

REGULATORY OVERVIEW FOR 2021

In this Bulletin we give a brief overview of the main areas the FCA is expected to focus on in the next year. This subject was addressed at a Griffin technical forum in February 2021. We focus here on the key areas of enforcement, crime, non-financial misconduct and operational resilience. We also look at Serious Fraud Office (“SFO”) prosecution developments.

FCA Enforcement

There were 646 open FCA investigations during 2019/20 and that number remains largely the same to date. This reflects the FCA’s continuing focus on pursuing firms for misconduct.

The costs of defending a firm against an FCA investigation can be very high. The trend is that these costs are increasing. During the period 2019/20 the average life cycle of an FCA enforcement case increased from 18 to 24 months. The average cost of defending a case has almost doubled (from £103k to £229k). One factor that is increasing costs is the growing volume of information that the FCA now requests during an investigation. In some cases, hundreds of thousands of documents need to be disclosed to the FCA.

There is an increased risk of an enforcement investigation if consumers, particularly vulnerable consumers, are buying products that are unsuitable for their needs. Firms should regularly review the adequacy of their procedures to comply with conduct requirements. Otherwise, a firm will be exposed to the substantial cost of regulatory investigations, even if, ultimately, it transpires there has been no wrongdoing by a firm.

Financial Crime

The single largest fine imposed by the FCA for the 2019/2020 period was for money laundering breaches and totalled £102.2m. This is a clear signal that the FCA remains committed to combatting financial crime.

A key area of note is that, over the last few years, the FCA together with the SFO, has taken action against insurance intermediaries for failures to adequately manage corruption risk. For example, recent cases involving Commerzbank and the 1MDB scandal (involving wide scale corruption in a state owned Malaysian investment vehicle) highlight the FCA’s corruption concerns. Key points of note are:

1. The investigations spanned multiple jurisdictions, which is a growing trend in regulatory cases, where international agencies work together to achieve coordinated outcomes.
2. In these cases the FCA found failures to act upon clear warnings regarding weaknesses in firms’ anti-financial crime systems and controls. For example, the FCA said Commerzbank had failed to take reasonable steps to address concerns with its automated system for monitoring money laundering. 40 high risk countries were found to be missing from its money laundering system.

3. The FCA also looks at the role of a firm's committees with responsibility for assessing financial crime exposures. In the 1MDB case the FCA found (i) there had been failures to ensure appropriate information regarding financial crime risk was escalated to relevant committees and (ii) minutes of committee meetings did not contain enough detail on the rationale for decisions.
4. Firms should assess corruption risk factors in their relationships with clients and third parties.
5. These cases also highlight the importance of ensuring that employees are trained to spot and act on financial crime risks.

It is important to note that even where there is no evidence a financial crime has been committed (as in the Commerzbank case) the FCA said that a lack of compliance with FCA principles warranted a sizable fine.

Non-Financial Misconduct

Non-financial misconduct is likely to be a significant focus for the FCA in the years ahead.

Behaviour such as bullying, victimisation, harassment and discrimination fall under the FCA's definition of non-financial misconduct. There may be serious consequences for firms that do not take appropriate steps to ensure they have a "healthy culture" where staff are, and feel, "psychologically safe."

The FCA considers appropriate leadership as key to addressing non-financial misconduct.

The SMCR emphasises senior managers' responsibility for areas under their control and a failure to address non-financial misconduct could lead the FCA to consider whether the individual is fit and proper for a senior role.

The FCA has identified leadership, policies and governance as key factors in defining a firm's culture. For example, a firm's remuneration policies should not drive or encourage poor behaviour. Also a firm's approach to the well-being of personnel and issues such as bullying are current hot topics for the FCA.

Serious Fraud Office – SFO:

The SFO is often viewed as a 'sister agency' to the FCA: it plays a significant role in the FCA's anti-financial crime agenda. The SFO prosecutes serious financial crime.

A recent development in criminal prosecutions brought by the SFO is the introduction of deferred prosecution agreements ("DPA"). A DPA provides a mechanism, open solely to corporations subject to criminal prosecutions, which allow settlement with the SFO to avoid a criminal trial. At the SFO's invitation, the corporation settles with the SFO and enters into a DPA. The corporation accepts liability for its criminal conduct, pays a significant financial penalty and agrees to monitoring of its anti-crime controls. The costs of this monitoring are borne by the firm. This avoids an expensive and unpredictable criminal trial.

Operational Resilience

The FCA defines Operational Resilience as the ability of a firm to either prevent or recover and learn from operational disruptions. The importance of operational resilience has been significantly amplified in the face of the current pandemic.

Firms are obliged to consider how disruption to the services they provide can have impacts beyond their own commercial interests. In order to satisfy the FCA's core requirements for operational resilience, firms must:

- Identify areas where disruption could result in customer detriment and set tolerance levels for and mitigants to such disruption
- Ensure they can continue to deliver their services during severe but plausible disruption scenarios.

2021 PREDICTIONS – A Summary

The areas mentioned above are not new. The FCA will always continue to focus on the prevention of financial crime and investigate serious misconduct when it occurs. That said, it is notable that the defence costs of an FCA investigation is an increasing risk for firms. Operational resilience, to ensure customers' needs are addressed during periods of disruption, is also very topical in the current global pandemic.

One area to “watch this space on” for new developments is the FCA's focus on firm cultures, leadership and non-financial misconduct. The FCA is likely to take action against senior managers if a firm does not have a culture that (i) is “psychologically safe” for staff to work in and(ii) promotes positive outcomes for customers.

This bulletin is for general information purposes only and does not provide a comprehensive or complete statement of the law relating to the issues discussed nor does it constitute legal advice. In addition, by its nature, this bulletin may be superseded by subsequent regulatory or legal developments. Professional advice should be sought where appropriate in relation to any particular circumstances.

All rights reserved. No part of this publication may be reproduced in any material form, whether by photocopying, scanning, downloading to computer or otherwise without the written permission of Griffin Managers except in accordance with the provisions of the Copyright, Designs and Patents Act 1988.