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# BULLETIN | FINANCIAL SERVICES AND REGULATIONS

August/September 2014

This edition of the Bulletin is a bumper one covering a round-up of both August and September's important financial services and regulation developments. After a break in August, the FCA has provided an insight into its thoughts on the implementation of MiFID II at its September conference on the subject. There have been a string of important publications issued by the UK regulatory authorities, including various statements of new policy and consultations. Enforcement activity has continued apace throughout the summer with Barclays receiving the highest ever fine for CASS failings (£38m) and RBS and NatWest being fined heavily for mortgage advice failings. Finally, the FCA has continued to take its responsibility for the consumer credit sector very seriously, providing useful guidance to firms on authorisation requirements and warning them that rules on financial promotions must be taken seriously.

For an update on developments in the European Union, please see this month's bulletin here.

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## SPEECHES

### 1. David Lawton discusses implementation of MiFID II

David Lawton, the Financial Conduct Authority's ("FCA") Director of Markets, spoke about implementation issues for the recast package of measures known as "MiFID II", including both the recast Markets in Financial Instruments Directive and the Markets in Financial Instruments Regulation, at the FCA's conference on MiFID II on 18 September 2014. The main purpose of the speech was to highlight some of the options available to firms, and to stress that debate and interaction between stakeholders and regulators would be welcomed whilst the detailed rules were being finalised.

He stated that there were still 27 months until implementation in 2017, but that this is not a long period of time and he expected there to be "a lot of heavy lifting" to be done between now and then. He also explained that the FCA would not consult on any changes to its own rules until the European Securities and Markets Authority ("ESMA") publishes its recommendations to the European Commission, European Parliament and the Council of the EU in mid-2015, and the necessary regulatory technical standards and implementing technical standards are published in late 2015 or early 2016.

Mr Lawton said that there were still a number of issues for discussion.

- On transparency in the wholesale markets, he explained that questions such as how to increase transparency without reducing liquidity; which thresholds to use for large in scale; what is the definition of a "liquid" instrument, are all important areas to flesh out.
- On commodity markets, he said that the methodology that EMSA chooses to set position limits is a huge challenge still to be addressed.
- He outlined the challenge of designing a balanced regime for high frequency trading and algorithmic trading.
- He noted that the strengthening of best execution obligations and restrictions surrounding the use of dealing commissions would remain significant areas with regard to wholesale conduct.
- He stressed that getting the balance right with regard to disclosure and transparency on best execution so as to provide market participants with data that they need is a key topic for discussion.
- The FCA continues to support ESMA's proposal on dealing commission.

He also mentioned the raft of new protections coming in for retail investors, and that the consequences for the entire European financial infrastructure of getting implementation wrong in this area would be huge. He explained that the authorities need to ensure that they have considered very seriously the consequences of all proposals for stakeholders, including the markets, firms, trading venues and, most importantly, investors and end users. He recognised that the implementation of MiFID II poses a huge challenge to the industry as a whole, and that now is the time to get the detail absolutely right.

### 2. FCA examines MiFID II investor protection measures

Also at the FCA's MiFID II conference, Maggie Craig, Acting Head of Savings and Investments at the FCA, set out some of the challenges facing firms in connection with the new MiFID II investor protection rules and measures being finalised. She explained that many of the new requirements came out of the problems identified during the financial crisis, such as the new, stricter rules on structured products and putting in place rules to help protect local authorities across Europe from the attractions of high-risk instruments which they do not understand.

However, she noted that many of the new requirements come out of more general regulatory concerns, such as a need to improve oversight and governance, incentive structures and the quality of advice and sales processes across the industry.

Ms Craig stated that the FCA would be thinking carefully about the composition of the relevant rulebooks in the FCA Handbook, and what they should look like in time for MiFID II implementation in 2017. She stressed that there needs to be an intelligent discussion about the requirements and asks that firms consider the issues carefully over the coming months. She hinted that strict copy-out of the new standards from the EU text may not necessarily be the right approach, and deviation might not be “a bad idea” where this made sense.

With regard to senior management responsibilities, she expressed the desire that senior staff must be able to understand and engage with the new standards in practice. Having state of the art, compliant systems would only be half the battle. She said that firms should re-think their governance, and that it is important for them to take responsibility, at a senior level, for what they make or sell; what these products do; and where they will end up. Whilst systems are inevitably extremely important, firms must not lose sight of the management responsibility and governance issue.

On remuneration, Ms Craig stated that the FCA will be taking a look at the approach to financial incentives for sales staff as a whole across the industry. She also stated that firms will be expected to tackle a number of different risks through their systems and controls, including a wider obligation to record telephone conversations and stricter conflicts of interest requirements. On suitability and appropriateness, she expressed surprise at the industry response to ESMA’s consultation, and asked if perhaps there was more that the FCA could do to allay fears and to work with the industry to consider what sort of checks are needed in practice to comply with such requirements.

On costs and charges Ms Craig explained that the new requirements may not be easy to deliver, but that the FCA is aiming to implement new standards, which are workable for firms and result in useful and meaningful information for consumers. She believes that behaviorally-informed regulation should, in future, lead to a smarter and better disclosure regime. She also acknowledged that the requirement for best execution will present technical challenges for firms, owing to the relatively granular requirements for reporting of execution quality. She said that the FCA would remain conscious that more disclosure and more transparency may not be the answer and that it would be looking to get the balance right on this.

To sum up, she stressed that the new MiFID would not simply be about prescriptive sale standards or new systems. The mind set of senior managers, system designers and staff at all levels throughout different organisations will need to reflect the new responsibilities being created. She reiterated that it is crucial that both the standards of conduct and the organisation of firms reflect the interests of consumers and the duties owed to them. Chiefly, firms need to understand why the change is necessary if they are to implement any new requirements successfully.

## 3. Will Amos sets out FCA approach towards achieving right investor outcomes

On 24 September 2014, the FCA’s Director of Wholesale Banking and Investment Management, William Amos, gave a speech at the Investment Week Fund Management Summit in London on the FCA’s approach towards achieving the right investor outcomes. In it he explained that in order to do so, the FCA will need to be transparent, and initiate proper dialogue with firms. It will need to understand firms’ reasons for conducting business in a certain way and, therefore, spending more time than it has done historically with businesses and understanding what they do and, importantly, how they do it. He stated that the FCA will look at how firms think about risk, customers, the market, and how they identify, assess and control risks in businesses. He explained that the FCA’s expectation is for businesses to be responsible for ensuring proper market behaviour all the way from the Board room through to the investment manager and trading desk. The FCA believes that problems within retail and wholesale behaviours have been the result of strategies or practices driven by and implemented by the Board or within individual business lines, rather than a flawed compliance or internal audit framework.

He also mentioned that a key ingredient would be ensuring that firms have the right culture. He said this must be embedded throughout the business, and it needs to make the firm think about the consumer, as well as market integrity. It should be based on a concept of “should we do this?”. Firms must ask themselves at all points of the product cycle, whether a particular action fits within the values or culture of the company and whether it is in the interests of the client. Will it enhance the reputation or integrity of the market, or will it threaten it? Mr Amos set out the key drivers which reinforce the correct culture and values, including: clear and ongoing leadership from the top; constant reinforcement and support messages from senior management and the board, together with suitable incentive structures; effective performance management including penalties for not doing the right thing and, conversely, rewards for doing the right thing.

Mr Amos went on to explain that the FCA has made changes to the fund authorisation process, including an enhanced approach to its supervision of funds. As part of this process the FCA has set up a new Fund Authorisation and Supervision Team which will oversee the cradle-to-grave lifecycle of UK investment funds. The FCA believes that through aligning the authorisation and supervision functions in this way, it will be able to ensure that a consistent focus on investor outcomes will run throughout the product’s life.

On fund authorisations, Mr Amos explained that the process has been made more efficient and robust, with documents needing to be accurate and unambiguous. The fund structures must be clearly set out in language which an investor can understand and applicants must explain clearly what the investment strategy is and what the risks involved are. He also mentioned that the timelines for authorisation are coming down in line with FCA objectives. By way of example, he said that the FCA is already processing UCITS applications typically in under six weeks, which is two weeks inside the normal timeline.

On supervision, he stressed that the new unit would focus on supervising retail-focused funds and will comprise pre-emptive, reactive and thematic work. The approach will be data-driven, using new data streams to identify outlier funds for supervisory follow-up work. Much of the data will come from the AIFMD, but the FCA is also working with industry to extract more use from existing data and looking to build new capabilities to focus analysis of wider market data.
Mr Amos stated that the FCA expected fund supervision to complement existing FCA firm supervision. Ultimately, it desires firms “to operate as good agents”, with the client or investor interests being served in all areas of the business. Firms must consider whether their internal processes adequately cover the entire fund product life-cycle.

## UK PUBLICATIONS

### 1. FCA consults on implementation of the BRRD

The FCA published its consultation paper on implementation proposals concerning the European Union’s Bank Recovery and Resolution Directive (“BRRD”) on 1 August 2014. This consultation paper follows similar consultations published by HM Treasury and the Prudential Regulation Authority (“PRA”) back in July. The proposals concern those firms which are solely regulated by the FCA, that is investment firms subject to the recast Capital Requirements Directive (“CRD IV”) and which have an initial capital requirement of €730,000 (known as 730K firms) . The proposals also apply to group entities in groups which contain a 730K firm or a credit institution.

The consultation paper (CP14/15) explains the FCA’s approach with regard to: recovery planning requirements for both individual firms and groups; notifications of failure or likelihood of failure;

resolution planning; intra-group financial support; and contractual recognition of bail-in. The proposals require the Prudential Sourcebook for Investment Firms in the FCA Handbook ("IFPRU") to be amended to include a new Chapter 11 on recovery and resolution. In drafting these new rules the FCA has closely followed the wording of the BRRD.

In addition, the FCA intends to apply simplified obligations for recovery and resolution planning for the majority of IFPRU 730K firms. Only the largest and most significant firms in this bracket will need to apply the BRRD requirements in full. The definition of a "significant" IFPRU 730K firm is set out at IFPRU 1.2.3R. Currently, the FCA believes that 190 of the 230 FCA-authorised firms within scope will fall outside the most stringent requirements.

The FCA has also requested feedback on the metrics to be used as triggers for early intervention with regard to resolution and recovery and on whether firms should be required to main detailed records or financial contracts as part of their recovery plans. The FCA is also interested in firm's views on proposals for the minimum requirement for eligible liabilities and how this should be set on a firm by firm basis.

The consultation ended on 1 October 2014, and the FCA intends to publish its final rules in a policy statement at the end of the year prior to the BRRD implementation date of 1 January 2015.

## 2. FCA publishes guidance on supervisory approach to communications with customers using social media

The FCA issued a guidance consultation on its supervisory approach to financial promotions in social media on 6 August 2014. It notes that this is not a new area for guidance, given that the Financial Services Authority ("FSA") provided guidance on social media use back in 2010. However, the FCA acknowledges the need for an update, given that digital media "are now becoming the media of choice in many cases for customer communications".

The guidance defines social media as sharing the characteristic of being digital and including websites and applications that enable users to create and share content or participate in social networking. The FCA provides a non-exhaustive list including: blogs; micro-blogs; social networks; fora; and image and video-sharing platforms. It notes that some media impose character, space or time limits. The new guidance is designed to:

- confirm and set out clearly the FCA's approach to supervising financial promotions in social media;
- explain how firms can comply with the FCA's requirements when using social media; and
- remind firms that FCA rules are intended to be media-neutral to ensure that consumers are presented with certain minimum information, in a fair and balanced way. It explains that there are sector-specific requirements, but reiterates that there is an overarching principle for all communications to be fair, clear and not misleading.

The guidance covers various different areas of which firms should be aware, including standalone compliance for each individual communication; risk warnings; image advertising; and other regulatory issues such as whether a communication is considered "real time" and sharing and forwarding of communications. The FCA states that the guidance consultation will close to responses on 6 November 2014.

## 3. UK regulators publish letters to Treasury Select Committee on s.166 powers

The Treasury Select Committee of the House of Commons published a letter addressed to its chairman, Andrew Tyrie MP from Martin Wheatley, CEO of the FCA, and two letters (see here and here) from Andrew Bailey, Deputy Governor of the Bank of England and CEO of the PRA. The letters, which are all dated July 2014, respond to letters from the Treasury Select Committee from June 2014 asking for information on how the FCA and PRA deploy their powers to engage the use of Skilled Persons to prepare reports under Section 166 of the Financial Services and Markets Act 2000 ("FSMA"). The responses from both regulators shed further light on how they make use of these powers in practice.

Whilst the letters from the Treasury Select Committee have not been published, it is clear from the responses by the FCA and PRA that a number of specific questions in relation to the use of these powers have been raised. The letters explain how the FCA and PRA decide whether the firm concerned will be able to employ the Skilled Person itself, or whether the regulator will make the choice for them. They discuss how the FCA and PRA are promoting competition by opening the process up to a wider selection of firms to compete for such mandates. The letters also cover how far both the regulators cooperate, if necessary, in deciding on the scope of a Section 166 report and look at the costs and oversight relating to such reports.

## 4. FCA letter clarifies approach and use of regulatory attestations

The FCA has published a letter (dated 22 August 2014) from Clive Adamson, Director of Supervision at the FCA, to Graham Beale, Chairman of the FCA Practitioner Panel, which discusses the FCA's approach to attestations and in what types of circumstance such a tool might be used. Mr Adamson also explains that the FCA is revising the internal guidance it has previously issued to supervisors to ensure that they are using this important tool consistently to achieve the right outcomes.

Mr Adamson clarifies that attestations are now a formal supervisory tool for the FCA and he states that the aim of obtaining an attestation is to ensure that there is clear accountability and senior management focus on specific issues where the FCA would like to see change within firms, often without on-going regulatory involvement. The letter states that the focus of attestations is usually on firms putting things right rather than seeking to better understand the extent or materiality of any issue. The FCA has no intention of creating onerous or additional assurance processes within firms beyond those which firms see as reasonable.

Mr Adamson explains that the FCA will usually ask for attestations to be given by the most relevant significant influence function holder responsible for the area at which the issue has arisen or which is responsible for addressing any such issues. The letter goes on to identify four common scenarios in which attestations are likely to be used:

- Notification - the FCA may ask an appropriate individual at a firm to attest that they will notify it if an emerging risk, which is unlikely to result in material consumer detriment or negative impact on market integrity, changes in nature, magnitude or extent.
- Undertaking - the FCA will use this approach where it wishes a firm to take specific action within a particular time scale.
- Self-certification - where the FCA is confident that a firm can resolve an issue itself but it is a serious issue nonetheless, it will ask for an attestation that any such risks have been mitigated or resolved.
- Verification - the FCA will use this approach where it wishes a firm to resolve issues or mitigate risks, but also to verify that any such action has been carried out.

The letter also explains the ways in which the FCA intends to ensure that attestations are used consistently and clearly going forward. It states that it will be issuing revised internal guidance and supporting materials for its own supervisors, as well as strengthening its governance processes surrounding the use of attestations. The FCA also explains that it will publish data on attestations on a quarterly basis in a similar way to that which it publishes with regard to Skilled

Person Reviews. The letters between Mr Adamson and Mr Beale have been published on a special FCA webpage relating to attestations.

## 5. PRA sets out policy on foreign bank supervision

On 5 September 2014, the PRA published its policy statement on its approach to branch supervision for international banks headquartered outside of the European Economic Area ("EEA"). (PS8/14). The policy statement sets out the PRA's final approach and policies in connection with its consultation paper on the subject, published in February 2014. The policy statement also sets out the PRA's approach to subsidiaries and branches of banks based within the EEA.

The PRA's approach to non-EEA branches (i.e. branches of banks headquarters outside the EEA) focuses on three major factors. The first is that the home state supervisor for the bank has sufficient equivalence with the PRA in relation to supervision and resolution. The PRA must have assurance that the home state supervisor's actions will be aligned to delivering PRA objectives. The second factor is that the PRA will only allow non-EEA branches to undertake retail banking activities at *de minimis* levels, unless there is a high level of assurance over resolution. In addition, the branch should only carry on wholesale banking at a level which is not critical to the UK economy. The third factor relates to resolution and whether the home state supervisor's resolution regime is equivalent to that in the UK with a focus on the credibility of the individual bank's resolution plans. Where the PRA is satisfied the non-EEA branch meets these requirements, it will also look to ensure that its supervisory responsibilities are shared in a clear way with the home state supervisor. Where the PRA is not satisfied, it will take action, including potentially refusing or cancelling authorisation.

The PRA has made appropriate amendments to the PRA Rulebook, including inserting a new Incoming Firms and Third Country Firms Part. This includes rules requiring banks with international headquarters to take all steps within their control to ensure that their resolution plan provides adequately for the resolution of their UK branches. In addition, the PRA also issued the final supervisory statement (SS10/14) which expands the PRA's approach to international bank supervision and clarifies how it will supervise branches. It also explains that the feedback received on the February 2014 consultation led to the PRA making minor changes to the supervisory statement. The PRA states that it intends to bring the rule introducing a twice-yearly data return, applicable to all UK branches, into force at a later date following a further pilot exercise.

## 6. Treasury consults on regulatory scope for financial benchmarks

On 25 September 2014, HM Treasury published a consultation paper on extending the existing UK regulatory and legislative framework for benchmarks under the Financial Services and Markets Act 2000 ("FSMA") and the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 ("RAO") to include the following seven benchmarks:

- Sterling Overnight Index Average;
- Repurchase Overnight Index Average;
- WM/Reuters 4pm London Closing Spot Rate;
- ISDAFIX;
- London Gold Fixing;
- LMBA Silver Price; and
- ICE Brent

The consultation follows the publication by the Bank of England of a report to the HM Treasury by the Fair and Effective Markets Review ("FEMR"), which set out its recommendation to add to the number of financial benchmarks under regulatory scope in the UK. FEMR recommended that all seven benchmarks should be "specified" benchmarks under the RAO, and designated as "relevant" for the purposes of the criminal offence of making misleading statements in relation to benchmarks under the Financial Services Act 2012.

The Treasury's consultation states that the Government will publish an impact assessment setting out the potential costs and benefits of bringing the benchmarks within UK regulation, based on the experience gained by the authorities of bringing LIBOR within the UK regulatory perimeter. Bringing the new benchmarks under regulatory control is expected to reduce the risk of misconduct and improve resilience against any attempted manipulations of the benchmarks. It will also have the added benefit of increasing governance and regulatory oversight over them and increase benchmark credibility and integrity. The consultation closes on 23 October 2014.

## 7. Joint consultation on data collection for remuneration practices under CRD IV

On 22 September 2014, the Bank of England published a joint consultation issued by both the PRA and FCA (PRA CP17/14/FCA CP14/19) concerning data collection for remuneration practices under the recast Capital Requirement Directive and the Capital Requirements Regulation (together known as "CRD IV"). The consultation provides both regulators' proposals to update the current approach to data collection of remuneration practices and the connected reporting requirements for banks, building societies, investment firms and any other types of firm for which data must be collected in accordance with CRD IV.

In essence, the proposals affect the remuneration benchmarking information report and the high earners' report, which are contained in the appendices to the consultation. The consultation states that the benchmarking report template has been revised to enable the collection of more detailed data, with additional business area data on remuneration being broken down into different categories of staff and more information being disclosed about the form in which total fixed remuneration is delivered. Whilst it is unlikely that this requirement would be applicable to FCA-authorised firms, the FCA Handbook will be updated to introduce the amended rule, so as to mirror the PRA Rulebook. On the high earners' report, both the PRA and FCA will revise their existing rules to require firms to submit data on all employees with total remuneration of €1 million or more in a financial year for all subsidiaries and branches within a group based in the EEA or a branch of a firm with its head office located outside of the EEA. The template has been revised to introduce the collection of more detailed data with additional business areas included to ensure that the data is broken down into more categories of staff.

The revised rule will be slotted into the Remuneration Part of the PRA Rulebook and Chapter 16 of the Supervision Manual of the FCA Handbook. The remuneration code section of the Senior Management Arrangements, Systems and Controls Sourcebook of the FCA Handbook is also to be amended to reflect revised guidelines issued by the European Banking Authority on 16 July 2014 in relation to remuneration data collection. The consultation will close on 17 October 2014.

## 8. FCA publishes Thematic Review report on mobile banking

On 11 September 2014, the FCA issued the report into its Thematic Review of mobile banking and payments (TR14/15). The FCA explained that the purpose of the review was to determine how firms are achieving good outcomes for consumers when delivering mobile banking products, since these services should offer consumers a convenient way to bank flexibly, save time and money by enabling better management of finances. The FCA encouraged firms to consider how they would be able to ensure their mobile banking products and services remain useful and continue to work well for consumers.

The FCA identifies five key areas which are relevant to whether firms are delivering good outcomes for their consumers. These are:

- How easy it is for consumers to understand their legal rights and obligations when using mobile banking products and services, and what firms are doing to aid consumer education.
- How firms ensure that the knowledge and understanding of key decision makers in the business is in line with the pace of innovation.
- How firms ensure consumers' sensitive personal data and funds are secure, and technology is sufficiently robust to cope with changes in consumer behaviour when making payments.
- How firms providing mobile banking products and services retain oversight of third parties and outsourced functions involved in the delivery of their product offering to consumers.
- How new entrants to the mobile payments arena ensure that they have adequate knowledge and understanding of the regulatory framework surrounding payments.

The FCA states that it published an interim report in August 2013 which set out initial work it had done to understand mobile banking better. However, matters which were covered in that report, such as fraud against firms and anti-money laundering have not been prioritised in the latest Thematic Review report. The FCA states it is satisfied that firms are addressing these areas and encourage them to continue to do so as the products and services develop in popularity and complexity.

The FCA states that it will be working in future with the banking industry to ensure firms have a clear understanding of the key areas identified in the report. The findings will also be used to support Project Innovate, which is designed to help businesses bring innovative ideas that benefit consumers to financial markets. The FCA also highlights the fact that it will work closely with the new Payment Systems Regulator and with the relevant EU authorities on developments which have an impact on mobile banking and payments.

## CONSUMER CREDIT

### 1. FCA publishes checklist for consumer credit authorisation

The FCA has published two separate checklists for consumer credit firms applying to it for authorisation. The first relates to those firms which need to apply for full permission, and the second relates to those firms which only require a limited permission.

The type of permission which a firm should apply for will depend on which consumer credit related regulated activities they wish to carry on. Those applying to carry on higher-risk activities such as offering personal loans, credit cards, overdrafts or hire purchase and conditional sales, credit brokerage, debt administration or counselling and peer-to-peer lending will all need to apply for full authorisation. Firms which offer lending activities where the main business relates to non-financial services and there is no interest or other charge levied, consumer hire arrangements for items such as tools and cars, credit brokerage as a secondary activity and certain not-for-profit activities will be considered lower-risk consumer credit activities requiring only limited authorisation.

The two checklists set out what information the firms will require together with the ancillary documentation which will be needed for their application to the FCA, so that they may assemble it prior to putting together any application. In addition, the checklists explain that firms should be provided with a date from which they can apply for authorisation via email.

The FCA has published in conjunction with the checklists a decision tool designed to help firms work out which type of permission they will need from the FCA. Alongside the decision tool, the

FCA has also published a document which explains important FCA terminology to consumer credit firms who are new to the FCA's regulatory requirements.

## 2. New JMLSG guidance for consumer credit firms approved

HM Treasury confirmed that it has approved the guidance for consumer credit providers prepared by the Joint Money Laundering Steering Group ("JMLSG") in relation to Sections 330 and 331 of the Proceeds of Crime Act 2002 ("POCA"), Section 21A of the Terrorism Act 2000 ("TACT"), and Regulations 42 and 45 of the Money Laundering Regulations 2007 ("MLR"). The confirmation was provided by HM Treasury in a letter to the JMLSG dated 29 July 2014, which the JMLSG published together with a press release on the subject on 27 August 2014.

HM Treasury states in the letter that the new guidance has been approved with immediate effect and that it has the same status as other parts of the existing JMLSG guidance on money laundering. The new guidance is included as a new Chapter 11a in the sector-specific Part II of the JMLSG's guidance. It provides information on the money laundering and terrorist financing risks for consumer credit providers and help with how to assess the risk of money laundering and carrying out customer due diligence. The press release also includes a link to the final approved text of the guidance.

## 3. "Ensure financial promotions are fair" warns FCA

The FCA issued a warning to firms on 13 August 2014 via a press release which explained that, especially in the consumer credit sector, firms must do more to ensure all financial promotions are clear, fair and not misleading for consumers. The warning explains that since 1 April 2014, the FCA has looked at over 1,500 financial promotions for consumer credit products, and has opened 227 cases about non-compliant promotions for consumer credit products over the same period. The FCA explains that a quarter of the cases relate to advertisements for high-cost short-term credit which do not display a risk warning or representative APR prominently enough. In addition, the vast majority of cases come from digital media such as websites, emails and text messages.

The press release provided examples of financial promotions which fell foul of the FCA's regulations including:

- advertisements for fee-paying debt management firms which did not make it clear that a fee was payable;
- promotions guaranteeing firms would offer credit regardless of a customer's circumstances;
- a log book lender who provided misleading information about its APR, made unclear comparisons between its rates and those of other lenders, and implied its services were endorsed by the FCA; and
- internet search terms which took consumers to unrelated sponsored links, which were potentially misleading for such consumers.

The FCA states that it will continue to monitor financial promotions in detail and take action where required to push up standards. However, it did explain that firms were responding positively and speedily to make any requested changes to promotions in the event they were contacted by the FCA. Clive Adamson, FCA Director of Supervision, explained that the FCA is disappointed to see standards short of its expectations in this area, and reminded firms that they should be doing more to ensure that their financial promotions meet the FCA's required standards.

## INVESTIGATIONS AND ENFORCEMENT

### 1. Barclays handed £38m fine for putting client assets at risk

On 23 September 2014, the FCA published a final notice which it issued to Barclays Bank plc ("Barclays") for failings in its Investment Banking Division which led to clients' custody assets worth £16.5 billion being put at risk. The amount of the fine, £37,745,000, is the highest fine ever imposed by the FCA, or its predecessor regulator the Financial Services Authority for client assets breaches. The fine would have been over £54 million were it not for Barclays agreeing to settle at an early stage of the investigation.

The FCA found that Barclays had breached Principle 3 (Management and Control) and Principle 10 (Clients' Assets) of the FCA's Principles for Businesses ("PRIN") and associated rules in the Client Assets Sourcebook ("CASS"), set out in the FCA Handbook. The breaches occurred between 1 November 2007 and 24 January 2012.

During this period, the FCA stated that the Investment Banking Division failed to:

- take reasonable care to establish adequate and effective organisational, control and risk management systems in relation to the opening, on-going operation and monitoring of external accounts in which safe custody assets were held with sub-custodians outside the Barclays Group; and
- arrange adequate protection for, maintain its own books and records and perform its own reconciliations in relation to approximately £16.5 billion of safe custody assets for which it was responsible as custodian and/or custodian.

Further, Barclays did not implement or keep up-to-date adequate policies, procedures and monitoring with regard to external custody accounts, and it failed to maintain a complete and accurate record of its role in the custodial chain. It failed to capture account details accurately or in a manner consistent with the way in which the assets were being held. Failures also led to Barclays not applying the CASS rules when opening 95 custody accounts in 21 different countries.

In the accompanying press release, David Lawton, Director of Markets at the FCA, said that Barclays' lack of focus on the rules was unacceptable. Tracey McDermott, Director of Enforcement and Financial Crime at the FCA, said that Barclays had failed to apply the lessons from previous enforcement actions and numerous warnings across the industry, which exposed its clients to unnecessary risk.

### 2. RBS and NatWest receive fines for failures in mortgage advice processes

On 27 August 2014, the FCA published a final notice and accompanying press release for the fine issued to Royal Bank of Scotland plc ("RBS") and National Westminster Bank plc ("NatWest") for serious failings in their advised mortgage sales business. The fine of £14,474,600 was issued to both firms jointly and would have been for £20,678,000 had they not agreed to settle at an early stage of the investigation.

The FCA states in the final notice that between 1 June 2011 and 31 March 2013 both RBS and NatWest were in breach of Principle 9 (relationships of trust with customers) and Principle 2 (Skill Care and Diligence) of the FCA's Principles for Businesses ("PRIN") as set out in the FCA Handbook, as well as Chapter 4.7 of the Mortgages and Home Finance Conduct of Business Sourcebook ("MCOB") of the FCA Handbook which relates to advised sales. The FCA found that both firms had breached Principle 9 (and MCOB 4.7) through a failure to take reasonable care to ensure the suitability of advice provided to customers. During the same period, three reviews of the sales process were carried out, which identified serious problems in the advised business, including inadequacy of processes for assessing affordability and monitoring of advised sales. The FCA also found that RBS and NatWest had breached Principle 2 through failing to remedy problems identified by the previous regulator, the Financial Services Authority ("FSA"). Worse, both firms failed to communicate any changes made to the advised sales process to their sales advisors and no staff training in support of these changes was provided either.

In the accompanying press release, Tracey McDermott, FCA Director of Enforcement and Financial Crime said that taking out a mortgage is one of the most critical financial decisions that a consumer can make and, therefore, it is absolutely crucial that any advice provided is fit for purpose. She explained that both firms only started to take steps to put things right almost a year after concerns had been raised by the FSA in November 2011. In reaching its decision this time, the FCA took into account the previous disciplinary history of both firms stating that they had been fined six times over the last four years.

## 3. Deutsche Bank's London Branch hit with £4.7m fine for transaction reporting failures

On 28 August 2014, the FCA published a final notice and accompanying press release relating to the fine it imposed on Deutsche Bank AG (London Branch) of £4,718,800 for failure to report 29,411,294 Equity Swap Contracts For Differences transactions between 5 November 2007 and 19 April 2013. It states that the Bank, in failing to make these transaction reports, had breached the rules set out in Chapter 17 of the Supervision Manual ("SUP") of the FCA's Handbook. Had the Bank not agreed to settle at an early stage of the FCA Investigation, it would have received a fine of £6,741,215.

The FCA stressed the importance of transaction reporting, stating that accurate and complete reporting is essential to enable the FCA to meet its operational objective of protecting and enhancing the integrity of the UK financial system. Such reports are used to detect and investigate suspected market abuse, insider trading and market manipulation.

In the accompanying press release, Tracey McDermott, FCA Director of Enforcement and Financial Crime, stated that the bank is a serious market participant responsible for reporting millions of transactions every year and there can be no excuse for its failure to get this right. In addition, the FCA considered this failure to be of particular seriousness since it had communicated the importance of accurate transaction reporting to firms often, as well as publishing during the period relevant in this particular matter, a number of enforcement actions taken in relation to similar failings by other firms. The FSA had also issued the Bank with a private warning on 3 June 2010 relating to similar transaction reporting failures. Ms McDermott warned other firms that they should be in no doubt about the FCA's "continued focus on this issue".

## 4. FCA fines Stonebridge International Insurance Ltd for poor product sales practices

On 7 August 2014, the FCA published the final notice it issued to Stonebridge International Insurance Limited ("Stonebridge") which hands the firm a fine of £8,373,600 for failings in its telephone sales practices connected with accident insurance products. Stonebridge agreed to settle with the FCA at an early stage of its investigation, thereby qualifying for a discount. The penalty otherwise would have been £11,962,317.

The FCA found that between 1 April 2011 and 31 December 2012, Stonebridge had breached Principle 3 (Management and Control) and Principle 6 (Customers' Interests) of the FCA's Principles for Businesses ("PRIN"), as set out in the FCA's Handbook. The breaches related to telephone sales of personal accident, accidental death and accidental cash plan insurance products which were underwritten by Stonebridge and sold to customers on the firm's behalf through various authorised intermediaries. The customer target market was identified as being middle-to-low income market (those individuals without higher education or professional qualifications) located in the UK and various other European jurisdictions.

However, Stonebridge did not take reasonable steps to ensure that its customers were treated fairly.

It designed scripts for telephone sales to be used by its outsourcing firms which did not offer clear, fair and not misleading information. It also failed to put in place adequate systems of oversight for its outsourcing firms and was found to have poor systems and controls, including findings that its compliance department was inadequately resourced. The FCA found that Stonebridge's post-sale cancellation process presented customers with barriers to cancellation, which resulted in them not succeeding in cancelling policies despite several attempts to do so.

The FCA believes that up to 486,444 customers across the UK and the EU could be affected by the mis-selling, and Stonebridge is now carrying out an independent view of its past sales. It has also stated that it is contacting affected customers to ascertain whether they should be compensated as a result of the poor sales practices.

Further, Stonebridge has ceased distribution of these products in the UK and EU, made changes to its governing structure and operating board membership, and it has also replaced its executive management team. The firm has put in place new policies and procedures to manage its prudential and conduct risk. In the press release which accompanied the publication of the final notice, Tracey McDermott, reiterated that firms must take responsibility for their outsourcing arrangements and ensure that they treat customers fairly.

## 5. Fine and ban handed to former Senior Partner at St James's Place Wealth Management PLC

On 16 September 2014, the FCA published the final notice it issued to Peter Carron, formerly a senior partner at St James's Place Wealth Management plc ("SJPWM") relating to his fine of £300,000 and prohibition on performing any function in relation to any regulated activities.

The FCA found that between 6 November 2004 and 21 June 2010, Mr Carron advised 11 clients to invest a total of £2.4 million in three companies of which he was the director and majority shareholder: Primrose Associates Limited, Evaluate Technologies Limited and Comment Technologies Limited ("the Companies"). He did not disclose this fact to the clients, who came from his existing SJPWM client base and who had used him as their financial advisor whilst he was at SJPWM. Mr Carron told the clients that they would receive a guaranteed return of 10% on their investments. However, they lost approximately £2.2 million when the companies went into liquidation between 6 May and 2 August 2010. SJPWM agreed to pay the investors £1.9 million in compensation.

In the final notice the FCA state that Mr Carron breached Statement of Principle 1 of the FCA's Statements of Principle and Code of Practice for Approved Persons ("APER") in the FCA Handbook because he failed to act with honesty and integrity when he:

- Abused his position as senior partner at SJPWM through recklessly failing to disclose to clients that he owned and controlled the Companies, and in also misleading them into investing in the Companies on the basis that the investments were approved, authorised or otherwise endorsed by SJPWM, when in fact they were not.
- Deliberately advised clients to invest in the Companies, regardless of whether the investment was suitable for their needs and he actively did not consider whether there were alternative investments which were more suitable.
- Failed to provide clients with adequate information on investments including any risk warnings.

- Did not communicate clearly to clients which company they were investing in or what the funds were actually for. He also continued to advise clients to invest in the Companies from 2009 when he knew that they were already in financial difficulties.

The FCA states that it views these actions as deliberate and reckless, exposing clients to an excessive risk of financial loss which spanned a period of more than five years. The FCA also published an accompanying press release with the final notice.

## 6. FCA bans director for dishonest promotion of high-risk UCIS to retail customers

On 29 August 2014, the FCA published a final notice issued to Craig Cameron which imposes upon him a fine of £350,000 and bans him from performing any function in relation to any regulated activity carried on by a firm in the Financial Services Sector.

The notice states that between 1 January 2005 and 2 January 2006 Burlington Associates Limited, where Mr Cameron was a former director, was the appointed representative of a network. During early 2005, Mr Cameron helped to set up three high-risk unregulated collective investment schemes ("UCIS") which would invest in new property developments in Croatia, Bulgaria and Montenegro. These UCIS were then duly promoted to thousands of retail investors and little was done to ensure that any investors were eligible for such promotions.

The FCA found that Mr Cameron had:

- Involved Burlington Associates in promoting and arranging investments in these UCIS without the knowledge of the firm's principal. Further, the arrangement was in breach of the firm's agreement with its principal which did not permit it to conduct UCIS business.
- Recklessly devised a structure and participated in a process for promoting and arranging investments in the UCIS which was likely to provide false assurance to customers, potential customers and others that the firm was permitted to carry on UCIS business.
- In addition, Mr Cameron knew that such activities would be likely to result in the sale of the UCIS to investors for whom such products would be unsuitable.

The FCA stated that Mr Cameron stood to derive personal benefit from the firm's role in promoting and arranging the UCIS through commission and fees received. Approximately 880 investors invested a total of £30 million in the UCIS which then fell into financial difficulties from 2006. It is likely that any such investments are virtually worthless now. As a result, the FCA found that Mr Cameron had failed to act with honesty and integrity in his role as director of Burlington Associates Limited which was in breach of Statement of Principle 1 of the FCA's Statements of principle and Codes of Practice for Approved Persons Sourcebook ("APER") in the FCA Handbook.

The accompanying press release explains that the FCA has previously taken action against two other individuals, Jeffrey Bennett and John Leslie for failing to oversee the roles of their firms in the same UCIS sales adequately.

## 7. Insider dealers receive confiscation orders totaling £3.2m

The FCA has announced that confiscation orders totaling £3,249,488 have been made in a case brought it and heard at Southwark Crown Court between 10 September 2014 and 15 September 2014 against Ali Mustafa, Pardip Saini, Paresh Shah, Neten Shah, Bijal Shah, Truptesh Patel and Richard Joseph. The confiscation orders were made by His Honour Judge Pegden QC.

Mr Mustafa, Mr Saini and Mr P Shah were sentenced to three years six months imprisonment on 27 July 2012, together with Mr N Shah, who was sentenced to 18 months, and Mr B Shah and Mr Patel who were sentenced to two years all for offences relating to Insider Dealing under the

Criminal Justice Act 1993. The defendants were convicted of making a combined profit of £732,044.59 connected to trading which took place between 1 May 2006 and 31 May 2008.

In March 2013, Richard Joseph whose activities resulted in a net profit of £591,117 connected with trading which took place between September 2007 and July 2008, was also sentenced to four years' imprisonment for Insider Dealing. Additionally, Mr Joseph was ordered to pay a costs order of £200,000, and Mr N Shah was ordered to pay costs of £100,000.

The amount confiscated exceeds the profits generated due to the fact that the confiscation regime enables the court, in specific circumstances, to assume that the profits from other trading which took place within the same period represent the proceeds of crime.

If you have any questions concerning the material discussed in this bulletin, please contact the following members of our financial regulation practice group:


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