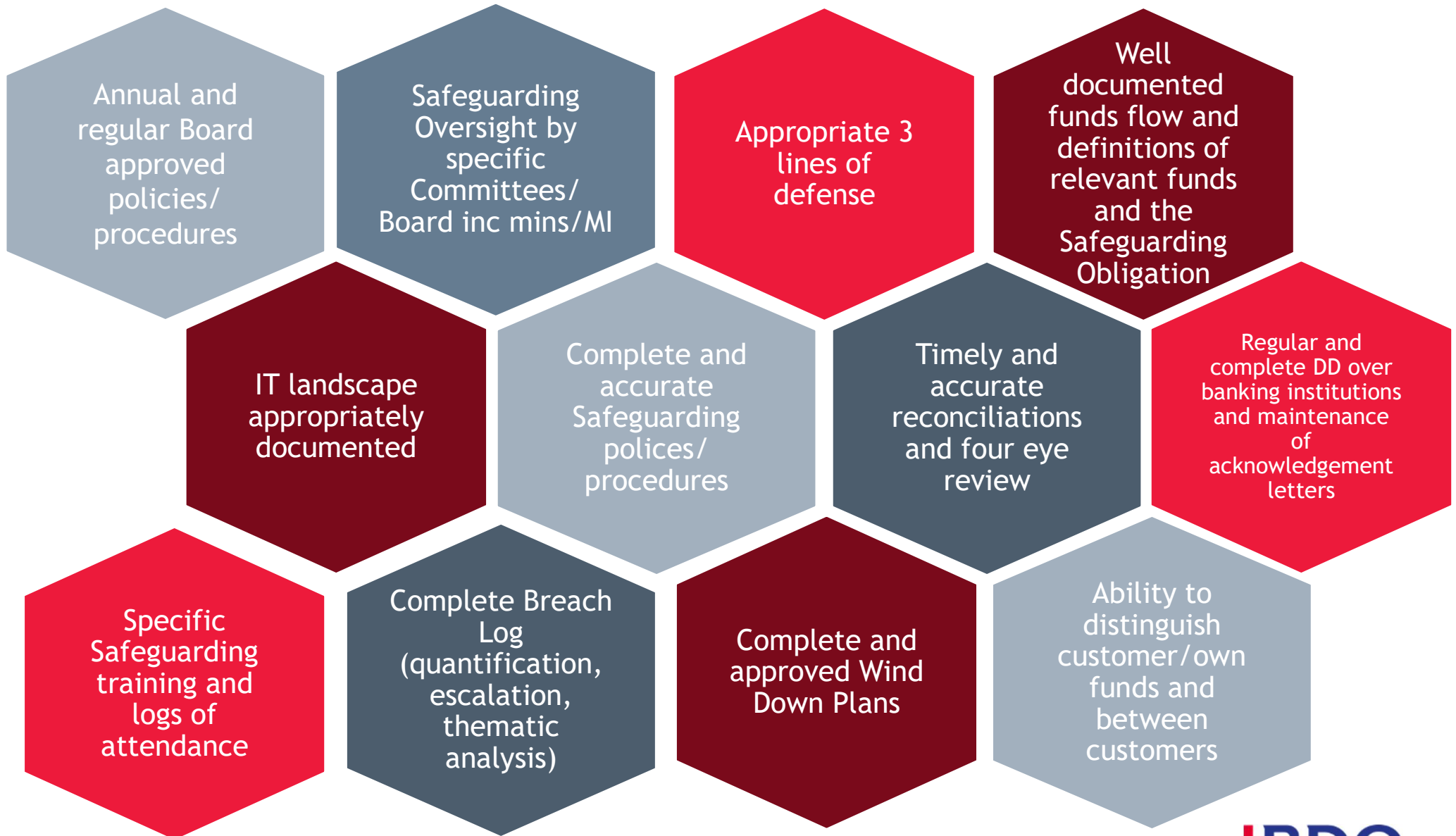


IDEAS | PEOPLE | TRUST

SAFEGUARDING BREACHES, FINDINGS AND COMMON THEMES

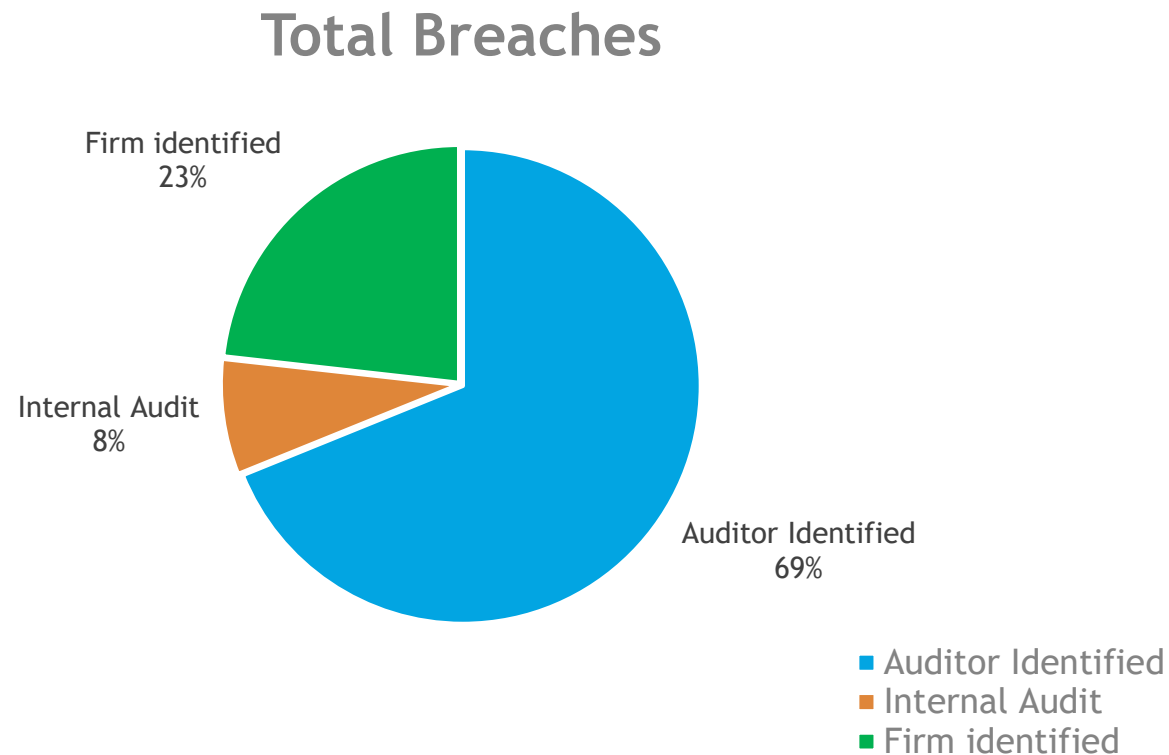
Luke Patterson, Partner

WHAT GOOD LOOKS LIKE?



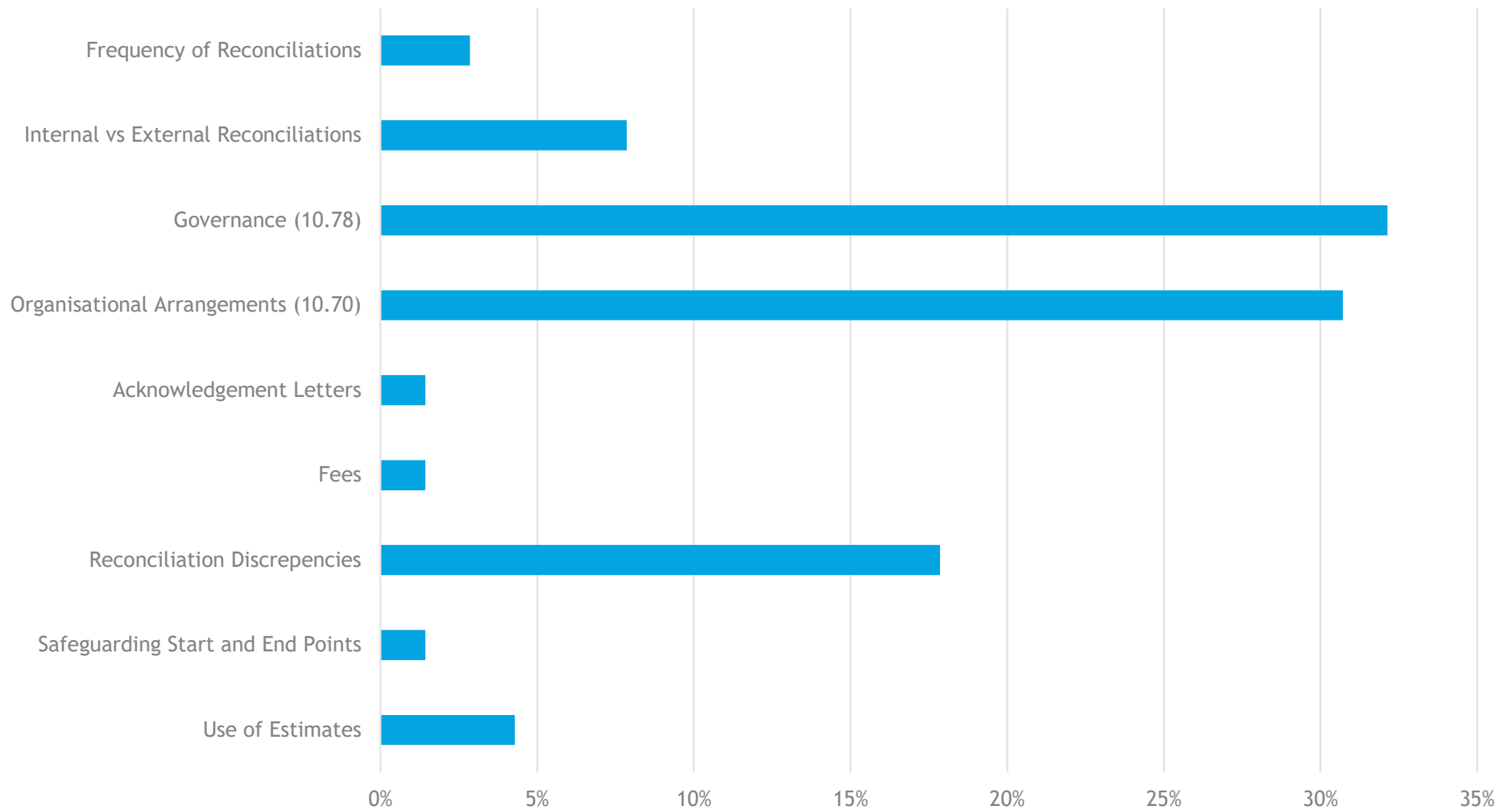
SAFEGUARDING TRENDS

- First year audits, increased occurrence of adverse opinions
- Lack of clean audit with multiple breaches identified
- Differences in output from audits
- Varying scope areas for audits



SAFEGUARDING TRENDS

Breach Trends



KEY MESSAGES

- Safeguarding is an increasing regulatory area of focus not just in the UK.
- UK is in advance of the rest of the world in regulatory oversight, however other territories increasing their focus, for example the CBI Dear CEO Letter issued in 2021 regarding Board Attestation of Safeguarding requirements.
- No firms are being given clean audit reports.
- Larger firms (PSR / EMI) are remediating first year audits and moving into second year.
- Smaller firms are developing their process and controls in this area and requirement for audit.
- Expectation of greater future regulatory scrutiny and monitoring.
- Firms are moving towards alignment to Firm's financial statement year end with reporting 4 months post year end.

QUESTIONS...

Thank you for attending

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