EXPLANATORY MEMORANDUM TO

THE FINANCIAL SERVICES ACT 2021 (OVERSEAS FUNDS REGIME AND RECOGNITION OF PARTS OF SCHEMES) (AMENDMENT AND MODIFICATION) REGULATIONS 2024

2024 No. 114

1. Introduction

1.1 This explanatory memorandum has been prepared by His Majesty's Treasury and is laid before Parliament by Command of His Majesty.

2. Purpose of the instrument

2.1 This SI supports the operationalisation of the Overseas Funds Regime (OFR), a new equivalence regime to recognise overseas funds under section 271A of the Financial Services and Markets Act (FSMA) 2000 (c. 8), which was legislated for in the Financial Services Act (FSA) 2021 (c. 22). This SI makes consequential amendments across the statute book to insert references to section 271A FSMA 2000. It also makes modifications to some of these new amendments and existing references to recognised funds where relevant, to ensure that such references account for recognised sub-funds - a commonly used structure whereby funds have an umbrella fund, under which different sub-funds sit, each with their own investment strategies.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Extent and Territorial Application

4.1 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is the same extent as the provision amended or modified.

4.2 The territorial application of this instrument (that is, where the instrument produces a practical effect) is the same application as the provision amended or modified.

5. European Convention on Human Rights

5.1 The Economic Secretary to the Treasury has made the following statement regarding Human Rights:

"In my view the provisions of the Financial Services Act 2021 (Overseas Funds Regime and Recognition of Parts of Schemes) (Amendment and Modification) Regulations 2024 are compatible with the Convention rights."

6. Legislative Context

6.1 The FSA 2021 introduced a new equivalence regime for overseas funds, the OFR, by amending FSMA 2000. The OFR provides a streamlined route for overseas funds to become recognised for the purposes of marketing to UK retail customers on a country or territorial basis, following an equivalence determination by HM Treasury.

6.2 This instrument serves to support the operationalisation of the OFR by making consequential amendments to provisions across the statute book to insert references to section 271A FSMA 2000, where such provisions refer to schemes recognised under section 272 FSMA 2000 (the route for individually recognising funds).

6.3 Many funds are structured with sub-funds, sitting underneath an umbrella fund, with the investment strategies being set out at the sub-fund level. By amending FSMA 2000, FSA 2021 provided for a power to modify legislative references to funds recognised under section 271A FSMA 2000 or section 272 FSMA 2000, to account for recognised sub-funds. It also set out that all such references within or contained in legislation made under Part 17 FSMA 2000, account for recognised sub-funds. This is important as recognition can take place at the sub-fund level and some sub-funds under an umbrella may be recognised and others may not be.

7. Policy background

What is being done and why?

7.1 Via this instrument, a number of legislative references to recognised schemes under section 272 FSMA 2000 are being amended so that they also refer to recognised schemes under section 271A FSMA 2000. Some references are also being modified to ensure that they capture recognised sub-funds. This will ensure that the OFR works as intended, as a streamlined route for overseas funds to market to UK retail investors.

7.2 The OFR is a new equivalence regime, which allows overseas funds from jurisdictions that are determined to be equivalent to the UK in terms of consumer protection, to market to UK retail investors following an application for recognition. It was legislated for in the FSA 2021 to provide a more streamlined route for overseas funds to be recognised and market in the UK, than the existing route in section 272 FSMA 2000, which requires an in-depth assessment of each individual fund by the FCA, before recognition is granted.

Explanations

What did any law do before the changes to be made by this instrument?

Rehabilitation of Offenders

7.3 The Rehabilitation of Offenders Act 1974 (Exceptions) Order 1975 (S.I. 1975/1023) makes exceptions to the operation of the Rehabilitation of Offenders Act 1974 (c. 53). Section 4(2) of the Rehabilitation of Offenders Act 1974 provides that when questions are asked about a person's previous convictions, offences, conduct or circumstances otherwise than in the course of judicial proceedings, the question shall be treated as not relating to spent convictions and the person shall not be subjected to liability by a failure to disclose such convictions. There is an exception, subject to certain conditions, so that section 4(2) does not apply when the FCA, the PRA or the relevant collective investment scheme, asks such questions of an associate of the operator or trustee of the relevant collective investment scheme. The term, "relevant collective investment scheme", is defined as only including schemes that are recognised under section 272 FSMA 2000.

7.4 Section 4(3)(b) of the Rehabilitation of Offenders Act 1974 provides that a failure by a person to disclose a spent conviction shall not be a proper ground for dismissing or excluding a person from any office, profession, occupation or employment, or

prejudicing them in any occupation or employment. Regulation 4(1)(d)(ix) of the Rehabilitation of Offenders Act 1974 (Exceptions) Order 1975 provides that this does not apply in relation to any decision made by the FCA, PRA or the Bank of England to refuse to make or to revoke an order declaring a collective investment scheme to be a recognised scheme under section 272 FSMA 2000.

7.5 The Rehabilitation of Offenders (Exceptions) Order (Northern Ireland) 1979 (S.R. & O. (NI) 1979 No. 195) and the Rehabilitation of Offenders Act 1974 (Exclusions and Exceptions) (Scotland) Order 2013 (S.S.I. 2013/50) addresses related or comparable issues by way of exceptions with regards to the Rehabilitation of Offenders (Northern Ireland) Order 1978 (S.R. & O. (NI) 1978 No. 1908) and the Rehabilitation of Offenders Act 1974, respectively.

Local Authorities Capital Finance and Accounting

7.6 The Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 (S.I. 2003/3239 (W.319)) set out that what would otherwise be treated as capital expenditure by a local authority with regards to the acquisition of share capital in any body corporate, shall not be if it is in an investment in a money market fund. In addition, where a local authority invests in a money market fund, any fair value gain or loss must not be charged to a revenue account and instead should be charged to an account established solely for the purposes of recognising such fair value gains or losses (excluding impairment losses or a sale or other disposals in relation to the authority's investment in the money market fund). In these regulations, the definition of a "money market fund" covers schemes recognised under Part 17 FSMA 2000, which now includes those recognised under section 271A FSMA 2000, as well as section 272 FSMA 2000.

Financial Promotions

7.7 Section 21 FSMA 2000 sets out a restriction that provides that financial promotions can only be communicated by authorised persons or those who have had their communication approved by an authorised person, or where an exemption applies. Article 40 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (S.I. 2005/1529) provides an exemption to this restriction with regards to non-real time communications or solicited real time communications made by operators of schemes recognised under section 272 FSMA 2000, to the participants of and in relation to such schemes.

Packaged Retail and Insurance-based Investment Products

7.8 Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPS) sets out requirements on key information documents for packaged retail and insurance-based investment products (PRIIPS). It provides that EEA UCITS funds recognised under section 272 FSMA 2000 must provide to UK investors the UCITS Key Investor Information Document (KIID).

Why is it being changed?

7.9 As necessary, these areas of legislation are being changed to additionally refer to funds recognised under section 271A FSMA 2000 or are being modified to be read as also applying to sub-funds recognised under either section 271A or section 272 FSMA 2000. By making these changes, funds recognised under section 271A FSMA 2000

will be treated in the same way as funds recognised under section 272 FSMA 2000, which otherwise would undermine the intent of the regime. Furthermore, these changes make clear that such legislative provisions also apply to recognised sub-funds, which is important as it is common for funds to be structured with sub-funds.

What will it now do?

Rehabilitation of Offenders

7.10 Within the Rehabilitation of Offenders Act 1974 (Exceptions) Order 1975, the exception relating to questions asked by the FCA, PRA, or the relevant collective investment scheme of an associate of the operator or trustee of the relevant collective investment scheme will be expanded, so that the definition of the term "relevant collective investment scheme" will also include recognised schemes under section 271A FSMA 2000. As a result, associates of the operator or trustee of section 271A FSMA 2000 schemes will be subject to liability when asked relevant questions by the FCA, PRA or relevant collective investment scheme, if they fail to disclose spent convictions. Furthermore, the exception in relation to decisions made by the FCA, PRA or the Bank of England to refuse to make or to revoke an order declaring a collective investment scheme to be a recognised scheme, will be expanded to also include section 271A FSMA 2000 schemes. As a result, a failure to disclose a relevant spent conviction in relation to such decisions for section 271A FSMA 2000 schemes, will be a proper ground for dismissing or excluding a person from any office, profession, occupation or employment, or prejudicing them in any occupation or employment. Modifications will also ensure that these exceptions apply in relation to sub-funds that are recognised under either section 271A or section 272 FSMA 2000.

7.11 Changes with regards to related or comparable issues will be made to the Rehabilitation of Offenders (Exceptions) Order (Northern Ireland) 1979 and the Rehabilitation of Offenders Act 1974 (Exclusions and Exceptions) (Scotland) Order 2013.

Local Authorities Capital Finance and Accounting

7.12 In the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003, a modification will be made to ensure that sub-funds recognised under section 271A or section 272 FSMA 2000 are captured within the definition of "money market fund".

Financial Promotions

7.13 The exemption for operators of section 272 FSMA 2000 recognised schemes within Article 40 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, will be extended to also apply to operators of schemes recognised under section 271A FSMA 2000. A further modification will also be made to ensure that this exemption applies with regards to sub-funds that are recognised under section 271A or section 272 FSMA 2000. As a result, the financial promotion restriction will not apply where an operator of a scheme or sub-fund, that is recognised under section 271A or section 272 FSMA 2000, markets to investors of such a scheme or sub-fund, about any recognised scheme or sub-fund that the operator also operates.

Packaged Retail and Insurance-based Investment Products

7.14 Regulation (EU) No 1286/2014 will be amended so that EEA UCITS that are recognised under section 271A FSMA 2000 are treated in the same way as section 272 FSMA 2000 schemes, in terms of disclosure. This will mean that schemes recognised under section 271A FSMA 2000 will be required to provide the UCITS KIID.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union.

9. Consolidation

9.1 This instrument does not consolidate any areas of legislation.

10. Consultation outcome

10.1 No public consultation was undertaken for this statutory instrument as a full consultation was run in advance of the OFR and the provisions with regards to recognised sub-funds, being legislated for. This consultation and the Government's response can be found at: https://www.gov.uk/government/consultations/overseas-funds-regime-a-consultation. This instrument serves to operationalise that regime.

10.2 Northern Irish, Scottish and Welsh administrations were consulted on the relevant devolved legislation to be amended or modified by this SI, which they agreed with.

11. Guidance

11.1 Guidance is not required.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 A full Impact Assessment has not been prepared for this instrument because this measure is extremely unlikely to have any impact on business or public services. There are currently no funds marketing under the OFR and so amendments to include references to section 271A FSMA 2000, along with relevant modifications so that such new references also account for sub-funds recognised under section 271A FSMA 2000, will have no practical impact.

12.4 Although there are funds marketing under section 272 FSMA 2000, the modifications to ensure references to funds recognised under section 272 FSMA 2000 also account for sub-funds recognised under section 272 FSMA 2000, are also unlikely to have any practical impact. This is because these modifications are intended to provide greater legal certainty on this point and in any event, there are a very small number of section 272 FSMA 2000 funds. If it has any effect at all, this modification would only affect the 44 section 272 FSMA 2000 sub-funds.

13. Regulating small business

13.1 The legislation may apply to activities that are undertaken by small businesses. However, as set out above, this legislation is unlikely to have any practical impact.

14. Monitoring & review

14.1 The approach to monitoring of this legislation is to continue to engage with the asset management sector, the Financial Conduct Authority and relevant other government departments to understand any impact.

14.2 The instrument does not include a statutory review clause and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015 (c. 26) the Economic Secretary to the Treasury has made the following statement:

"It would be disproportionate to include a statutory review clause in this legislation as it does not introduce additional regulatory burdens on businesses."

15. Contact

15.1 Matilda Embling at His Majesty's Treasury Email: Matilda.embling@hmtreasury.gov.uk can be contacted with any queries regarding the instrument.

15.2 Anna Harvey, Deputy Director for Personal Finances and Funds, at His Majesty's Treasury can confirm that this Explanatory Memorandum meets the required standard.

15.3 Bim Afolami, Economic Secretary to the Treasury, can confirm that this Explanatory Memorandum meets the required standard.