FCA
Practitioner Panel

THE FCA PRACTITIONER PANEL

Response to HM Treasury's Enforcement Decision Making at the Financial Regulators – Call for Evidence

4 July 2014

1. Introduction

The FCA Practitioner Panel (the Panel) was established by the Financial Services and Markets Act (as amended) to represent the interests of regulated firms and to provide input to the Financial Conduct Authority (FCA). The Panel provides advice to the FCA on its policies and strategic development of financial services regulation.

Whilst we have not sought to respond to every question in the call for evidence, we provide below some comments and observations with regard to HM Treasury's review of enforcement decision making processes at the financial regulators.

2. Executive Summary:

- The Panel is overall supportive of the FCA's credible deterrence strategy but, following the creation of the new regulators and their relative areas of focus, would welcome a refresh in its application with regard to proportionality, transparency and disclosure.
- To avoid undermining trust in firms and the industry more generally, the tone and content of communications from the regulators relating to the outcomes of enforcement action need to be balanced and factual, and should demonstrate an appreciation of their audience base.
- The Panel would welcome additional clarity regarding the PRA's enforcement process.
- The Panel considers that improvements might be made to the current FCA enforcement process, such as permitting earlier discussion between the practitioners or firms subject to the enforcement process and senior level staff at the regulator. As part of the decision-making process regarding how best to deal with non-compliance with regulatory requirements, the regulator should also give due consideration to where firms have self-reported or already taken remedial action.
- A settlement process is generally in the interest of the industry and the regulators, although benefits might be derived for all parties by engaging in discussions sooner in the settlement process, and for representations to be heard earlier.
- The Panel is supportive of the RDC process overall and considers that it is generally valued in practice.
- More broadly, we would observe that we are aware of instances where the FCA has sought for firms to go further on actions which were pre-agreed and incorporated into legal agreements relating to remediation exercises. It is important that if legal agreements are the FCA's preferred approach, the regulator follows the terms agreed. This supports trust between the regulator and firms, and enables all the parties involved to operate in an environment which provides certainty.

Panel response:

Question 1: Do current enforcement processes and supporting institutional arrangements provide credible deterrence across the spectrum of firms and individuals potentially subject to the exercise of enforcement powers by the regulators? If not, what is the impediment to credible deterrence and where does it arise?

The Panel is overall supportive of the FCA's credible deterrence strategy. The Panel also considers that enforcement action is taken very seriously by practitioners and firms who, as demonstrated by the results of the Panel's 2014 industry survey, generally watch and learn from enforcement action in their sectors.

As the credible deterrence strategy was, however, established under the FSA, we would welcome a refresh of its application with regard to proportionality, transparency and disclosure following the creation of the new regulators, and given the FCA's consumer focus.

Whilst there is a delicate balance between the need to be transparent and the risk of undermining trust in individual firms and the industry more generally, we consider that improved transparency and a robust internal procedure is required for the FCA's approach to external communications about enforcement action. To ensure consistency with the regulator's statutory objectives, communications need to be balanced, objective and fair, not headline driven, and to demonstrate an appreciation of the broad audience base.

The regulator should state clearly why a firm has been fined and communicate the details of any breaches, but the tone of communications should be factual and demonstrate an awareness of the potential implications for firms, the industry, consumers and markets. It would also be helpful for the regulator to provide clarity in its communications regarding the timeframe of when the enforcement issues were identified, as these are often historic, and any remediation activity the firm has undertaken to ensure that the issues do not happen again. That the regulator has had to engage in enforcement action should not be viewed as a media 'win' for anyone concerned, least of all any customers who may have suffered as a result of the issues.

Question 3: Should the PRA say more publically about its enforcement processes? In particular, should the PRA publish enforcement referral criteria?

As the PRA's enforcement function is relatively new and differs from the FCA's (e.g. there is no RDC and it relies on internal decision making committees), the Panel considers that the PRA should provide all regulatory stakeholders with more information on its enforcement processes so they can better understand how it operates. It is critical that financial services can operate with certainty. Industry and customers will ultimately be better served if both regulators operate their enforcement functions in a clear, coordinated and predictable manner.

Question 6: Do any suggestions for improvement or reform relate to the referral stage, the investigation stage, the decision making stage or all three stages?

The Panel is concerned that the FCA enforcement process may not always be perceived as fair by practitioners and firms. This could be due to the nature of

the current process and/or the view that enforcement action seems to follow automatically from self-reporting an issue. As a result, there is risk that firms will be deterred from self-reporting and, indeed, that firms who do not self-report will avoid enforcement action.

More broadly, we would observe that we are aware of instances where the FCA has sought for firms to go further on actions which were pre-agreed and incorporated into legal agreements relating to remediation exercises. It is important that if legal agreements are the FCA's preferred approach, the regulator follows the terms agreed. This supports trust between the regulator and firms, and enables all the parties involved to operate in an environment which provides certainty.

The Panel considers that improvements could be made to the current FCA enforcement process, such as:

- By introducing formal opportunities for firms to engage with the regulators at a senior level, both before an issue is referred to enforcement and ahead of starting any settlement process. This would update the current practice whereby firms do not have unmediated access to the regulator's senior decision makers to discuss the key facts of the case. Instead, dialogue is usually with the enforcement team.

- By introducing a formal break in the enforcement process, at which time a decision is taken by senior level staff at the regulator as to whether or not enforcement action should be taken. Decisions should be made on the basis of published criteria - requiring not only an assessment of whether the case is winnable, but also whether it is fair to take the case in all the circumstances, including consideration of any action which the firm has already taken to resolve the issue.

- Where a company acknowledges that it is has made a mistake and is ready to apologise and make redress, resolution might be achieved much more quickly if there was simply a joint resolution press notice straight away. Taking enforcement action in those circumstances can serve to delay the point of resolution and redress, which is detrimental to the consumer. This approach, however, may require some cultural change at the FCA.

- By introducing a clear mechanism for monitoring the fairness, speed, transparency and efficiency of the enforcement process (both for the FCA and RDC), with oversight from the FCA Board (whilst recognising that it cannot be expected to intervene in individual decisions).

- Giving credit for the self-reporting of issues and actions taken by firms to remediate concerns (for example, a discount could be applied to any fines for undertaking remediation work, as well as for early settlement). The present system seems to treat and penalise those who self-report and proactively manage issues in the same way as those who do not.

Question 9: Are there sufficient opportunities for individuals and firms to make representations?

The Panel considers that subjects of enforcement action should have the ability to make meaningful representations at appropriate times throughout the process but, in particular, before and during Stage 1 of the settlement process. This would require greater transparency from the FCA early about its case and the

evidence relied upon. Where the FCA provides increased transparency, this has generally been found to result in faster agreement of the points in issue.

Question 12: Settlements are faster and more efficient than exhausting the decision making process. They often deliver fairness to consumers by providing earlier opportunity for redress. Is it appropriate to give a discount for early settlement? Should there be any types of case where such discounts are not available? Could the settlement process be changed to offer clearer incentives to settle after the time limit for receiving a 30% discount has expired? Do you agree with the incentives given?

The methodology behind the calculation of fines should be transparent and consistently applied, although the Panel considers that care should be taken not to replace the current system with formulaic penalties.

The Panel believes that it is firmly in the interests of the regulated sector, regulator and consumers for a matter subject to FCA enforcement to be settled as expeditiously as possible with appropriate regard to fairness, proportionality and transparency. We would suggest fairness in the process could be improved by allowing the introduction of new rights for a firm/individual to seek to agree part-settlement of a case and the inclusion of one or more without prejudice settlement meetings to seek early resolution and open dialogue.

Question 13: Do the current approaches to settlement also deliver fairness to firms and individuals subject to enforcement action, bearing in mind that settlement is a voluntary process? If not, what improvements could be made better to balance the interests of all parties?

Currently, there is limited transparency from the FCA during the 28-day period when deciding on the size of the settlement and there is no access to the senior decision makers before they sign off on a settlement.

The 28-day period to accept settlement offers can put undue pressure on firms and individuals, particularly where it is hoped to secure an agreement with an overseas regulator at the same time. The Panel considers that the FCA should publish the basis on which it will grant extensions to this period, rather than simply saying that they will be “exceptional”.

Question 16: Almost 40% of cases considered by the RDC are subsequently referred to the Upper Tribunal. Does the RDC process duplicate too much the Tribunal process for firms and individuals who are likely to refer a Decision Notice to the Tribunal? What changes could be made to make the process more proportionate and/or efficient, consistent with the delivery of the regulatory objectives?

As the concentration of critical decision-making powers sits with relatively few people, this may not allow adequate room for objectivity. Whilst not all enforcement cases reach this stage, the Panel considers that the RDC is an important part of the enforcement process, which is generally valued in practice and the representation from impartial members is positive.

The Panel would not wish to see the RDC process removed and also believes there is an advantage to the RDC meetings remaining private. If they were made public, the frequency with which modifications are made to decisions would likely diminish.

Question 17: What more could the UK learn from international practice?

In terms of international comparisons we would not want to advocate for the US system, however, Australia seems to get resolutions much more quickly and it may be worth studying how and why that is the case.