

# ALLEN & OVERY

## FCA Enforcement Themes and Trends

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February 2020

# What we will cover this morning

**A look back at  
2018/19**

**FCA  
investigation  
styles and  
methods**

**Culture,  
governance  
and individual  
accountability**

**Financial  
crime**

**Competition**

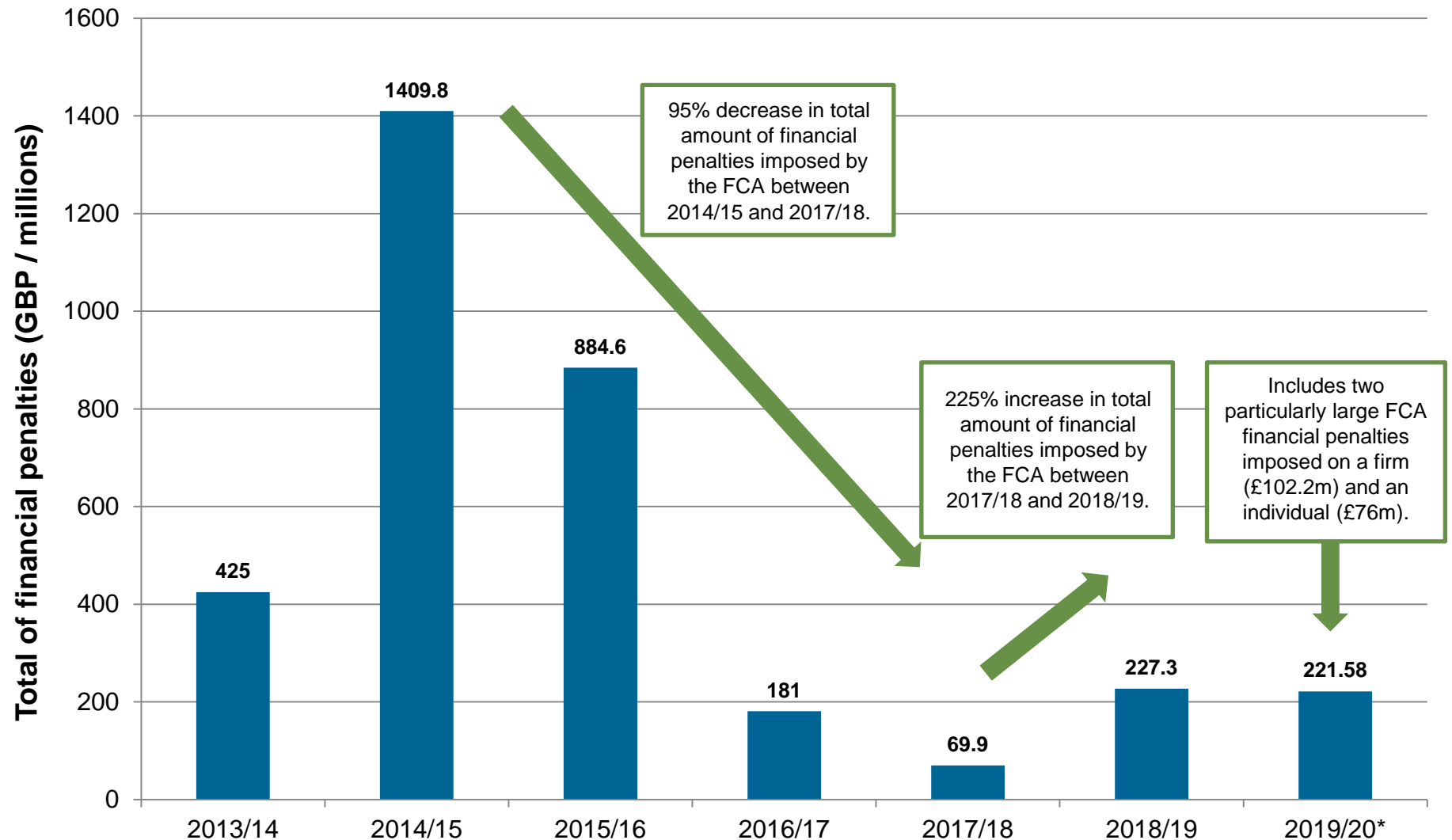
**Market abuse**

**Operational  
resilience:  
cyber and  
data security**

**Predictions  
for 2019/20  
and beyond**

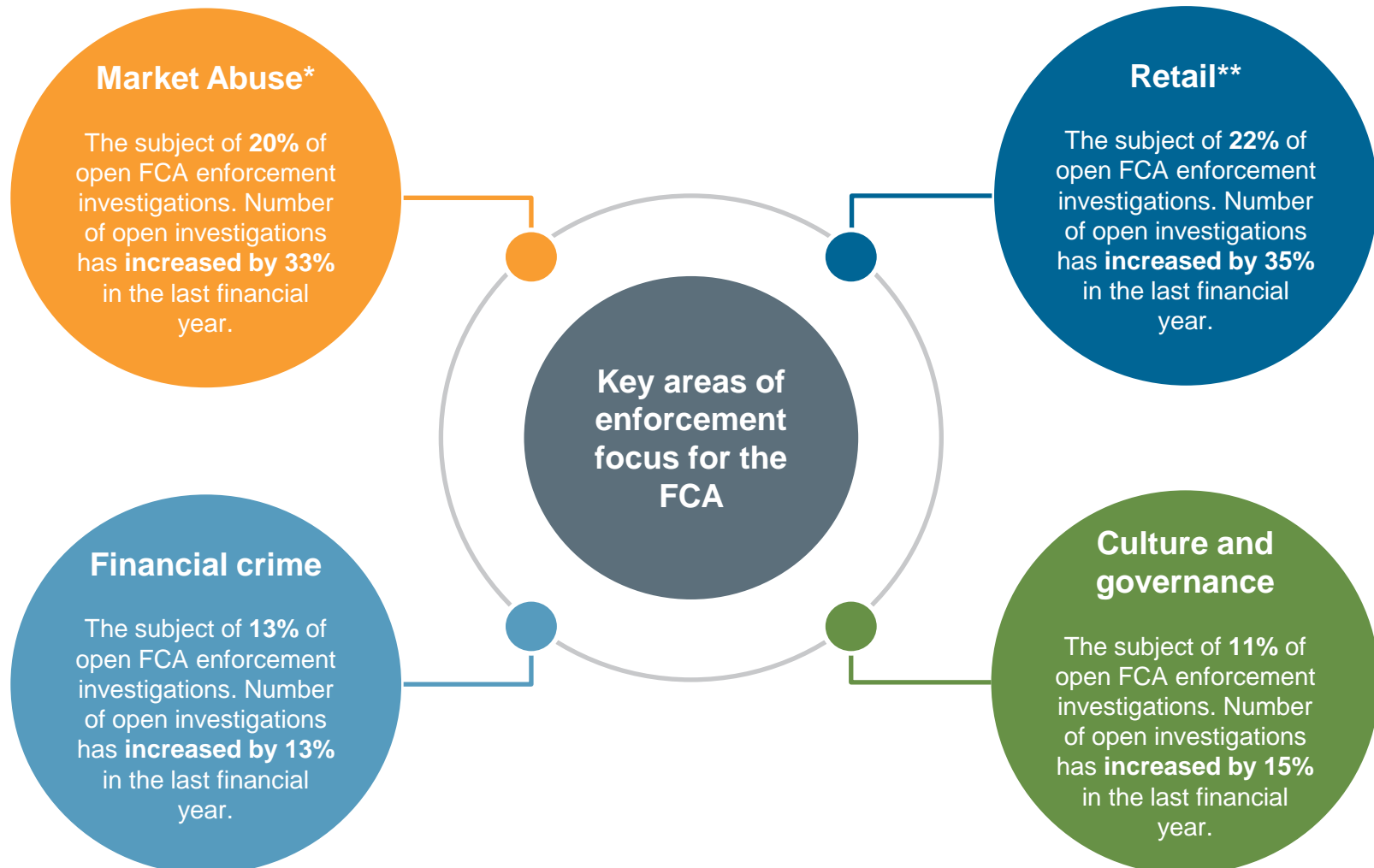
*A look back at 2018/19*

# FCA financial penalties: On the rise (again)?



Sources: FCA website and Annual Reports | \* As at 2 February 2020

# The FCA has increased its number of open enforcement investigations across all categories



Source: FCA Annual Reports. All figures as at 31 March 2019 | \* Includes insider dealing and market manipulation investigations | \*\* Includes mis-selling and financial promotions investigations | Further detail about the FCA's current investigation portfolio is included in an Appendix to these slides.

# *FCA investigation styles and methods*

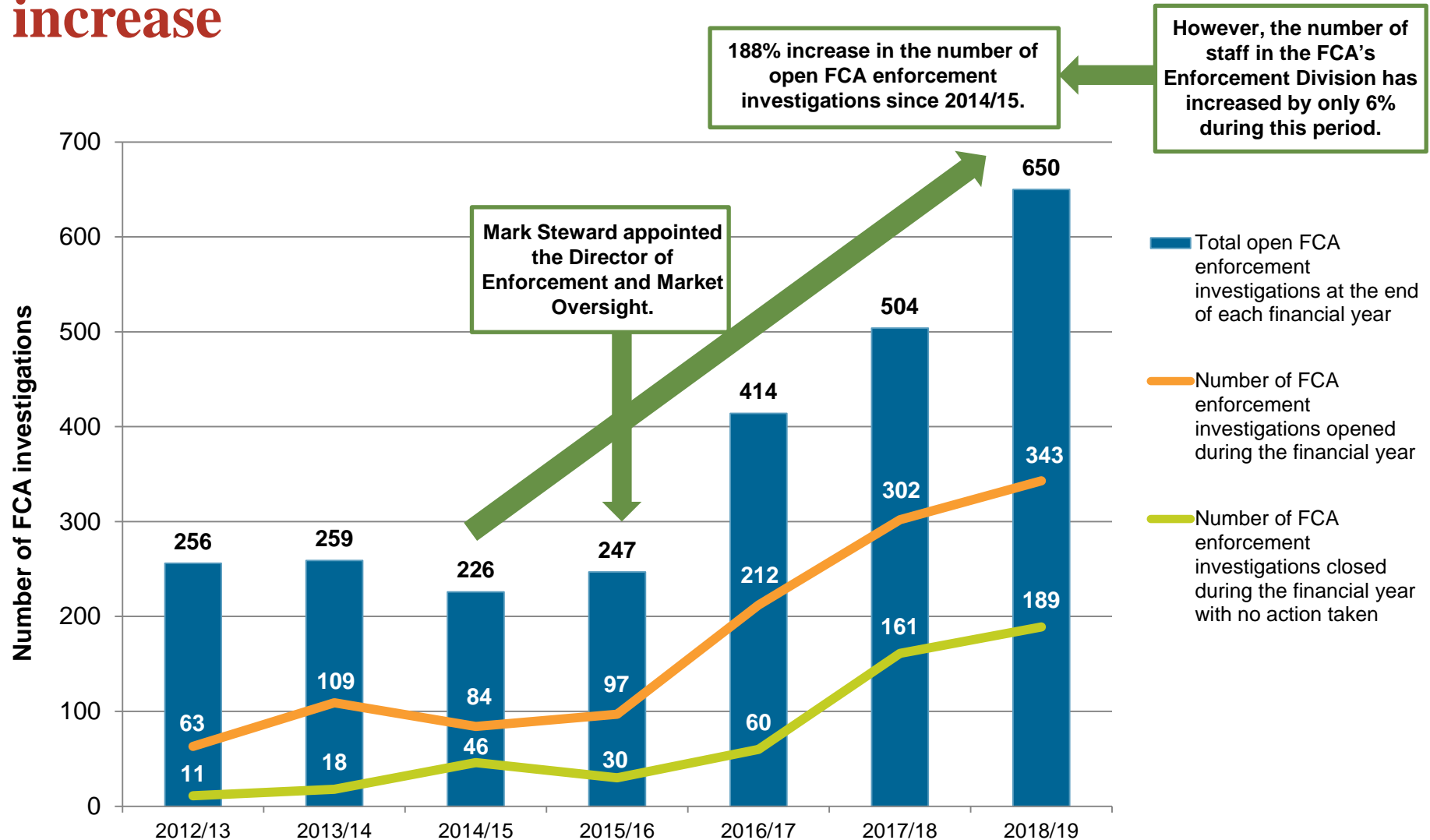


# The FCA published new enforcement referral criteria in April 2019

## The FCA

- ‘The purpose of an FCA investigation is to find out whether **serious misconduct** has occurred and get a full **understanding of the facts**, so that we can **decide whether to take action** and, if so, what kind of action may be necessary’.
- ‘We will start an... investigation where we **have reason to believe serious misconduct may have taken place** (i.e. where there is suspected serious misconduct). This means that we may investigate at an early stage’.
- ‘The opening of an investigation **does not mean we believe misconduct has occurred** or that anyone involved in the investigation is necessarily guilty of misconduct’.
- Focus on the concept of ‘**foreseeability**’, i.e. was it foreseeable that a breach could occur, or should it have been foreseeable.

# The number of open FCA investigations continues to increase



Sources: FCA Annual Reports and Freedom of Information Act request.



# The FCA is starting to reduce the time it takes to conclude most of its enforcement investigations

**17.5 months**

Average length of all investigations (including those discontinued with no action taken).

Decreased by 8.3% (1.6 months) from 2017/18.

At its lowest level since the FCA was established.

**29.1 months**

Average length of cases settled prior to a referral to the FCA's RDC.

Decreased by 9.9% (3.2 months) from 2017/18.

Still 9.5 months (48.4%) longer than in 2012/13.

**50.8 months**

Average length of cases settled after a decision is reached by the FCA's RDC.

Decreased by 14.5% (8.6 months) from 2017/18.

Still 13 months (34.3%) longer than in 2012/13.

**74.1 months**

Average length of cases that are concluded following an Upper Tribunal judgment.

Increased by 34.4% (21.7 months) from 2017/18.

Still 24 months (47.9%) longer than in 2012/13.

Sources: FCA Annual Reports. All figures as at 31 March 2019.

# Self-reporting and co-operation remain key enforcement focus for the FCA

Since 2013, the FCA and the PRA have imposed £256.9 million in financial penalties for breaches relating to failures to self-report and lack of co-operation.



Notifying the FCA of matters involving overseas regulators/authorities that they would expect notice of.



Ensuring that notifications to the FCA are sufficiently fulsome, clear and sign-posted, especially when updates about multiple matters are being provided.



Ensuring the accuracy of information that is provided to the FCA, including using appropriate caveats and clarifying the basis upon which questions are being answered.



If information requested by the FCA is not available or may take time to retrieve, ensuring that clear and accurate explanations on these points are provided.



Correcting the FCA if they appear to have misunderstood or misinterpreted information that has previously been provided to them.



Keeping the FCA up-to-date about matters as they develop and the accuracy and timeliness of those updates.

# The FCA has concluded three investigations that have involved Focused Resolution Agreements



The three cases involved firms and concerned findings relating to misselling, financial crime and market abuse systems and controls.



All three cases involved the firms challenging the FCA's proposed financial penalty. The facts and breaches in each case were agreed.



Two of the three cases settled after the RDC issued its decision. The third case was referred by the firm to the Upper Tribunal.



The RDC appears to have reduced the financial penalty proposed by FCA Enforcement in at least one of the three cases. The amount of the reduction is not known.



The RDC has taken on average 2.75 months to handle cases that are the subject of Focused Resolution Agreements (compared to its average of 11 months for all cases it considers).

# *Culture, governance and individual accountability*

# Culture remains a key focus for the FCA and underpins much of its enforcement work



Sources: FCA Annual Reports | FCA Final Notices | Various FCA speeches.

# The FCA is focusing on governance issues as part of broader investigations into other issues



Internal escalations to key individuals and committees.



Consideration of issues by committees and collective decision-making.



Delays associated with internal decision-making and escalations.

# The FCA continues to pay considerable attention to firms' internal whistleblowing arrangements



Most firms have adequate whistleblowing arrangements. But are firms over-complicating things and '*blurring the lines between day-to-day healthy challenge and [a] specific whistleblowing channel*'?



Some firms' messaging around how they expect their employees to 'speak up' has been described by the FCA as being '*too strident*'.



Continued challenges in deciding which issues should be directed to a whistleblowing channel and which issues can be dealt with through other mechanisms.



Firms have reported significant increases in whistleblowing allegations, especially in relation to non-financial misconduct.



Since March 2016, the FCA has received four complaints that concern the actions of one or more Whistleblowing Champion(s). It has received a total of 19 disclosures from whistleblowers about firms' compliance with whistleblowing controls.

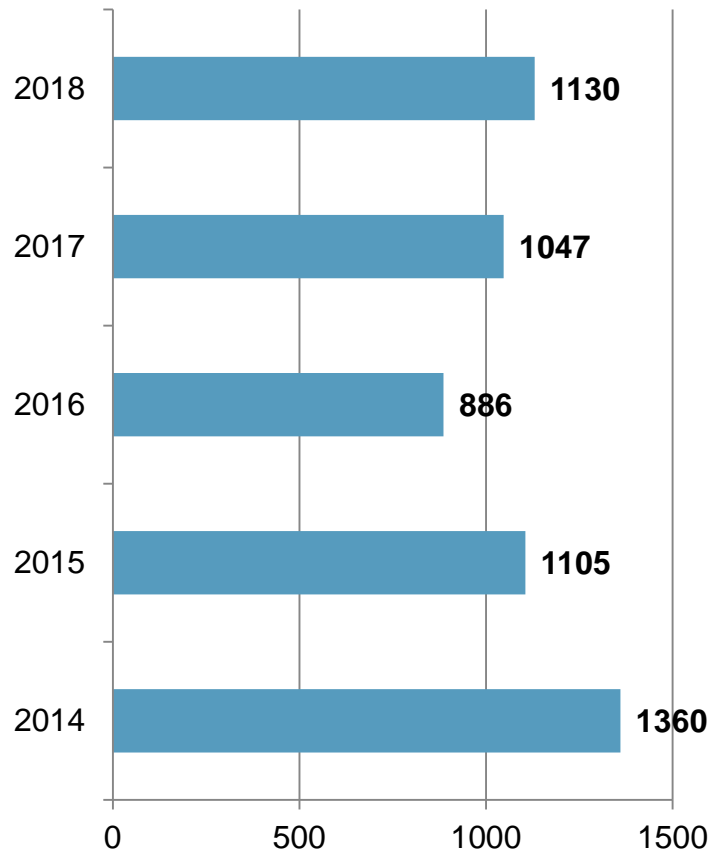


More questions being asked about how firms are ensuring that whistleblowers are not being subjected to detriment, not just in the immediate future but in the longer term.

Source: FCA Report: 'Progress and challenges: 5 Conduct Questions – Industry Feedback for 2018/19' (May 2019).



# The FCA continues to receive relatively steady numbers of whistleblowing allegations



Number of whistleblowing allegations received by the FCA each calendar year

28% of whistleblowing allegations received by the FCA were made on an anonymous basis.

The FCA has received most whistleblowing allegations about fitness and propriety (18%), culture (12%), consumer detriment (11%) and systems and controls (10%).

Recent increases in allegations made about sexual harassment, financial crime and whistleblowing controls.

The FCA can refer allegations it receives to other authorities, including HMRC, the ICO and the NCA, as well as overseas regulators and authorities.

Only 2% of whistleblowing allegations contributed directly to FCA enforcement or consumer protection activity. A further 20% of whistleblowing allegations were of 'significant value' to the FCA.

Source: Freedom of Information Act request submitted to the FCA. Information as at May 2019.

# Increased FCA focus on ‘non-financial misconduct’

“

*...we have seen a noticeable upturn in reports which concern issues like discrimination and sexual harassment in financial services. Our message to firms is clear: non-financial misconduct is misconduct, plain and simple.*

”

“

*Non-financial misconduct is an inherent risk in any industry. Serious misbehaviour is toxic to a working environment and can lead to bad outcomes for customers, staff, other stakeholders and the firm. This area clearly requires management attention and a broader change in firms' mindsets.*

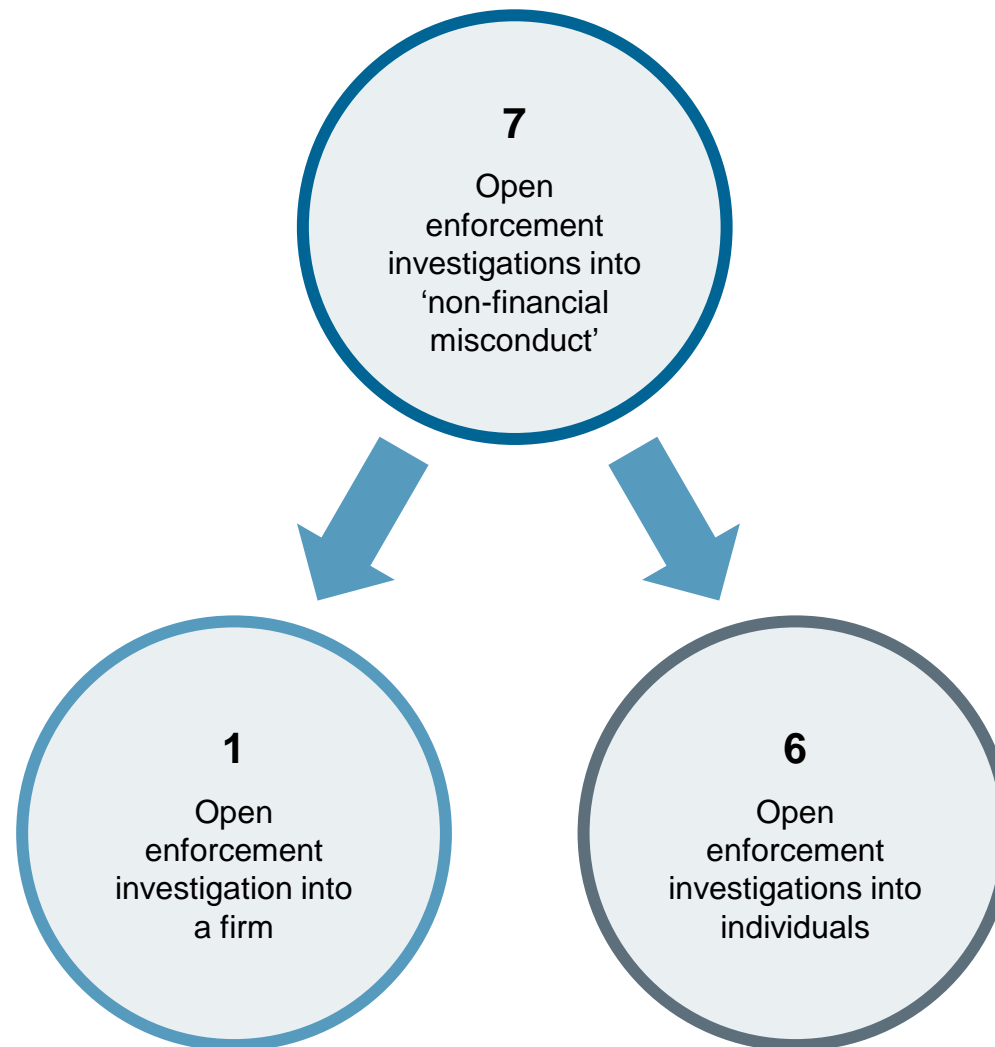
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Includes sexual misconduct, harassment, bullying, discrimination, favouritism, exclusion and intimidation.

The FCA has expressed concerns about the adequacy of firms' efforts to identify this kind of misconduct as part of their conduct risk programmes, as well as the adequacy of firms' responses to allegations of non-financial misconduct when they are raised.

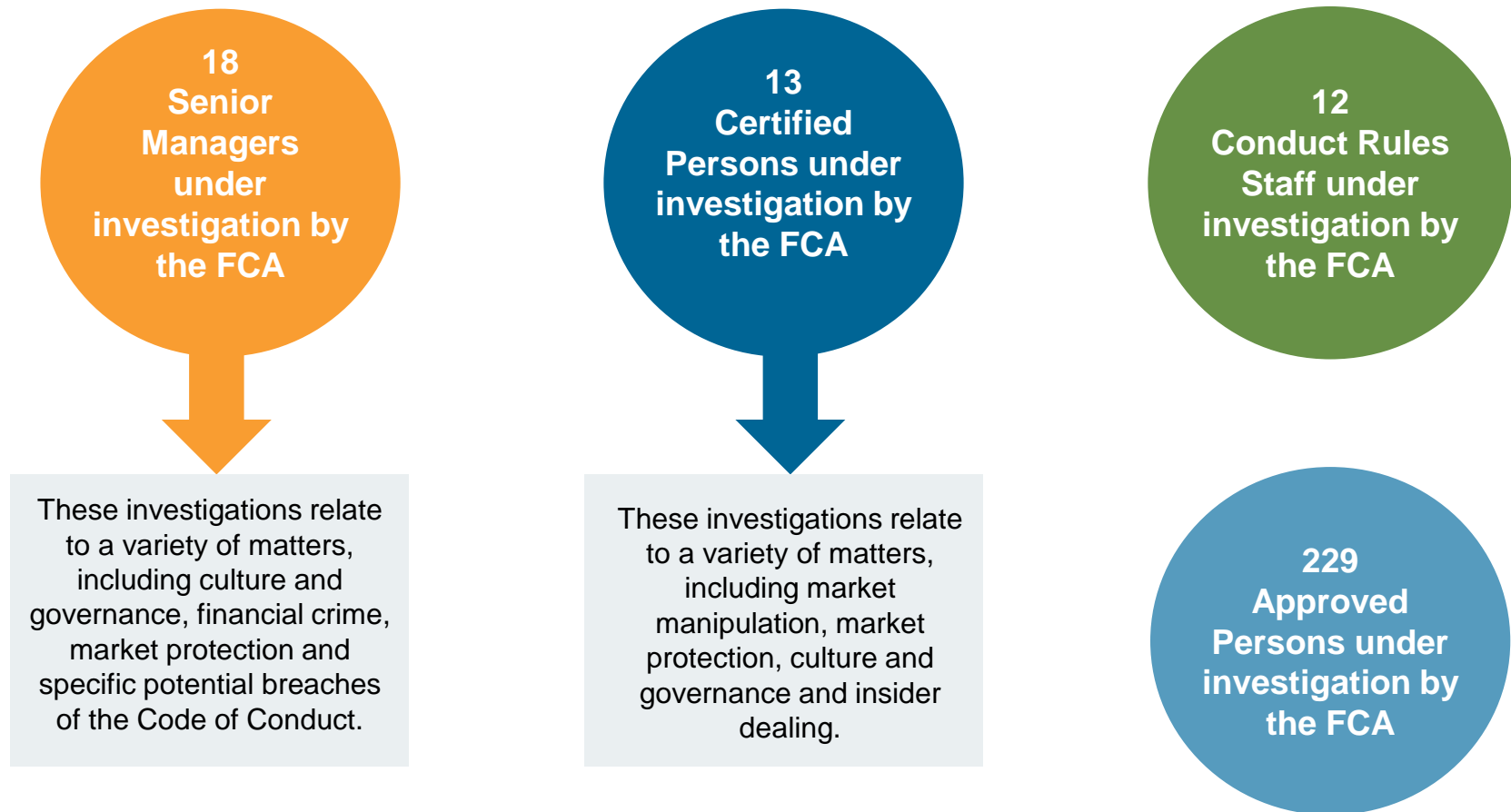
Sources: FCA Speech 'Opening up and speaking out: diversity in financial services and the challenge to be met', Christopher Woolard | FCA Report: 'Progress and challenges: 5 Conduct Questions – Industry Feedback for 2018/19' (May 2019).

# FCA enforcement activity in relation to 'non-financial misconduct'



Sources: Freedom of Information Act request submitted to the FCA

# Investigations into individuals\* represent approx. 41%\*\* of all current FCA enforcement investigations

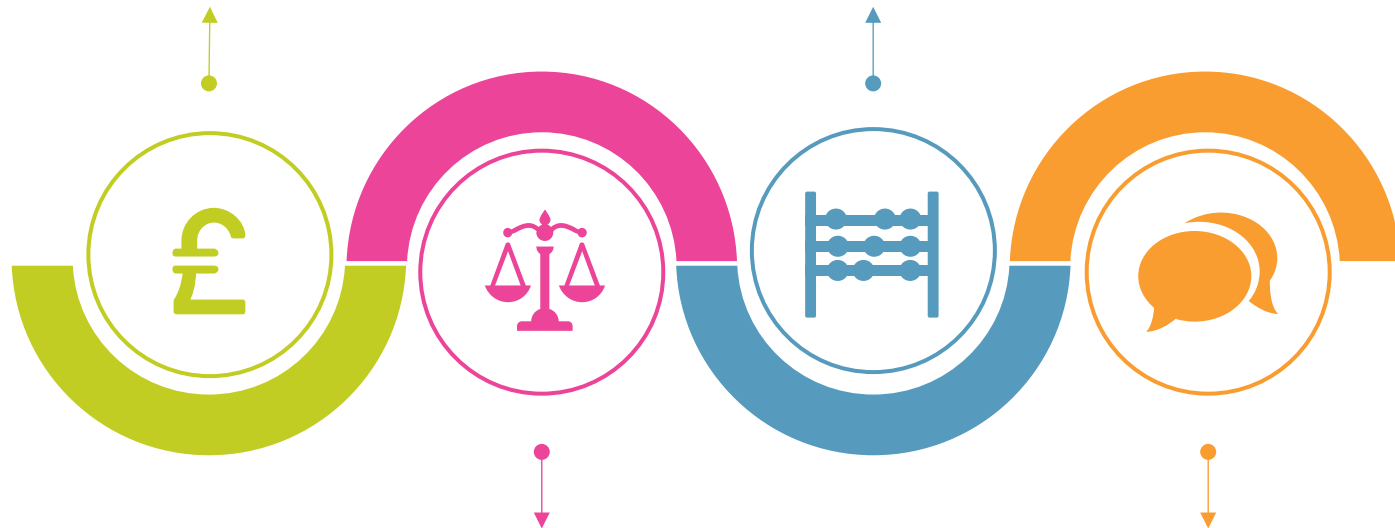


Sources: Freedom of Information Act request submitted to the FCA | \* This figure includes FCA enforcement investigations into Senior Managers, Certified Persons, Conduct Rule Staff and approved persons. It does not include FCA enforcement investigations into other individuals | \*\* Information as at October 2019.

# The FCA has identified areas for improvement in relation to remuneration policies

Proportionality of and link between rewards or penalties for conduct is *'patchy'*.

*'Limited'* evidence of malus or clawback provisions being exercised.

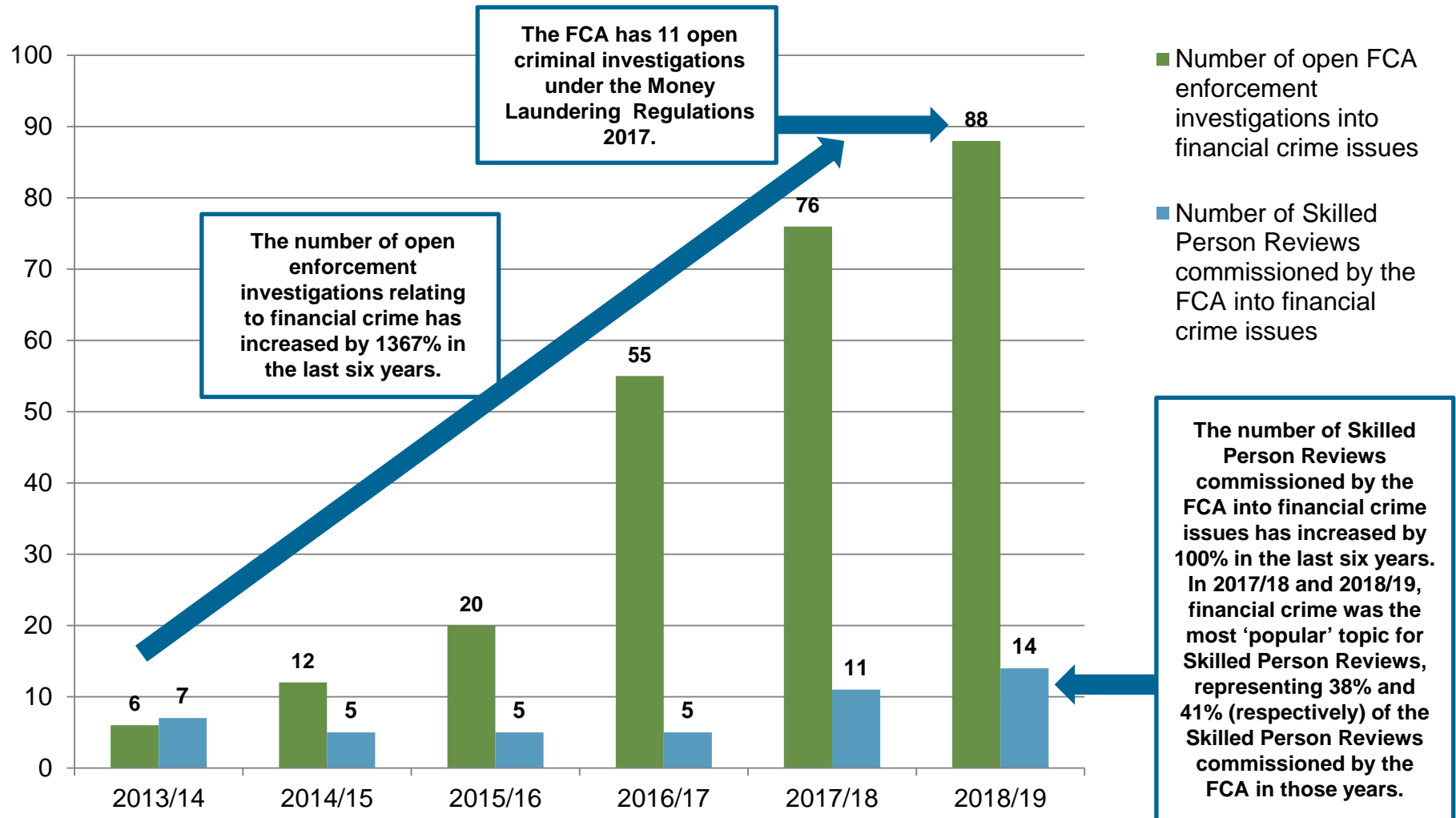


Weighting of conduct element of remuneration remains *'modest'*.

Inconsistency with which control functions can make *'meaningful'* input into remuneration decisions.

# *Financial crime*

# The FCA's focus on financial crime is reflected in its open investigations and Skilled Person reviews



Sources: FCA Annual Reports | FCA website | Freedom of Information Act Requests submitted to the FCA.



# Criminal investigations under the Money Laundering Regulations: Not a ‘white elephant’

“

*I have been asked to say something about the Money-Laundering investigations given we are now conducting ‘dual track’ AML investigations, i.e. investigations into suspected breaches of the Money-Laundering Regulations that might give rise to either criminal or civil proceedings.*

*I don’t think there should be anything controversial here. It would be **inconsistent with the investigative mindset to narrow the scope of potential outcomes** provided for by the law before you have made any inquiries or been able to assess the nature of the matter under investigation. Moreover, this practice **brings AML investigations into line with the FCA’s practice in market abuse investigations** which have been conducted on a ‘dual track’ basis for many years as well. More importantly, I think it is **time that we gave effect to the full intention of the Money-Laundering Regulations** which provides for criminal prosecutions [...]*

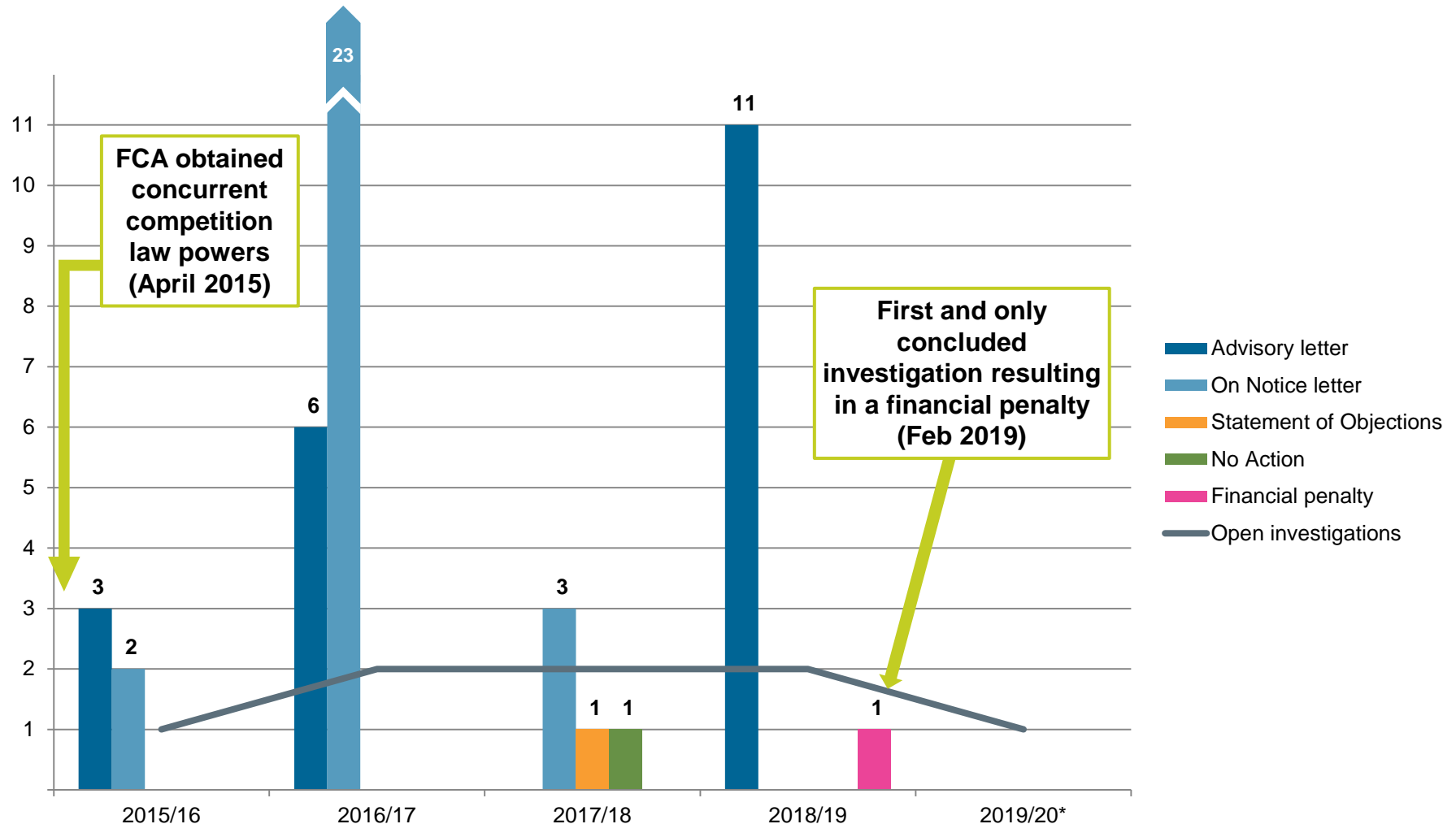
*This does not mean every investigation where we think there is a case to answer will or should be prosecuted in this way. I suspect **criminal prosecutions, as opposed to civil or regulatory action, will be exceptional**. However, we **need to enliven the jurisdiction** if we want to ensure it is not a white elephant and that is what we intend to do where we find **strong evidence of egregiously poor systems and controls and what looks like actual money-laundering**.*

”

Source: FCA speech ‘Partly contested cases, the pipeline and AML investigations’ delivered by Mark Steward, Director of Enforcement and Market Oversight (April 2019).

# *Competition*

# Limited enforcement activity by the FCA under its concurrent competition law powers



Source: FCA Competition Annual Report 2018/19 and Freedom of Information Act request submitted to the FCA by Allen & Overy | \* As at September 2019  
Information about the FCA's market studies portfolio is included in an Appendix to these slides.

## Competition enforcement may still be carried out by the CMA and in parallel to FSMA investigations

“

*On 13 November 2018, the CMA launched an investigation into suspected anti-competitive arrangements in the financial services sector...*

CMA Press Release, November 2018

”

“

*Our power to investigate breaches of the Competition Act 1998 may be used at the same time as our powers to investigate under FSMA and may give rise to evidence of other breaches which may be the subject of enforcement action under FSMA.*

FCA Mission: Approach to Enforcement, April 2019

”

# One concluded investigation relating to sharing of strategic information in the asset management sector



Sharing of '**strategic information**' (bidding intentions) between asset management firms during an initial public offering and a placing shortly before share prices were set



**Concerted practice** constituting a **by object** infringement, so no concluded agreement and the FCA did not need to examine whether there was any actual effect on the market



Strategic information defined as a *statement of intention by which a competitor eliminates or **substantially reduces uncertainty** as to its conduct on the market*



Burden on recipient to rebut **presumption that strategic information is acted on** (even where unsolicited) if recipient remains active in the market



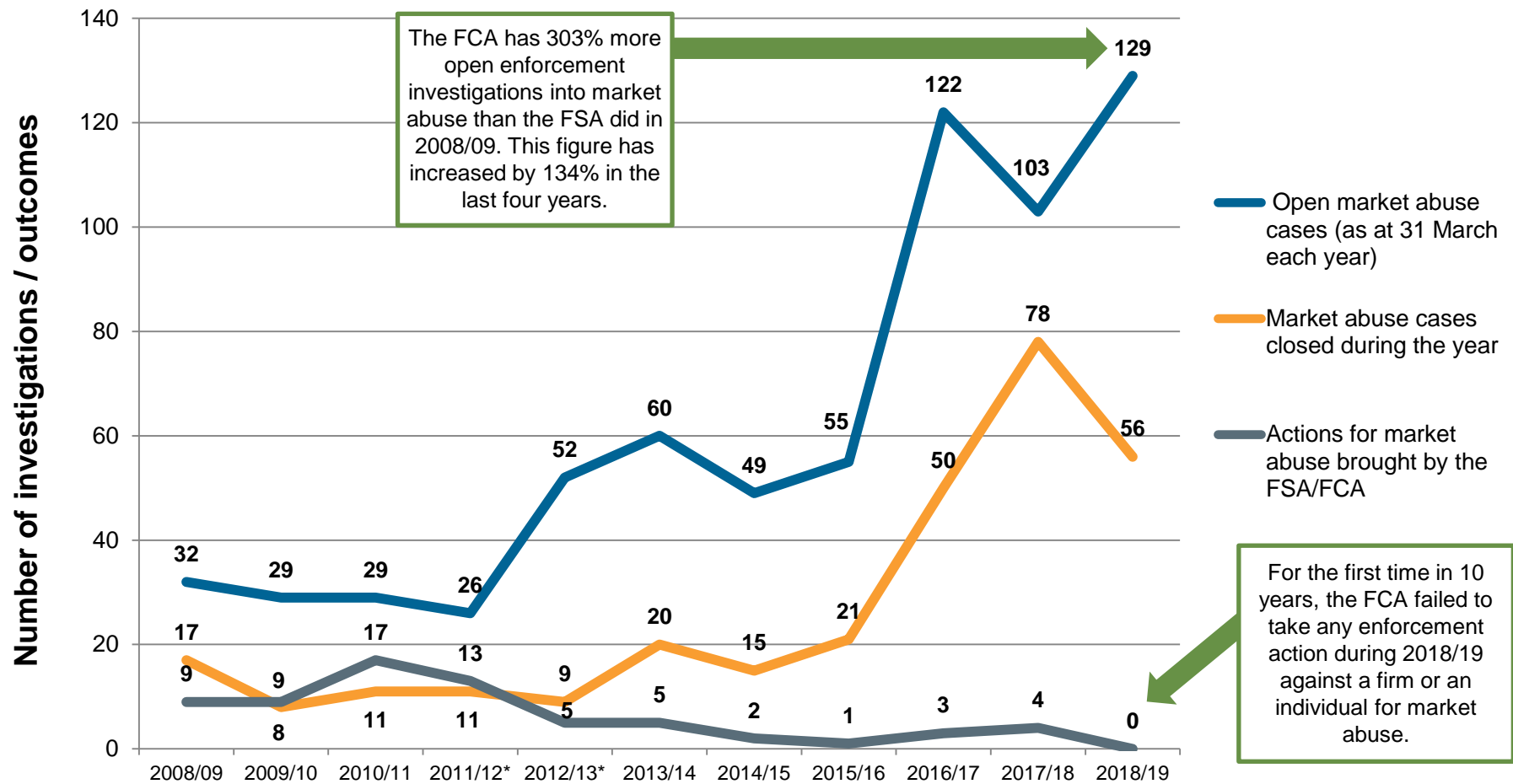
One asset manager obtained **immunity**; two others were fined £306,300 and £108,600 respectively



**Parallel FSMA investigation** resulted in a financial penalty (£32,200) for an individual fund manager for failing to observe proper standards of market conduct and acting without due skill, care and diligence

# *Market abuse*

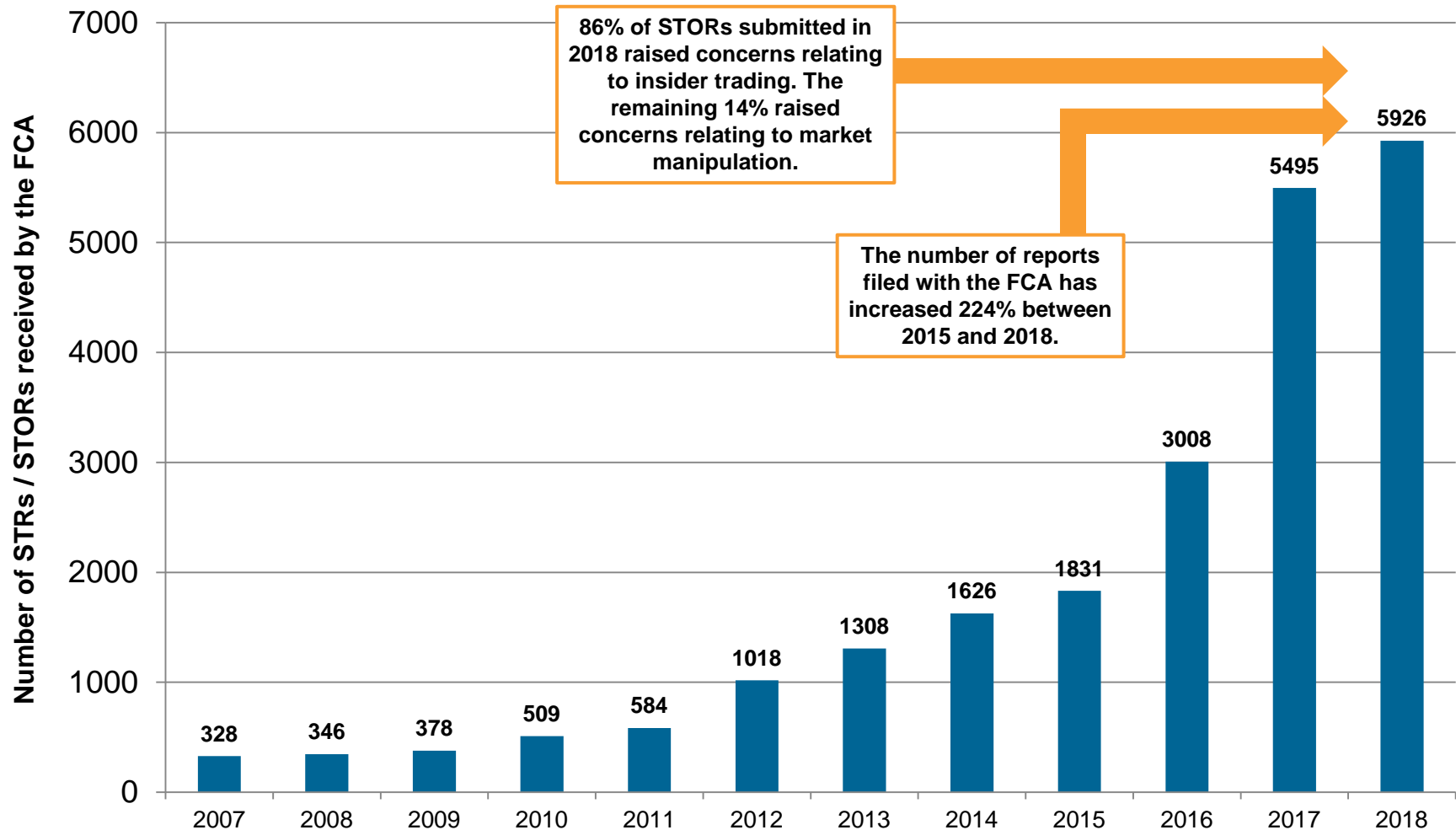
# FCA market abuse investigations are at an all-time high, but the level of enforcement action remains low



Sources: FCA website and Annual Reports | These figures reflect investigations into and enforcement action taken for civil market abuse offences | \* In 2012/13 the FCA changed the way it reported its closed market abuse investigations.



# The FCA continues to receive more STORs, 92% of which related to equities in 2018



Sources: FCA website | On 3 July 2016, the Market Abuse Regulation came into force and introduced STORs in place of STRs.

# Key areas of FCA focus that extend beyond substantive market abuse offences



Controls to detect and report suspected market abuse.



Production and maintenance of insider lists.



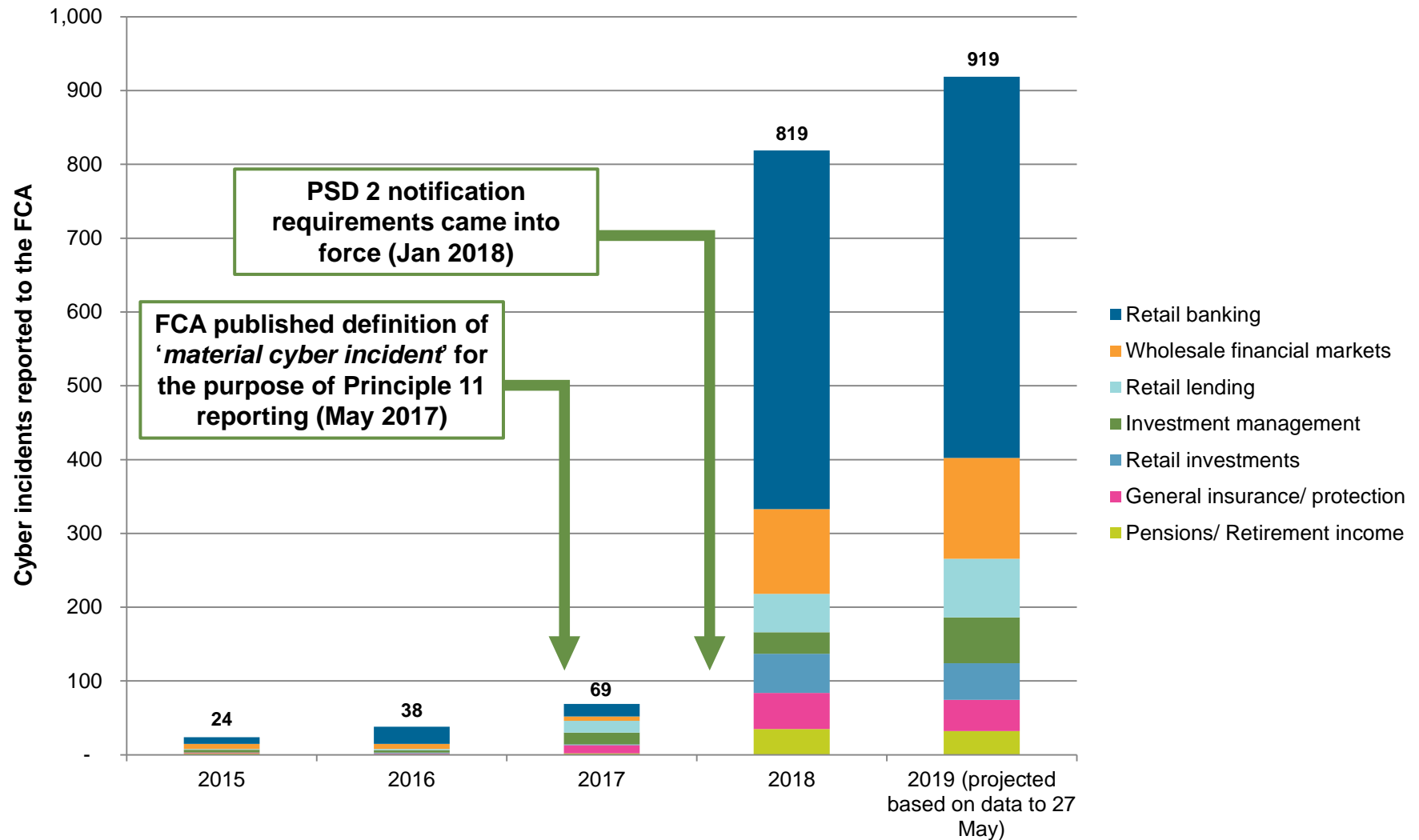
Systems and controls relating to pre-soundings



Control, access to and flow of inside information within regulated firms

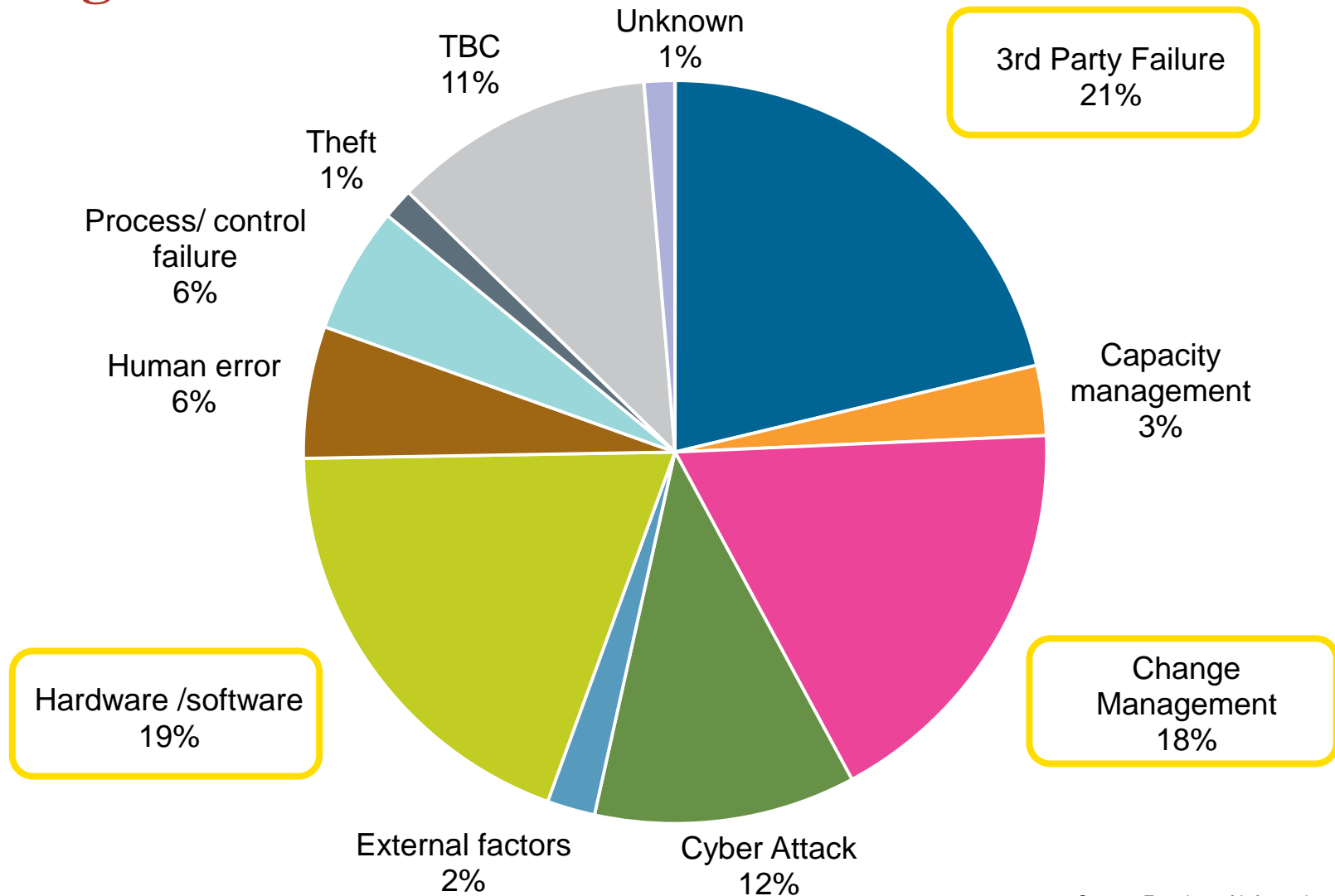
# *Operational resilience: Cyber and data security*

# Reporting of cyber incidents to the FCA has markedly increased in the last two years



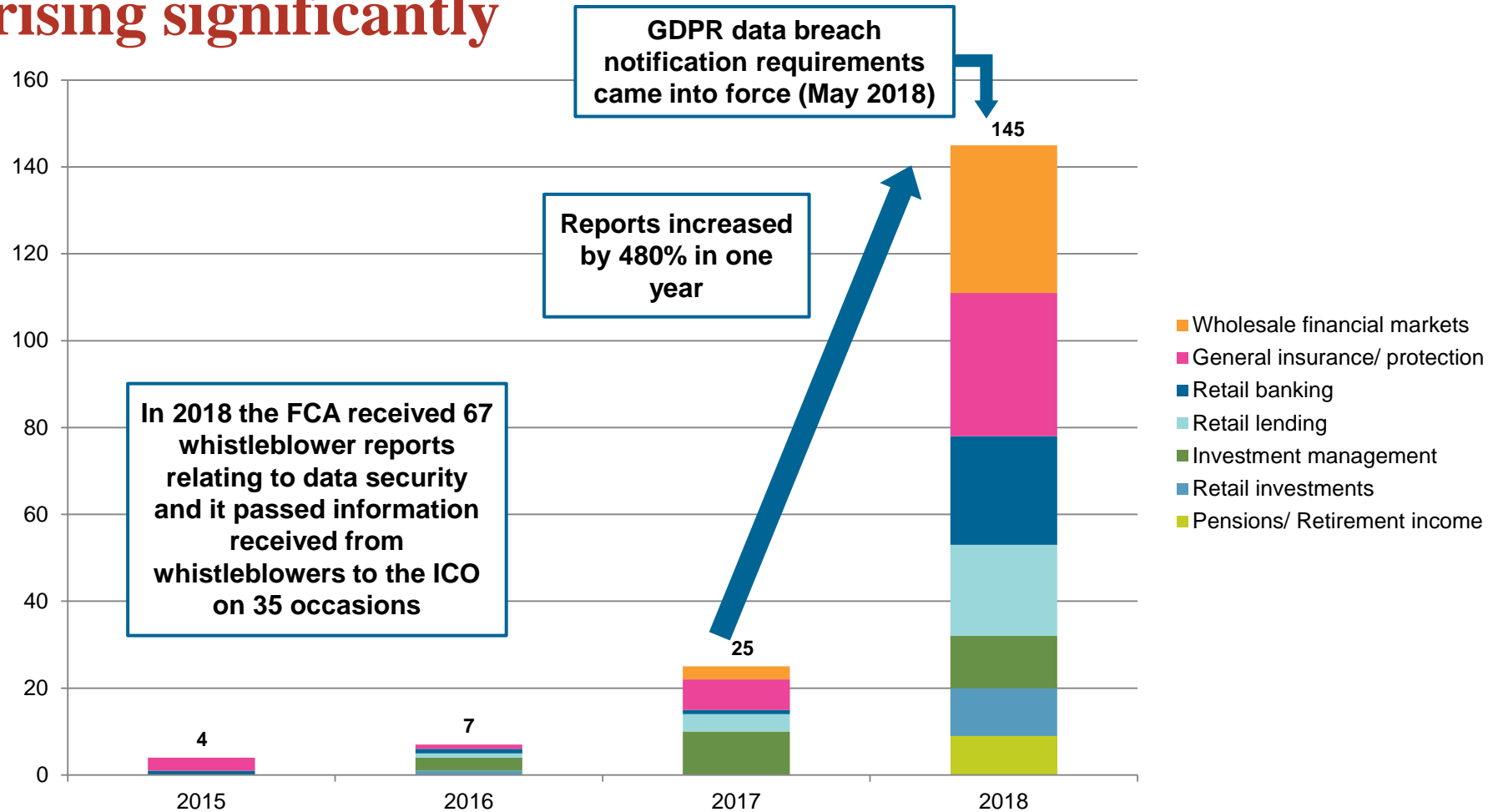
Source: Freedom of Information Act request

# Root causes of cyber incidents reported to the FCA during 2018



Source: Freedom of Information Act request

# Reporting of data breaches to the FCA is likewise rising significantly



**Data breach:** “a confirmed incident in which confidentiality of company or personal data is breached”

# FCA expectations for managing operational risk



## Oversight

- Operational resilience '*no less important than financial resilience*' and must be on the board / senior management agenda
- Responsibility and accountability must be clear
- SMs and risk/compliance/audit require appropriate knowledge, skill and expertise



## Establish a proportionate level of operational resilience

- Identify and prioritise most important services and set '*risk tolerances*'
- Identify critical outsourcing services and review the third party's controls
- Anticipate the consequences on the firm, customers and markets



## Respond quickly and effectively

- Develop (and test) business continuity and disaster recovery plan to preserve continuity of services or minimise disruption
- Have clear escalation paths and identify decision makers
- Communicate with stakeholders, including the FCA and customers



## Compensate and learn

- Proactively and quickly deliver customer redress
- Undertake an appropriate post-hoc investigation and implement remediation



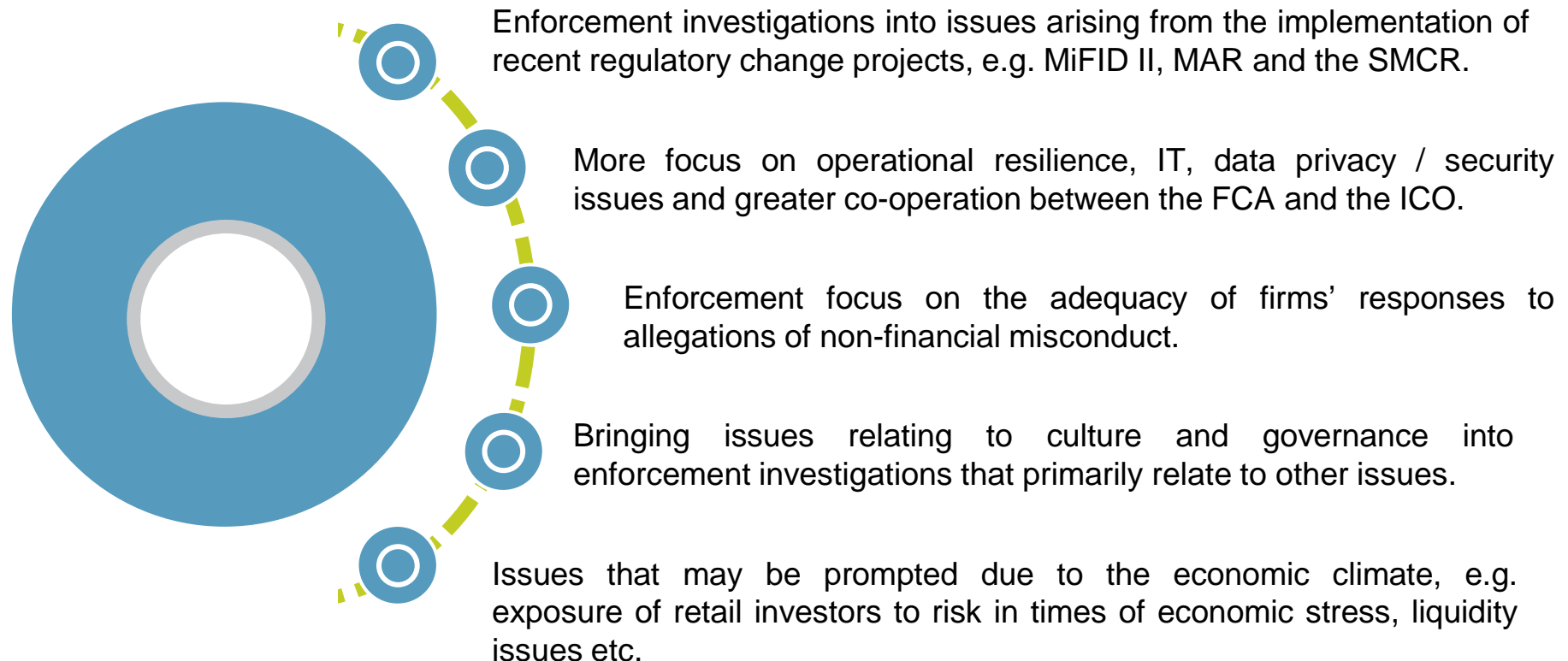
# Recent FCA proposals in relation to formalising operational resilience arrangements



Source: 'Building operational resilience: impact tolerances for important business services' (December 2019)

# *Predictions for 2019/20 and beyond*

# Future areas of UK regulatory enforcement focus



# Key contacts



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# Questions?

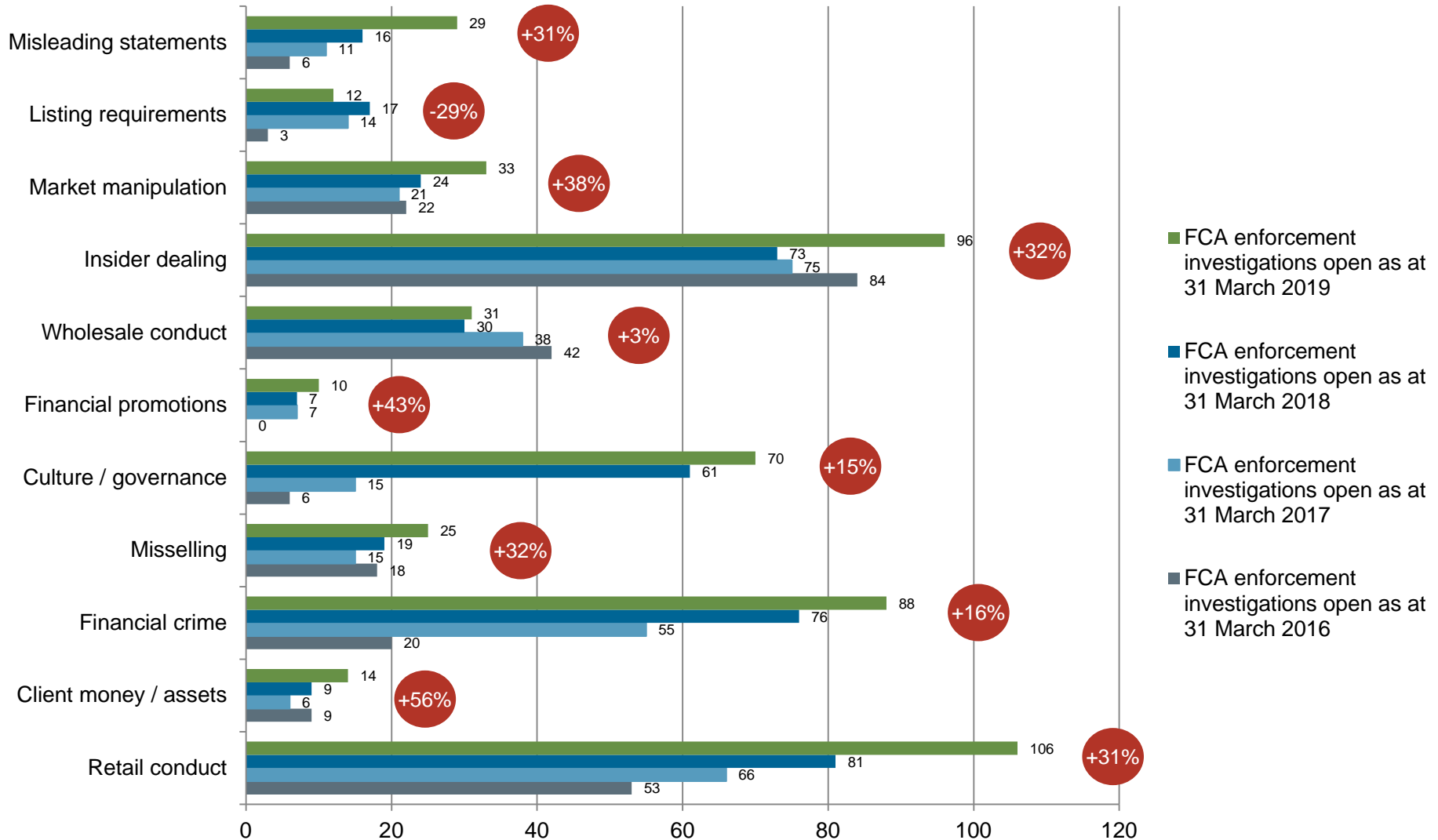
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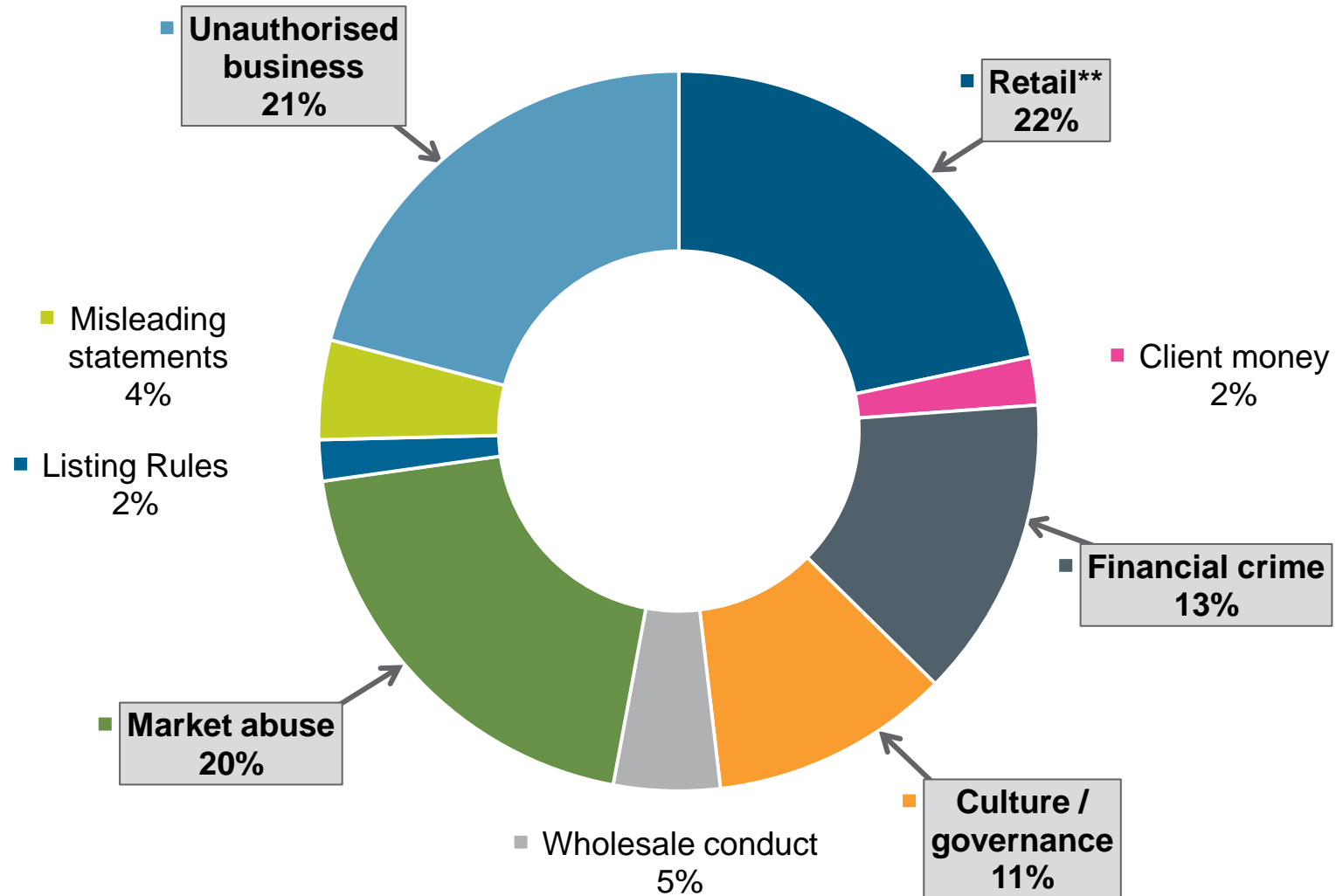
# *Appendix*

# FCA areas of enforcement focus 2015/16 – 2018/19



Source: FCA website and Annual Reports.

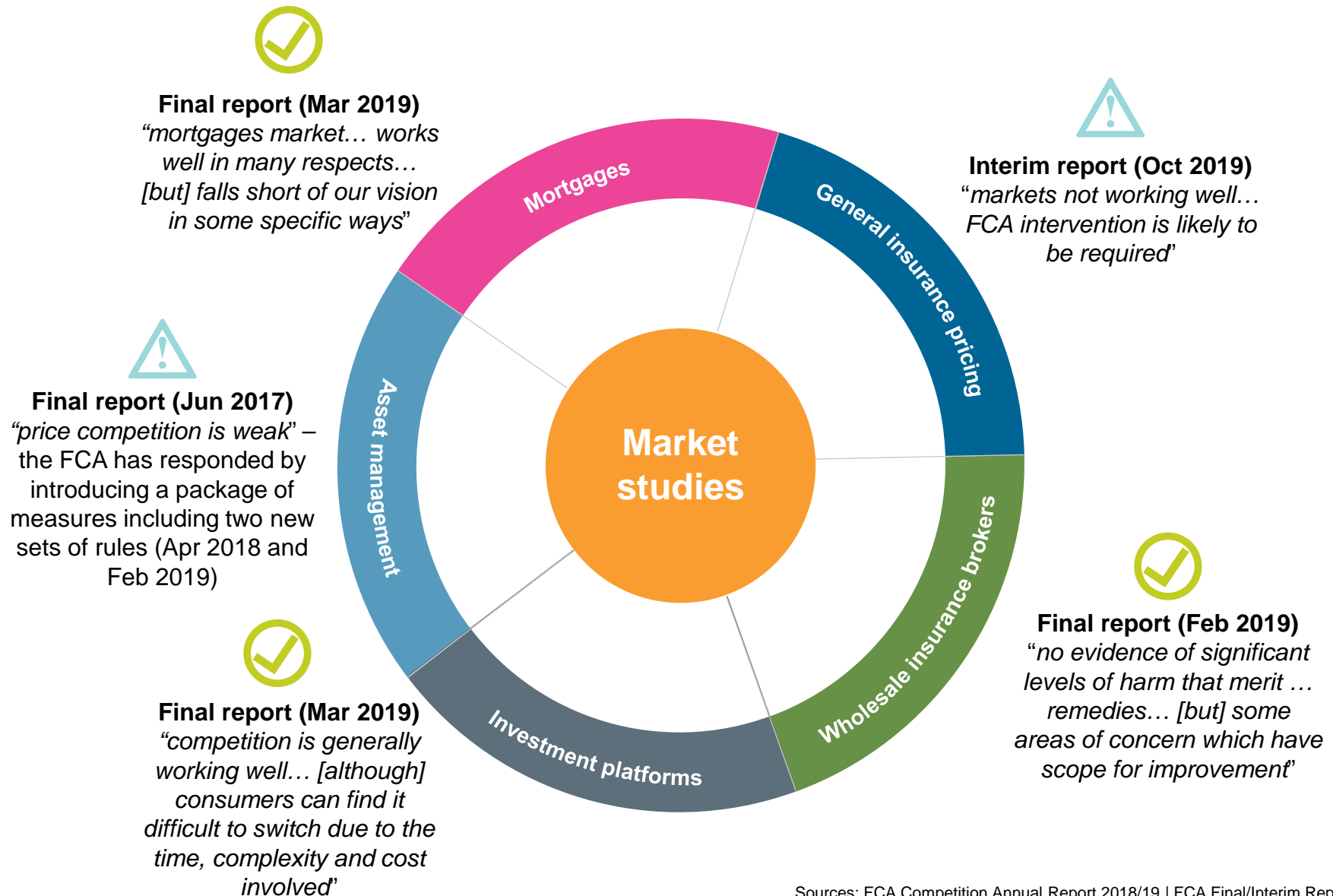
# The FCA's current\* enforcement case portfolio



\* As at 31 March 2019 | \*\* Includes investigations relating to mis-selling and financial promotions | Source: FCA Annual Report 2018/19.



# FCA competition law market studies



Sources: FCA Competition Annual Report 2018/19 | FCA Final/Interim Reports.