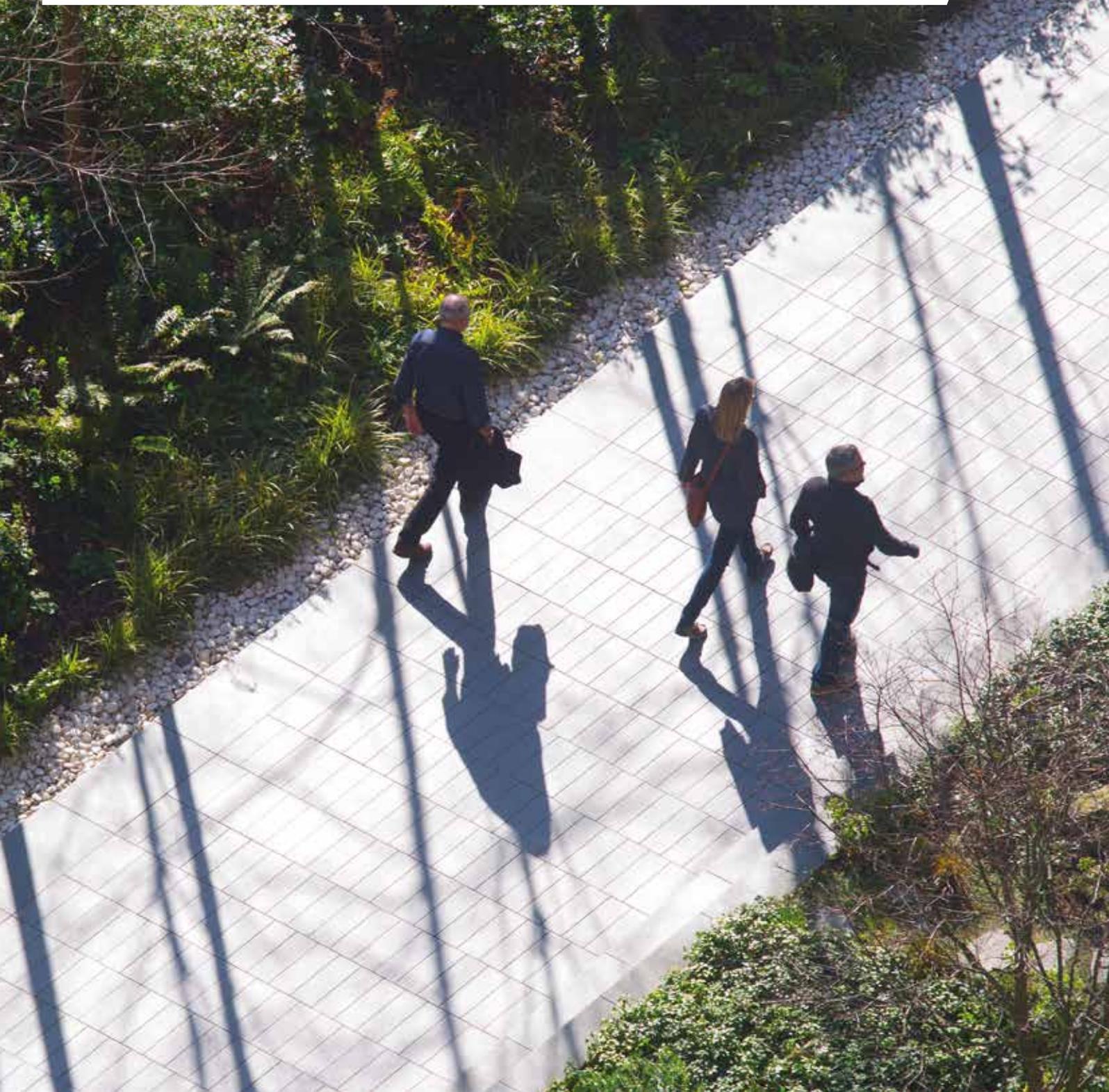


Business Plan
2017/18





Business Plan

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Setting the scene

Consumers

16m+

people have under
£100 in savings

(Money Advice Service)

£7.3bn

cumulative lending
in peer-to-peer platforms

(peer2peer Finance Association)

20.4m

of the UK's 27m households
have contents insurance

(Association of British Insurers)



£16bn

withdrawn from
cash points each
month

(Link, 2016)

A changing population

850,000

people living with dementia,
including **1 in 6** over the
age of **80**

(Alzheimer's Society)

£9.2bn

withdrawn from pensions
by **970,000** consumers since
April 2015

(HMRC & FCA)

66% of workers

now members of a workplace pension

(The Pensions Regulator)



Our work

£26.2bn

paid in redress for PPI to date



Over

115,000

consumers helped
by our contact centre
in 2016

63m

circulation of newspapers
carrying our ScamSmart
warnings

UK financial services

£4.3tn

assets overseen by
UK fund managers

(FCA)

250+

Foreign banks in London –
more than any other centre

37%

of the global market for
FX trading - largest in the world

(Bank for International Settlements, 2016)

12%

of total
economic output

(TheCityUk)

Our priority work for the year ahead



Our cross-sector priorities

Firms' culture and governance

- Consult on the accountability regime for all FSMA firms
- Continue to review our regulatory framework that governs remuneration

Financial crime and anti-money laundering (AML)

- Prepare to take on responsibility for reviewing the quality of professional bodies' AML supervision
- Investigate how new technology can improve the efficiency of AML processes
- Roll out a further ScamSmart campaign warning of investment fraud

Promoting competition and innovation

- Publish resources to help firms developing 'robo-advice' services
- Engage with regional and Scottish FinTech hubs
- Investigate how near and real-time compliance monitoring can reduce the regulatory burden

Technological change and resilience

- Establish cyber co-ordination groups across five sectors to share experiences and foster innovation
- Undertake technology and cyber-capability assessment on all firms considered 'high impact'
- Analyse resilience risks in major initiatives, including ring fencing and the Payment Services Directive II

Treatment of existing customers

- Analyse the effect of wake-up packs on consumers' decisions at the point of retirement
- Look at how firms treat borrowers whose interest-only mortgages are approaching maturity

Consumer vulnerability and access

- Publish our 'Consumer Approach' to define our overarching approach to addressing UK consumers' needs
- Continue our work in the consumer credit sector, including our continued focus on high-cost credit and overdraft



Our sector priorities

Wholesale financial markets

- Ensure the new MiFID II regime is implemented effectively
- Continue to implement remedies to improve competition in investment and corporate banking
- Introduce changes to improve the effectiveness of primary markets

Investment management

- Consult on proposed remedies in the asset management market
- Review our policy options in relation to fund liquidity

Pensions and retirement income

- Propose a package of remedies to improve competition in the retirement income market
- Undertake initial work looking at the non-workplace pensions market
- Review non-advised drawdown sales

Retail banking

- Work with the PRA, Bank of England, the Treasury and the larger banks to support the implementation of ring-fencing
- Launch a strategic review of retail banking business models
- Launch a communication campaign to raise awareness and understanding of the PPI complaints deadline

Retail lending

- Set out our analysis and preliminary conclusions on the mortgage market
- Continue to monitor the debt management sector to ensure that it is fit for purpose
- Undertake an exploratory piece of work on the motor finance industry

General insurance and protection

- Conduct a review of pricing practices in general insurance
- Assess how effectively competition is working in the wholesale insurance market

Retail investments

- Assess the market for investment platforms and what we can do to improve competition
- Assess the developing market for automated advice models
- Undertake further work to address the risks in the Contracts for Difference market

Chairman's foreword

John Griffith-Jones

Welcome to our 2017/18 Business Plan. It sets out our work programme and priorities for the coming year.



It explains how we plan to work on our three operational objectives of protecting consumers, promoting competition and enhancing market integrity to meet our overarching strategic objective of making markets work well.

A fundamental part of our Business Plan is the Risk Outlook. It identifies key trends in, and implications for, the markets and firms we regulate, as well as emerging risks we may need to respond to in the future. It explains the wider context within which we regulate and therefore how we decide upon our priorities for the next year.

As is particularly clear this year, many of the biggest risks to markets and consumers are outside our control. International events, demographic changes, the impact of the UK's decision to leave the EU and the course of the UK economy are just four relevant examples. However, while we cannot control them, we cannot afford to ignore them. Quite the opposite; we are required to be a regulator for all seasons. The FCA has learned over the past four years that there is great merit in predictable regulatory outcomes, requiring us to allocate our resources flexibly in response to new developments.

By contrast, most of the risks to the good conduct of financial services firms are longer term, ongoing and change little from year to year. We remain wholly committed to high standards of conduct in the UK's global capital markets and in domestic wholesale and retail financial services businesses.

The central function of our work will remain our challenge of poor conduct in the industry. There is a clear link between poor culture and poor conduct, and industry must continue its work to achieve and embed its own cultural change. This should reduce the need for regulatory intervention, rebuild trust in markets and align firms' business models and practices more closely with their users' needs. So it is no surprise that proportionate supervision, effective market oversight, studies into competition and, where necessary, enforcement are at the core of this Business Plan. Combined with a regular and productive dialogue with industry and consumers, we continue to aim for constructive deterrence, seeking wherever possible to prevent things going wrong in the first place.

Of the increasing risk areas that we have identified, one in particular stands out – cyber resilience. Cyber-attacks are increasing in number, scale and sophistication.

A growing number of firms are also outsourcing processes as their business models adapt to cut costs and try to keep pace with evolving services and systems. And varying levels of investment in legacy systems are increasing market vulnerability to disruptions and cyber-attacks. Firms' technological resilience has significant implications, both for markets and for their customers. Therefore it needs to be, and stay, high on all of our agendas.

The flipside of cyber risk is, of course, the opportunities that technological innovation can offer. At its best, technological innovation has the potential to reduce the costs and widen accessibility of products and services. As such, it presents opportunities to fundamentally change the way financial products and services are delivered. We are actively working to support this type of development in an increasing number of projects.

A closing word on Brexit. I am regularly asked whether the FCA has enough resource and enough involvement. On the former, our planning includes the mindset of doing whatever is needed to fulfil the duties required of us as the process becomes clear. On the latter, we are already making our considerable technical knowledge available to the Government, and we will continue to do so throughout the process.

2017/18 is already looking like it will be an eventful year. I trust that all of our stakeholders find this Business Plan useful. I look forward to working with you as we put it into action.



John Griffith-Jones
Chairman,
Financial Conduct Authority



There is a clear link between poor culture and poor conduct, and the industry must continue its work to achieve and embed cultural change.



Chief Executive's introduction

Andrew Bailey

The FCA regulates the UK's financial services sector to ensure that markets work well for individuals, businesses and the UK economy as a whole. This Business Plan explains our priorities over the next year.



This year's Business Plan represents two firsts – my first as the FCA's Chief Executive and the first time we have published our Business Plan alongside our Sector Views. We are also publishing our Mission document at the same time. Together, they provide a more complete picture of the way we identify and assess risks in the sectors we regulate, and how and why we choose our Business Plan priorities.

These priorities reflect the speed and variety of changes affecting both wider society and financial services. Firms are being challenged by rapidly evolving user needs, as well as heightened uncertainty in the economic and political outlook. They need to adapt and compete to meet these challenges successfully. Both they and consumers require markets that are stable, demonstrate integrity and are regulated effectively and proportionately.

The UK's decision to leave the European Union creates uncertainty for both the UK's financial industry and the FCA. Both we and the Government are keen to ensure that the financial services industry remains resilient and well placed to meet users' needs and thus make the most of opportunities in a post-Brexit world.

Leaving the EU inevitably creates a higher risk of disruption to our Business Plan priorities. So it is particularly important that we retain the flexibility to respond swiftly should we need to review them further.

The Business Plan explains the context, and desired outcomes for, our cross-sector priorities which, being longer-term in nature remain broadly consistent with the previous year's Business Plan. This year we also give more detail about our priorities in individual sectors.

However, there is an even stronger emphasis on consumer vulnerability and access to financial services. This priority runs across financial sectors, is an important part of our Mission and will also be a key focus of our forthcoming 'Consumer Approach' document.

This strategy will reflect consumers' growing responsibility for their own financial choices, at a time when these choices are becoming more complex. The social and economic implications of an ageing population, together with factors like continuing low interest rates and a rise in less secure forms of employment, are likely to have major implications for the pensions and retirement income sector. This Business Plan explains

our planned activities to encourage firms to address this growing need and ensure they provide consumers with the information they need to make suitable choices.

Firms themselves will always have the most important role to play in ensuring continuing trust and confidence in the UK's financial services. As well as embedding the Senior Managers and Certification Regime (SM&CR) we will also consult on our proposals to extend the accountability regime to all firms under the Financial Services and Markets Act. Our aim is to ensure firms are well prepared for implementation in 2018 and that we deliver a regime which is simple, proportionate and clear.

Implementing the Markets in Financial Instruments Directive II (MiFID II) allows us to introduce major reforms to improve resilience and strengthen integrity and competition in wholesale markets. The additional information we will get from firms when the Markets in Financial Instruments Regulation (MiFIR) is introduced next year will further increase the effectiveness of our market abuse work.

Large and thriving markets inevitably attract financial crime; it is an area where both we and firms must stay

vigilant. Last year we rolled out our Financial Crime Data Return and this year we will analyse the early responses to ensure we focus our supervision on the right firms. We will also continue to work closely with the Treasury on anti-money laundering (AML) policy as it transposes the 4th Money Laundering Directive into UK law.

We want to help firms avoid the unintended consequences of applying disproportionate AML measures, which risk excluding groups of consumers from access to financial services. So our work with banks will look more closely at how technology can help improve how they identify money laundering risk.

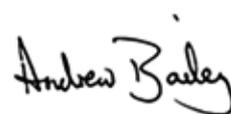
We will also expand our role in supporting technological innovation more widely, actively engaging with firms across the UK to find out more about specific areas of financial innovation and potential implications for regulation.

The FCA itself has been looking at ways to ensure we continue to provide value for money and give our staff the infrastructure they need to do their jobs as effectively as possible. We are moving our offices to The International Quarter in Stratford in 2018. This will allow us to bring all our

London staff together under one roof, provide a better technological specification that offers better value. We are focusing strongly on preparatory work this year to make sure the move has a minimal impact on our regulatory work.

These are just some of the priorities explained in this Business Plan. The vast majority of our resources will always be used for our core business. Authorising firms and individuals, maintaining oversight of firms' activities, conduct and behaviour, supporting effective competition and implementing and enforcing policy and rules are the bedrock of our regulation.

We look forward to working with our growing number of stakeholders in the year ahead to deliver financial regulation that serves the public interest in respect of the activities of firms, the experiences of consumers and the resilience of the UK economy.



Andrew Bailey
Chief Executive,
Financial Conduct Authority



Our role

We are the conduct regulator for 56,000 financial services firms in the UK, and the prudential regulator for over 18,000 of these firms. We also regulate financial markets in the UK and over 140,000 approved persons.

The FCA was established on 1 April 2013, taking over responsibility for conduct and relevant prudential regulation from the Financial Services Authority (FSA).

The Financial Services and Markets Act 2000 (FSMA) sets out our objectives.

We have an over-riding strategic objective to ensure that the markets we regulate function well. To advance this strategic objective we also have three operational objectives:

Operational objectives

Protect consumers:

To secure an appropriate degree of protection for consumers

Protect the integrity of financial markets:

To protect and enhance the integrity of the UK financial system

Promote competition:

To promote effective competition in the interest of consumers



FSMA also provides a competition duty for us which states that we must, so far as it is compatible with acting in a way that advances the consumer protection or integrity objective, discharge our general functions in a way that promotes effective competition in the interests of consumers.

FSMA also states that in discharging our general functions, we must have regard to the following regulatory principles:

1. Efficiency and economy

We are committed to using our resources in the most efficient and economical way. As part of this, the Treasury can commission value-for-money reviews of our operations.

2. Proportionality

We must ensure that any burden or restriction we impose on a person, firm or activity is proportionate to the benefits we expect as a result. To judge this, we take into account the costs to firms and consumers.

3. Sustainable growth

We must ensure that our decisions consider the desirability of sustainable growth in the economy of the UK in the medium or long term.

4. Consumer responsibility

We consider the general principle that consumers should take responsibility for their decisions.

5. Senior management responsibility

A firm's senior management is responsible for the firm's activities and for ensuring that its business complies with regulatory requirements. This secures an adequate but proportionate level of regulatory intervention by holding senior management responsible for the risk management and controls within firms. Firms must make it clear who has what responsibility and ensure that its business can be adequately monitored and controlled.

6. Recognising the differences in the businesses carried on by different regulated persons

Where appropriate, we exercise our functions in a way that recognises differences in the nature of, and objectives of, businesses carried on by different persons subject to FSMA requirements.

7. Openness and disclosure

We should publish relevant market information about regulated persons or require them to publish it in appropriate cases (with appropriate safeguards). This reinforces market discipline and improves consumers' knowledge about their financial matters.

8. Transparency

We should exercise our functions as transparently as possible. It's important that we provide appropriate information on our regulatory decisions, and that we are open and accessible to the regulated community and the general public.



Our aim is to ensure that the UK has an effective, innovative and trusted financial services sector that provides public value and meets the needs of all those who use it.





FSMA also requires the Treasury to make recommendations to us about the aspects of the economic policy of Government for which we should have regard. On 8 March 2017, the Treasury recommended that we take the following considerations into account in our assessment of the costs, burdens and benefits of potential rules or policies:

- Competition – the Government is keen to see more competition in all sectors of the industry, particularly retail banking.
- Growth – the Government wishes to ensure financial services markets make a positive contribution to sustainable economic growth in the UK economy in the medium and long term.
- Competitiveness – the Government wishes to ensure that the UK remains an attractive domicile for internationally active financial institutions, and that London retains its position as the leading international financial centre.
- Innovation – the Government is keen to see innovation in the financial services sector and how this can support the wider economy, through new methods of engaging with consumers of financial services and new ways of raising capital.

- Trade – the Government aims to encourage trade and inward investment to the UK that can help boost productivity and growth across our economy.
- Better outcomes for consumers – the Government wants to see financial services work in the best interests of the consumers and businesses they serve.

Building on the objectives, principles and recommendations that are given to us by law and by the Government, we develop our approach to regulation, including through our Mission. Our priorities, as set out in this Business Plan, are areas in which we believe we can make the most positive impact on our objectives, enhance public value, and take into account the principles of regulation and recommendations given to us by the Treasury.

Our approach to regulation

Our aim is to ensure that the UK has an effective, innovative and trusted financial services sector which provides public value and meets the needs of all those who use it. As the Mission explains, we use a decision-making framework to do this. We identify the harm, diagnose its cause

and extent, and then consider how best to remedy it. Our framework is focused on fully understanding the relevant market and carefully combining our tools to effectively deal with the identified harm.

Our remit is broad and covers a wide range of firms, from sole practitioners to multinational corporations, providing very different services to very different users. We carry out a correspondingly broad range of work to achieve our objectives. As financial services adapt to meet new needs in innovative ways, we need to ensure our regulation remains proportionate and effective.

Assessing harm, encouraging innovation

We take a forward-looking approach to assessing potential and emerging harm. We assess the extent, degree and type of harm posed to identify and respond promptly to emerging issues before they become more widespread. Where we identify harm in the market we will consider what the most appropriate action is to remedy it, including whether compensation should be provided and whether any enforcement action is necessary.

We believe that competition can deliver better results for consumers. We also believe part of our role is to support innovation. So we aim to ensure our regulation strikes the right balance between encouraging innovation that delivers consumer benefits, ensuring that consumers receive adequate protection, and that it is measured and does not create gaps in supply of products and services.

Transparent, accountable regulation

We want to be transparent with all our stakeholders about the decisions we take, the work we do, the outcomes we expect and how we measure our performance.

Measuring changes to outcomes that are a direct result of our intervention is challenging. It can often take several years before the impact is seen. This is because regulatory interventions rarely happen in isolation and because the harm we have prevented can be difficult to quantify. We do, however, monitor and report on a range of performance factors. These include the delivery of our Business Plan commitments, how well we have met our service standards and our operational effectiveness and efficiency.

This Business Plan also includes further details on the outcomes we aim to achieve in a number of priority areas and sets out the indicative success measures we use to assess progress.

An evolving way to measure our effectiveness

As we have said in our Mission, in the future we will use an assessment of the public value of our regulation to help measure how effectively we perform. Our Mission also states that we will use a three-tier approach to measure how we are doing. This will consider areas, including:

- assessing our internal operations against value for money criteria; the impact of our interventions
- measuring the impact of the interventions we make using our available tools; and outcomes in markets

Measuring performance against the statutory objectives

Ensuring that financial services markets function well

Statutory objectives	Securing an appropriate degree of protection for consumers		Promoting effective competition in the interests of consumers		Protecting and enhancing the integrity of the UK financial system	
	Outcomes	Outcomes	Outcomes	Outcomes	Outcomes	Outcomes
	Consumers have access to fair products and services, which deliver what they promise	Consumers can be confident that firms treat them fairly and fix problems promptly	Competition contributes to improved consumer outcomes	Firms compete on clear costs and consumers have the information they need	Consumers can trust firms to be fit and proper and for financial markets to be clean	A respected regulatory system that lets good firms know where they stand
Outcomes indicators	Fair products and services	Building trust and engagement	Value for money products and services	Competitive markets	Clean regulated markets	Attractiveness of market
	Improved consumer experience	Effective remedies	Getting better service	Clear and useful information	Low financial crime	Respected, joined-up regulation

This performance framework applies to both retail and wholesale markets. 'Consumer' here means not only retail consumers but also wholesale market participants.

- looking at markets and sectors as a whole to identify common root causes.

Another key tool we use to evaluate our performance is our outcomes-based performance framework. This framework breaks down our statutory objectives into outcomes that we want to see in the industry, indicators of how we will identify the success of these outcomes and performance measures. As our three-tier approach to measurement continues to develop, there may be changes to this framework.

Accountable and independent

We are an independent body, accountable to the Treasury and to Parliament.

We are funded by the firms we regulate. How much they pay depends on their size, what type of business they are and the activities they carry out.

Brexit and the FCA's role

The UK's withdrawal from the European Union will have important implications for the FCA over the coming years and will be a key area of focus. We have dedicated resource to co-ordinate and manage this work and are liaising closely with the Treasury and the Bank of England to ensure a smooth transfer of EU rules and legislation into the domestic framework, and ensure that the regulatory framework continues to operate without interruption following the UK's withdrawal from the EU.

We will provide the Government with technical support during the withdrawal process. As part of this we have identified five principles that will guide our advice to Government:

- Cross-border market access – open markets are an important enabler of healthy competition, supporting FCA objectives.
- Consistent global standards – across regions and jurisdictions in order to minimise the risks of regulatory arbitrage.
- Cooperation between regulatory authorities – a robust framework that provides for continued cooperation will be fundamental regardless of the outcomes of the negotiations.
- Influence over standards – the UK authorities should have influence over the standards that apply in the UK.
- Opportunity to recruit and maintain a skilled workforce – a diverse workforce with varied experience and the requisite expertise supports UK markets and firms that are well run and remain competitive.

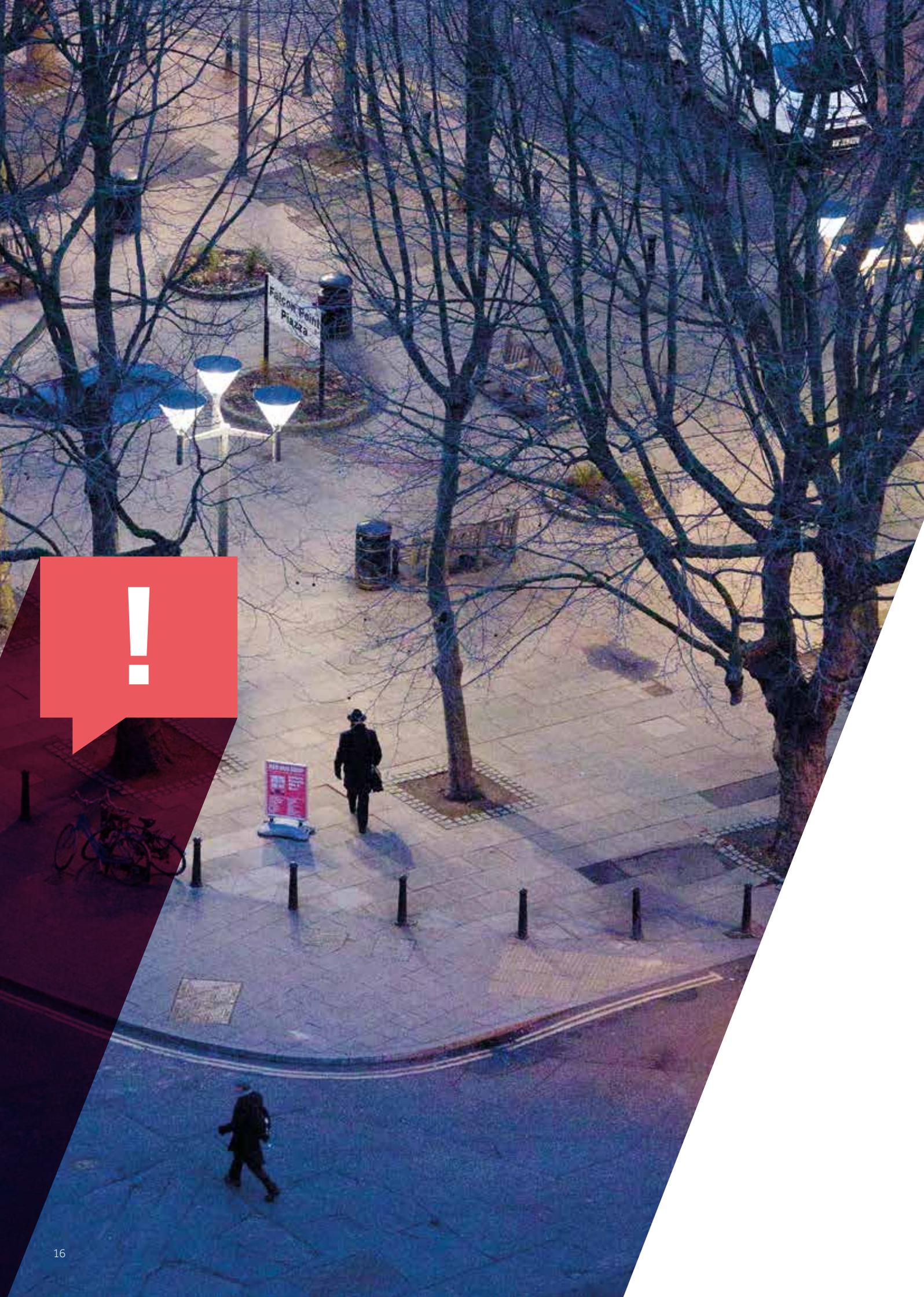
At the same time we are carefully considering what withdrawal from the EU may mean for our objectives. We are working to make sure that any risks to our objectives, including any operational challenges, are identified and addressed, and that the UK's domestic markets, and the role they play in supporting the wider economy, is safeguarded. The FCA stands ready to respond to any contingencies or new obligations arising as a result of EU withdrawal.

Existing financial regulation, much of which derives from EU legislation, remains in place until the Government and Parliament make any changes. We are also continuing with implementing the EU legislation that will come into force before the UK leaves the EU.



We want to be transparent with all our stakeholders about the decisions we take, the work we do, the outcomes we expect and how we measure our performance.





Risk Outlook

As part of our forward-looking approach to assessing emerging risks to our objectives, this chapter sets out our Risk Outlook – the medium to long-term trends that could influence the shape of the financial sector and the risks these pose to the FCA's objectives in the years to come.

An assessment of the global context, technological and socio-economic trends is an important tool in defining our priorities and strategy as a regulator. While the possible policy implications of many of the trends discussed here are beyond our regulatory remit, their consequences for firms and consumers could pose risks to consumer protection, market integrity and competition.

Many of the issues are long-term and more clarity over the potential for harm is likely to emerge over the coming years. As such, it may not be appropriate for us to address some of these issues now, and many of them may not crystallise. We include some of the more immediate issues in our cross-sector and sector priorities in this Business Plan, and these important trends will be reflected in our future business planning.

We use our risk framework, including our tolerance of risk to our statutory objectives, as a key tool in prioritisation and decision-making.

Our assessment of emerging risks is drawn from key trends in four areas that have an impact on the financial sector and our risk landscape: macroeconomic, social and environmental, technological, and firms and consumers. Overlaying these themes are geo-political dynamics that will affect some aspects of the financial services sector.

Macroeconomic

Understanding how the macroeconomic environment could affect the functioning of the financial markets is important for financial regulation. Changes in the macroeconomic environment can influence behaviour of market participants and firms' business models, strategies and financial soundness. Understanding the risks posed by changes in this environment is a key factor in developing our Sector Views and prioritising our work.



The UK's withdrawal from the European Union will have important implications for the FCA over the coming years and will be a key area of focus.



In the last year, economic and political events have added to domestic and global macroeconomic uncertainty. These changes could have a negative effect on the financial sector's ability to serve the real economy, and thus our ability to pursue our objectives.

Key trends

UK macroeconomic trends

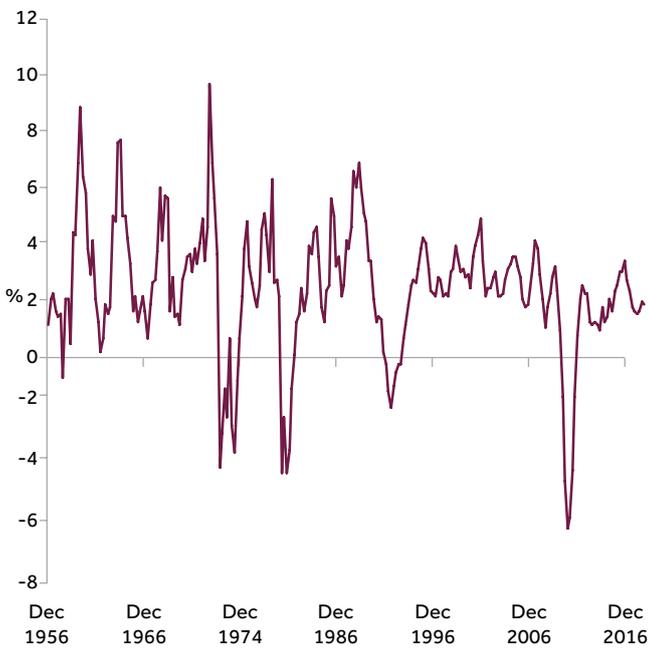
UK economic growth, while slower than in previous decades, has recovered since the aftermath of the financial crisis (Figure 1). Despite recovering faster than anticipated at the end of the crisis, UK output growth remains subdued.

The latest projections suggest that economic growth could slip below the post-crisis average over the next three years.¹

Private consumption has remained the main driver of growth. Credit conditions remain favourable and the cost of credit remains low, sustaining an increase in consumers' debt. Although secured lending growth has stabilised, consumer credit lending has continued to grow rapidly. UK household indebtedness is at a very high level by historical standards; the household cash savings ratio has fallen since 2010 (Figure 2). Households are vulnerable to any potential shocks to their employment, income or debt-servicing costs.²

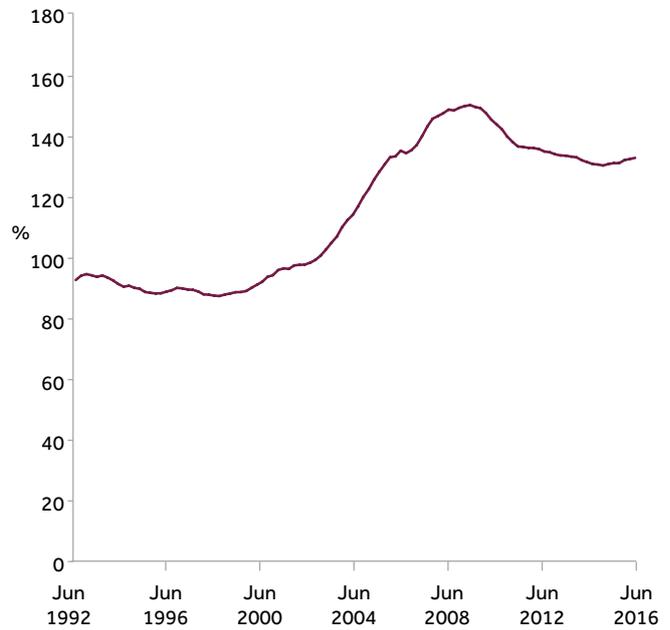
Unemployment has fallen since the financial crisis, while employment growth has been in less-secure forms, such as self-employment, part-time or short-term contracts and zero-hours contracts.³ Income variability associated with these employment trends combined with weak income growth could reduce households' resilience to changes in financial circumstances. A sustained rise in inflation is likely to put further pressure on household budgets.

Figure 1: GDP Q-on-Q4 growth



Source: ONS.

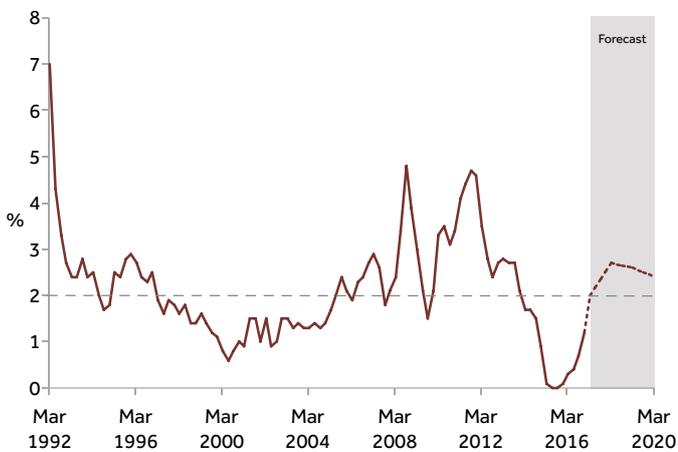
Figure 2: UK households' debt to income ratio



Source: Bank of England Financial Stability Report Nov 2016.

1 Economic and fiscal outlook, March 2017, Office of Budget Responsibility.
2 Financial Stability Report, November 2016, Bank of England.
3 UK Labour Market, February 2017, Office for National Statistics.

Figure 3: CPI yearly inflation



Source: ONS and Bank of England Inflation Report Feb 2017. Quarterly data.

Figure 4: Gilt yields



Source: FCA calculations using Bank of England's data on British Government Securities 10 year nominal par yield (quarterly average) and British Government Securities, 10 year inflation implied forward (quarterly average).

The fall in sterling after the EU referendum and subsequent rise in import and commodity prices has been raising inflation levels and could reduce spending power (Figure 3). CPI inflation reached 2.3% in February and the latest Bank of England Inflation Report projects that it is more likely than not to stay above the 2% target in subsequent quarters. This could increase the pressure on households, leading to a lower growth rate of real consumer spending. Economic activity could be further affected if households cut back sharply on their spending to service their debts.⁴

There has also been a prolonged period of negative real interest rates and these are expected to remain low or negative (Figure 4). There are concerns about the potential impacts of a persistent low interest rate environment on the behaviour of economic agents, the resilience of financial firms and financial stability.

UK withdrawal from the European Union

In the 2016/17 Risk Outlook, we noted that the UK's referendum on EU membership was being considered as part of the FCA's normal activities. The consequences of the UK's exit on the financial sector will depend on the outcome of the Article 50 negotiations. The resilience of the sector will be affected by the negotiations over leaving the EU and agreeing a future trade agreement.

The UK's decision to leave the EU creates a number of uncertainties with the potential to affect the UK and European financial markets, with potential knock-on effects for the UK economy, tax, balance of payments, and the value of sterling. With little information available about the form and nature of these negotiations, it is currently unclear how these will materialise.

This lack of clarity will potentially lead to a period of prolonged uncertainty for markets, firms and consumers. Firms will need to assess the impact that a changed relationship with Europe and any changes to the regulatory regime have on their business models.

Depending on the outcome of the negotiations on the UK withdrawal from the EU, there could be consequences for the firms and markets we regulate. We have a responsibility to ensure markets work well particularly during this period of change and will continue to work closely with the Treasury and the Bank of England to bridge the gap between policy, markets and firms.

⁴ Inflation Report, February 2017, Bank of England.



Changes in the macroeconomic environment can influence behaviour of market participants and firms' business models, strategies and financial soundness.



Risk to our objectives

Lower long-term growth and low interest rates continue to pose challenges for many financial services firms' business models and profitability. Banks, insurance companies and pension funds could face profitability pressures as they seek to find assets to match their liabilities. These firms could increase the risk they take in their asset portfolios to offset the fall in their investment income, either due to the low yield environment or to fund past guarantees. Pension plans are also vulnerable to considerable interest rate risk as most assume higher interest rates than those seen since the financial crisis. Weak profitability diminishes firms' future ability to rebuild capital following a shock, which could affect some of the firms that we prudentially regulate.

There is a risk of additional strain in lenders' profitability if households default on their debts,⁵ given the high levels of consumer debt and the potential impact on household budgets due to inflation and weak income growth.

Increased concentration, due to loss of profitability or lower investment, would pose competition concerns. Uncertainty and macroeconomic risks could lower investment in financial services, reducing supply. Heightened uncertainty around future economic and political developments can also reduce demand for financial services, potentially leading to exit and/or consolidation, reducing competitive pressure.

Furthermore, there is some evidence that, at least in the UK deposit-taking sector, major participants were increasingly able to earn positive economic profits in the periods leading up to and after the crisis despite

an increased number of firms participating in the market.⁶

Other long-term risks to our objectives

Rising inflation and subdued income growth can affect already stretched household budgets and saving ratios. Unsustainable levels of debt and variable income streams resulting from temporary or zero-hours contracts could affect households' long-term ability to access financial services products, potentially leaving them paying higher costs or limiting their credit options. A sudden increase in interest rates could put further pressure on indebted households and pose challenges to consumers and firms who have become accustomed to low rates.

Prolonged periods of negative or low real interest rates can prompt investors to increase their exposure to risky, illiquid or complex assets. The search for yield could heighten conduct risks as investors seek improved returns and so could take on greater risk. Firms and consumers could be left over-exposed to risk, particularly where products offer lower levels of protection and liquidity. Unwinding these search-for-yield positions can challenge market integrity and financial stability if consumers race to exit these positions. In addition, given the search for yield and poor understanding of the risks, consumers may become more vulnerable to scams and fraud; this environment can also create conditions for mis-selling.

Liquidity in capital markets could be affected under adverse macroeconomic conditions. The observed decline in the inventories of dealers in recent years could

⁵ Bank of England, 'Financial Stability Report', November 2016.

⁶ De-Ramon, S. and M. Straughan (2016) 'Measuring competition in the UK deposit-taking sector', Bank of England Working Paper 631.

affect the ability of market participants to find the liquidity to buy or sell in certain secondary markets. A recent FCA study found that even if corporate bond markets have become less liquid since 2014, the overall evidence indicates liquidity is still relatively healthy compared with the overall period 2008-16.⁷ However, liquidity risks exist and some of these markets have yet to be tested under severely stressed conditions.

Increased levels of uncertainty can increase volatility in secondary markets. Unexpected news or major changes in macroeconomic conditions can cause sudden price movements that could, in extreme cases, be a source of instability in secondary markets. Today's fast electronic markets might react differently to these sudden volatility shocks than the traditional markets, which were less dependent on speed.

Social and environmental

Social and environmental factors can have an important role in shaping the decisions of markets, firms and consumers. It is important to consider the long-term social and environmental factors that are likely to have an impact on financial services and pose risks to our objectives.

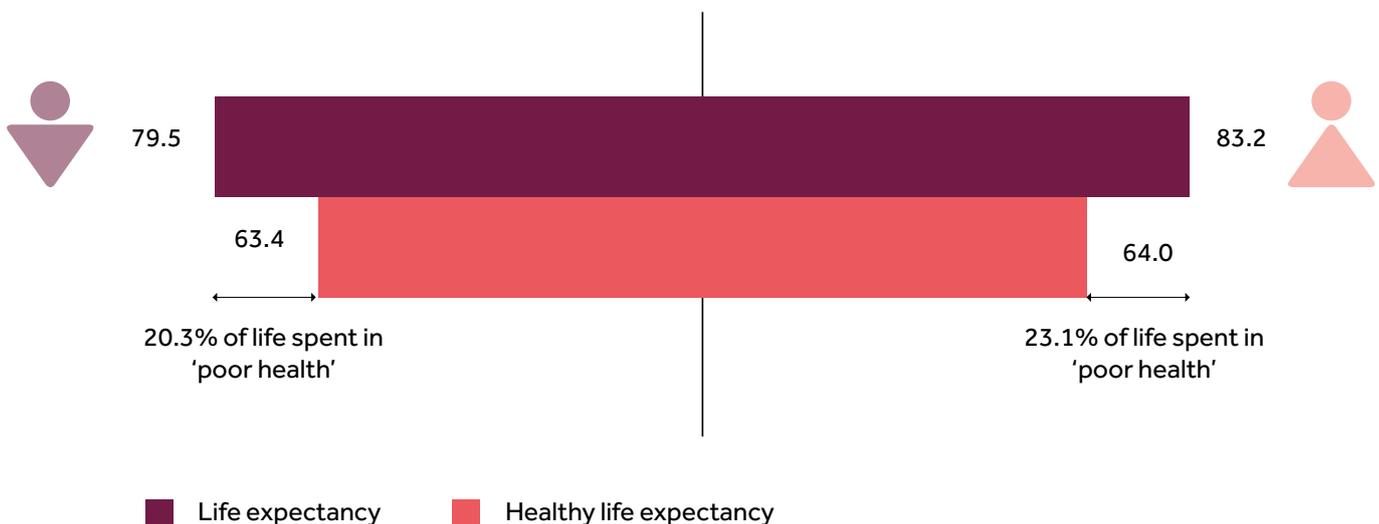
Key trends

Demographic trends and longevity

The average age of the UK population is increasing and older people are a growing proportion of the population – by 2040, projections are that nearly one in seven people will be over 75.⁸ The ageing population and increasing life expectancy places a greater reliance on retirement income over a longer time period. Whilst life expectancy is increasing, people are spending more years potentially living in poor health (see Figure 5).⁹

The baby-boomer proportion of the UK's ageing population holds comparatively high levels of pension and housing wealth¹⁰; as this generation ages, their wealth will be utilised to fund retirement and care. In comparison, younger generations have relatively lower incomes, lower pension contributions and are more likely to rent their homes, which means they are unlikely to accumulate the same levels of wealth in the same timeframe as the baby-boomers. This intergenerational wealth inequality will pose a challenge to younger generations as their long-term savings will not fund the same quality of retirement that baby-boomers will experience; the younger generation will have to work a lot longer and amass more wealth if they want a similar retirement experience. In addition, the younger generation's engagement and behaviour with the financial sector may evolve with their technological preferences.

Figure 5: Life expectancy and healthy life expectancy, in years, of people born 2012-14



Source: ONS
Note: Life and healthy life expectancy of people born 2012-2014

7 Suntheim, F. and M. Allan (2017) 'New evidence on liquidity in the UK corporate bond market', FCA's Insight article.
8 Future of an Ageing Population, Government Office for Science (2016).
9 Healthy life expectancy at birth and age 65 by upper tier local authority and area deprivation: England, 2012 to 2014, Office for National Statistics.
10 Chapter 2: Total wealth, Wealth in Great Britain, 2012 to 2014 Office for National Statistics wealth and assets survey.

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Intergenerational wealth inequality and the challenges younger consumers face in accumulating adequate long-term savings will present challenges to future generations.

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During this period, people's ill-health is increasingly likely to reflect chronic conditions, cognitive impairments and long-term frailty.¹¹ Rising care costs and increasing longevity will place pressure on the adequacy of consumers' long-term savings. In addition, changing demographics (including living longer but not necessarily healthier) and state health provisions, coupled with pressure in health-cost inflation, will continue to challenge insurers' current customer propositions, profitability and ways of managing and pooling risks (eg longevity and morbidity).

Younger consumers

Younger consumers face the prospect of lower earnings and poorer housing affordability than previous generations.¹² Median income growth is lower for younger age groups, and this has contributed to a fall in pension contributions among the young. This has coincided with higher living costs, income variability, higher education fees and availability of credit, meaning that a significant number of young people now have high levels of debt at the start of their working life.

Financial firms will need to consider their customer proposition in light of these trends. A reasonable proportion of older people currently hold relatively stable pension income streams and property wealth. In comparison younger generations have less certainty around future incomes (due to rising short-term contracts and self-employed status), lower savings and long-term indebtedness – but are potentially living longer than prior generations.

Environmental change

The consequences of climate change and other environmental risks are expected to become more widespread if flooding and extreme weather events become more frequent. At the same time, the protection gap between economic loss and insured loss associated with climate change risks is growing – the annual protection gap is estimated to have increased from \$23bn to \$100bn since the 1980s.¹³

The industry and UK Government are already taking steps to manage climate change risks. For example, Flood Re seeks to improve access to property-related insurance by pooling flood risk to ensure consumers in high-risk areas still receive access to affordable insurance, and the Government is investing in flood protection. Government efforts to improve the protection and resilience of high-risk communities will help manage these risks; however these protections will take time and may have limited effect.

Risks to our objectives

There are a number of risks affecting the current population of older consumers, particularly in the pensions sector. These include the **quality of advice around retirement income, difficulties in comparing products and services and potential exclusion through increased use of digital services.**

Older consumers are at increased risk of scams. In some cases due to large holdings of wealth and the release of funds under pension reforms, older consumers can be more susceptible to scams and fraud.

11 'Dementia and cognitive decline – a review of the evidence', Age UK Research, 2014.

12 'The Intergenerational Commission, 2016 Stagnation Generation? The case for renewing the intergenerational contract', Resolution Foundation.

13 Climate Wise, Investing for resilience, University of Cambridge Institute for sustainability leadership.

Consumers face a range of challenges around the security and value of their future pension pots.

In some circumstances, the value of Defined Benefit (DB) pension pots could be lower than foreseen due to pension deficits and the low returns environment, posing challenges to employers managing these schemes.¹⁴ Consumers may also face challenges accumulating sufficient savings for retirement through Defined Contribution schemes (DC) or private pensions. If the affected groups cannot increase their contributions or work for longer, they could take on higher risk products later on in life to make up losses without understanding the associated risks. They could also be more susceptible to scams.

Consumers are at increased risk of taking on unsustainable levels of debt if affordability assessments do not take account of underlying circumstances, particularly where younger consumers face variable income and high levels of existing debts across varied types of credit.

Other long-term risks to our objectives

Consumers could face limited product availability and advice if firms fail to evolve to meet the changing needs of an ageing population – particularly those with lower prospects for wealth accumulation – including pensions, insurance and other retirement-income products. If innovation and the number of new entrants servicing older consumers remains low – in particular around retirement needs – and consumers are inert and fail to shop around, consumers could get a poor deal.

For example, there is likely to be increased demand for products that allow older people to tap into housing wealth or manage long-term health expenses. This demand for these products is likely to be driven by those with low pension wealth, for example consumers who currently belong to lower income groups, but in the future this could include the ageing younger generations who may have lower pension holdings.¹⁵

Firms fail to take into account the needs of an ageing population in delivering their services, posing a threat to consumer protection.

The mental and physical well-being of an ageing population will have an impact on how consumers interact with financial products and services. Cognitive decline will affect the way consumers are able to engage in financial decisions and digest financial information. Some firms are already responding to ageing trends, providing audio and larger print statements.

The financial needs of future generations of consumers are likely to become more diverse than previous generations. If firms are slow to respond to changing needs, consumer inertia or an inability to switch providers due to underlying circumstances (eg variable income and high debts), this could lead to a lack of competition in the market.

If younger consumers are unable to accumulate long-term savings or contribute to a pension, they could be left with insufficient income and limited financial choices later in life.



Credit conditions remain favourable and the cost of credit remains low, sustaining an increase in consumers' debt.



14 Security and Sustainability in Defined Benefit Pension Schemes, February 2017, DWP.

15 Equity release council.

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**FinTech firms are
challenging traditional
financial business models.**



Technology and innovation

Technology has the potential to increase competitiveness, support innovation and efficiency, transform firms' activities and shape consumer and counterparty access to products and services. It is important to consider the increasingly prominent role of technology and innovation in the financial sector, the impact they're likely to have on financial services and the risks they could pose to our objectives.

Key trends

Technological innovation and automation of value chains

Technology and IT systems play an important role in the execution of market activities and firms' business models. Digitalisation of financial markets is increasing both the volume and speed of transactions. Digitalisation and automation can increase cost-efficiencies for markets, firms and consumers, improving the delivery of products and services to consumers and counterparties. However, where this is accompanied by insufficient investment in legacy systems by market participants and poorly planned and executed IT change management plans, markets are more susceptible to disruptions, price shocks and heightened risk of successful cyber-attacks.

There is a continuing trend to use third-party providers to support cost-cutting efforts and adopt more up-to-date services and systems. Outsourcing processes and the fragmentation of market infrastructure arising from the adoption of new technologies, as well as the use of new platforms, can make it harder for firms to exercise effective oversight and governance, and for regulators to monitor the market.

Financial technology (FinTech) firms are increasing in number and some of these firms want to harness data and analytics. FinTech firms are challenging traditional financial business models and are likely to play a key role in firms moving towards less capital-intensive business models, where (after the initial investment) firms benefit from economies of scale with lower ongoing costs. Here, technology could provide ways for firms to service large client bases at lower costs, most recently seen in the wave of digitalisation. FinTech-enabled new entrants are increasing competition in some sectors that will place pressure on existing business models and activities (for example, alternative lending facilities or Robo-advice). Existing firms may look to acquire these firms in order to benefit from these innovations.

Distributed ledger technology (DLT)-based FinTech firms have increased in number over the past three years.¹⁶ **DLT is not widely used in financial services but could enhance some activities,** for example automating simple processes such as recording client data for Know Your Customer (KYC) and anti-money laundering purposes.¹⁷

16 The Boston Consulting Group – Fintech in capital markets, November 2016.

17 The Boston Consulting Group – Fintech in capital markets, November 2016.

DLT could be used to support full automation of trading, clearing and settlement across asset classes, particularly across syndicated loans, FX and OTCs, where back-office activities are manual.¹⁸

Smart data, digitalisation and data analytics

Advances in firms' capacity to process large amounts of information, profile clients, undertake risk analytics and build algorithms are shaping market activities, financial products and services.

The use of application programming interface (API) and decisions like the Competition and Market Authority's (CMA) Open Banking proposal, together with Payment Services Directive 2 (PSD2) implementation, will promote opening up access to clients' account data. As the number of smart device users and online traffic grows, the volume of digital data will also increase. Annual global IP traffic is expected to increase nearly threefold over the next five years.¹⁹

In wholesale markets, increasing use of big data in business models means firms need to ensure they are using data appropriately and managing it effectively. This is especially true where firms, including those that undertake wholesale activities, have multiple different business lines and access to the data needs to be restricted within an organisation. Effective cyber risk management across both financial and non-financial sectors is needed to ensure data is not mis-used for fraud or market abuse purposes.

Cyber crime and money laundering

Cyber-attacks continue to increase in volume, scale and complexity.

We have seen a significant increase in attacks reported by firms over the past three years. While many of these attacks may be minor individually, taken together they may give greater cause for concern. Increasingly sophisticated, market-wide or simultaneous cyber-attacks (directly on financial institutions or market infrastructure providers) could affect the stability and integrity of markets, placing continued focus on firms' cyber-resilience and financial crime controls.

Financial crime statistics from the ONS suggest there were 2.11 million victims of cyber crime and 2.5 million incidents of bank and credit account fraud in 2015/16.²⁰

Increasing terrorist activity across the globe presents new types of threats to market integrity. Financing terrorist activities through financial markets and laundering money through the financial system present risks to the soundness and stability of the financial system. Globally, money launderers and terrorist financiers can exploit loopholes among national anti-money laundering systems to move funds, and financing could also move into the shadow banking sector.



Advances in firms' capacity to process large amounts of information, profile clients, undertake risk analytics and build algorithms are shaping market activities, financial products and services.



¹⁸ The Boston Consulting Group – Fintech in capital markets, November 2016.

¹⁹ Cisco VNI Global IP Traffic Forecast, 2015–2020.

²⁰ Overview of fraud statistics: year ending Mar 2016, Office for National Statistics.

Risks to our objectives

Growing use of technology, particularly electronic and digital services, in firms' business models and market infrastructure (including outsourced functions) increases cyber security risks, opportunities for money laundering and scams in some markets. Cyber continues to be a major risk to our objectives. These risks threaten the integrity of the information flowing through financial markets, affecting the availability of financial services and increasing the risk that consumers and clients will suffer, either directly or as a result of a firm's breach.

- **While greater use of technology and analytics could solve many financial crime problems, innovation can also create new opportunities for financial crime as interfaces become multi-faceted and systems use greater volumes of data and automation.** Inadequate controls in using data appropriately could also pose risks to consumer protection and market integrity. Furthermore, the way in which firms incentivise their customers to provide data could pose risks to those market participants.

- **Information security risks could increase, particularly where firms don't fully assess the capability of existing infrastructure, including systems and controls.** Information security risk is the threat to the confidentiality, integrity or availability of information, which can be as a result of a process failure, human error or attack, which in turn can lead to service disruption, service outage, data loss or the manipulation of data, reputational damage and potentially fraudulent or other criminal activity. The scope and impact of this risk may increase with increased data volumes. In addition, as non-financial firms gain access to consumers' financial information as their role in payments increases, there is a risk that firms could misuse their data, in particular targeting products through consumer profiling. This could lead to loss or theft of consumer data.

Shortcomings in the way firms' systems are designed, maintained and overseen could limit the effectiveness and resilience of technologies. Firms need to have well planned and executed IT change strategies to ensure their services to market participants, including counterparties and customers, are not disrupted.

Regulation doesn't keep pace with innovation, stifling competition.

The pace of technological integration and innovation could challenge the ability of regulators to adapt to growing competition from new entrants. In some cases, competition could be stifled because regulatory policy does not adequately respond to technological changes, (for example, by limiting the way in which firms can offer services).



Growing use of technology, particularly electronic and digital services, in firms' business models and market infrastructure increases cyber risks in some markets.



More complex value chains that utilise FinTech could pose a risk to consumer protection and market integrity. The issues associated with the oversight and controls of increasingly complex chains of third-party relationships are reflected in our priorities. The technological resilience of incumbent firms will also continue to be an area of focus because of the risk of disruption to financial markets. FinTech firms may not fully understand the scope of regulation and its impact on their business model. This could lead to cases of non-compliance with our rules, which could pose risks to consumer protection and market integrity.

Other long-term risks to our objectives

Accessing products and services through mobile and other digital devices could lead to consumers paying insufficient attention to terms and conditions, leading them to buy unsuitable products. The behavioural preferences for online access and speed of services and transactions could present challenges. This is particularly relevant when younger consumers are making important long-term financial decisions, but may be reluctant to engage with lengthy advice processes and literature.

Increased use of data and algorithms could lead to poor consumer outcomes or threaten market integrity. While the use of algorithms to make use of growing volumes of data should promote competition, it also has the potential to encourage 'herding' behaviours or lead to data being mis-used if underlying algorithms are not fully understood by firms.

- **Technology strategies that focus on servicing particular consumer groups could result in targeted consumers benefiting from more personalised lower cost products through risk-based pricing. However, there is increased risk that firms cannot cater for nuanced consumer needs if they don't align with underlying algorithms.**²¹ This could create access issues for groups of consumers whose circumstances don't match product criteria. This risk could be exacerbated if a large number of providers use the same automated systems. Vulnerable consumers are at higher risk of exclusion by automated services (eg due to low income, a criminal background, poor credit history, inadequate documentation, or the newly divorced or widowed). Other access problems arise around 'non-standard' consumers, such as those living with a disability, illness or those with a criminal record.
- **Adverse risk selection could leave higher risk consumers priced out of the market or unable to access products and services as firms use data analytics to exploit information about consumer behaviour.** Widespread use of telematics and wearable devices will continue to allow insurance risk models to be calibrated with richer consumer behaviour data. Innovative ways to use growing data volumes are likely to influence insurers' calibration of individual vs pooled risk; this might include innovations in genetic testing to predict health problems. The potential rise in those who are excluded in some way from accessing the financial products and services they need is a long-term challenge for the financial sector.²²



Vulnerable consumers are at higher risk of exclusion by automated services.



²¹ 'Revolutionary change is transforming the financial services landscape', Financial Services Leadership Summit.

²² Access to financial services in the UK – OP 17 (May 2016).

- **Where senior management and control functions do not have adequate understanding of underlying algorithms** it could lead to insufficient controls or reduced access for some consumers and market participants. Firms have a responsibility to ensure they have the appropriate skills and knowledge to service and maintain algorithms to ensure data and algorithms are not being misused.

Information differences could be exacerbated where institutions have the capacity to use big data to analyse large amounts of information, impacting competition. Smaller investors or less tech-savvy firms may only have access to limited and potentially inconsistent information. There may be information asymmetries in markets where well-funded firms are able to harness smart data to 'cherry pick' business. If firms operate risk analytics that are not transparent, then increasing use of big data could create information asymmetries that disadvantage less-efficient and technologically established firms and their customers. If consumer inertia prevents them from switching, consumers could face poor outcomes. There is also a risk that both firms and third-party firms could mis-use consumer data in a way that harms consumers.

Greater reliance on technology poses increased operational risk, and risks to market integrity. The operational risks of widespread automation, for example loss of service and technical problems around delivery, could lead to wholesale firms being unable to transact, value portfolios or settle trades, with significant consumer harm as a result. Existing firms that face legacy system and IT resilience issues will need to overcome these challenges to remain competitive if challenger and FinTech firms take advantage of advances in artificial intelligence (AI) and growing data volumes. Where firms exercise poor governance and have weak IT strategies in place, the adoption of new technologies such as cloud storage, new payment technologies, and automation that uses blockchain (eg back-office activities) could lead to security or structural weaknesses and increased outages.²³

Firms, businesses and consumers

Firms' conduct is a key factor driving risks to our objectives. This section lists key trends in the business environment in which firms operate, and also looks at consumer trends and draws out the risks these trends pose to our objectives.



High reliance on technology and the interconnectedness of markets at the global level mean that cyber-attacks or system glitches may create widespread disruption.



²³ How Blockchain technology will disrupt financial services firms. Wharton Business School, University of Pennsylvania.



Key trends

Shifting business models and product innovation

There is an ongoing need for firms to improve cost efficiencies, reduce labour costs and improve their financial performance. Many firms seek technological solutions like digitalisation and automation to reduce costs, simplify or reduce their products or diversify into new markets and improve their market share. Firms' adjustments are partly driven by a desire to improve customer experiences, but also reflect a continuing effort to leave less-profitable markets and reduce costs. Consumer focus and increased awareness of fair standards is expected to increase in firms as a result of the Senior Managers Regime.

Technology and IT systems are driving some changes to market structures and business models. High reliance on technology and the interconnectedness of markets at the European and global level mean that cyber-attacks or system glitches may create widespread disruption.

Reliance on technology to deliver innovation in the financial sector has increased the number of non-financial players. In some markets, technology has enabled new entrants to start replacing traditional firm activities, for example market makers.

In some sectors, traditional business model boundaries are becoming blurred. Examples include the treasury of large firms financing its suppliers or clients, life insurers, and asset managers and hedge funds seeking higher returns by moving into new markets such as non-prime or buy-to-let mortgages or small business lending.

Furthermore, the adjustment of market participants to post-crisis regulation, for example MiFID II, has the potential to lead to structural changes in financial markets that will have implications for competition, consumer protection and market integrity.



A lack of investment by firms in understanding the interdependencies between new technologies and their existing business model could present risks to consumer protection and market integrity.



In other sectors, particularly wholesale financial markets, network effects remain strong and can lead to relatively concentrated markets. Examples of wholesale markets where network effects may play an important role include trading venues, benchmarks, post-trading services and market data.

Consumers' financial decisions and individual accountability

Consumers are increasingly using mobile and digital solutions, enabled by the growth in financial technology. This is delivering digital and automated platforms that appeal to consumers who prefer mobile and digital. However, increasing use of digital technology has become a barrier for some. Older people in particular are less likely to be computer literate and 12 million people in rural areas have limited internet access.

Research from Ernst & Young on a sample of bank customers suggests that although a significant proportion of consumers go online to research products, a significant proportion believe that a physical presence is also important.²⁴ Firms will need to balance their desire to reduce costs through increasing their digital presence with the demands of some consumers for face-to-face engagement.

Low financial literacy levels may mean consumers are not able to appropriately assess their needs. There remains a significant proportion of consumers with low levels of financial capability. Consumer behaviours and biases will always exist in financial decision making and are often exacerbated by low financial capability.

Social and technological developments have increased the sophistication of financial services – this presents both risks and opportunities for improving consumers' financial capability and financial inclusion.

Financial services are becoming more complex. This, coupled with an emphasis on individual accountability and consumers taking on an increasing number of financial products, mean that consumers need to improve existing levels of financial capability just to keep pace.²⁵

Anticipated growth in 'smart' artificial intelligence could resolve some financial capability issues through smart advice and improved targeting of products and services.²⁶ Although technology may limit access for some, it could open up access for others, such as translating text into audio for visually impaired people. While technology may enhance and support financial capability as more products and services become digitalised and automated, it could also present challenges around access to services and products. This may be particularly relevant for vulnerable groups such as those with mental health issues. This could lead to consumer protection risks, for example, where someone may change their spending habits or debt repayments during periods of depression or ill-health, leading to financial difficulties.

Risks to our objectives

A lack of investment by firms in understanding the interdependencies between new technologies and their existing business model could present risks to consumer protection and market integrity. For example, where new technology is adopted at different speed within a business,

²⁴ Global Consumer Banking Survey, Ernst and Young 2016.

²⁵ 'Changes Past, Present and Future in Financial services', Oliver Wynman.

²⁶ 'Changes Past, Present and Future in Financial services', Oliver Wynman.

this could lead to potential poor outcomes if new and old systems cannot interact, such as consumer-facing mobile apps, or if data are linked inappropriately. Demand for technological transformation is growing at a time when firms are already responding to significant environmental and regulatory change. In addition, the adoption of technological solutions could increase firms' operational risk if systems are not adequately maintained and serviced. Firms' ability to deliver and manage large-scale change programmes that involve new technologies could place firms' systems and controls under stress and reduce the effectiveness of cyber resilience.

The ability of firms to manage multiple layers of risk effectively could be challenged by the volume, scale and pace of change required.

Firms could struggle to manage these risks effectively. Large-scale business transformation by firms seeking to become more IT resilient, improve cyber security and anti-money laundering controls at the same time as implementing regulation, dealing with legacy issues and new entrants is likely to place firms' management and controls under stress. This could lead to cases of non-compliance or inefficient short-term responses that present longer term risks to firms' business and to consumers.

Firms outsourcing IT systems or processes may fail to exercise appropriate oversight over the supplier, resulting in user protection and stability and resilience risks.

Network effects may create significant barriers to entry or provide some firms with market power. Although network effects provide some market users with benefits, market power creates a risk to our competition objective and can lead to sustained higher prices or poorer quality.

Firms may also change the risk criteria they use to assess new clients to expand their client base, resulting in weaker checks and anti-money laundering controls, which could allow markets to be used for criminal activities.

Firms fail to positively address known consumer behaviours and instead look to capitalise on them. These include:

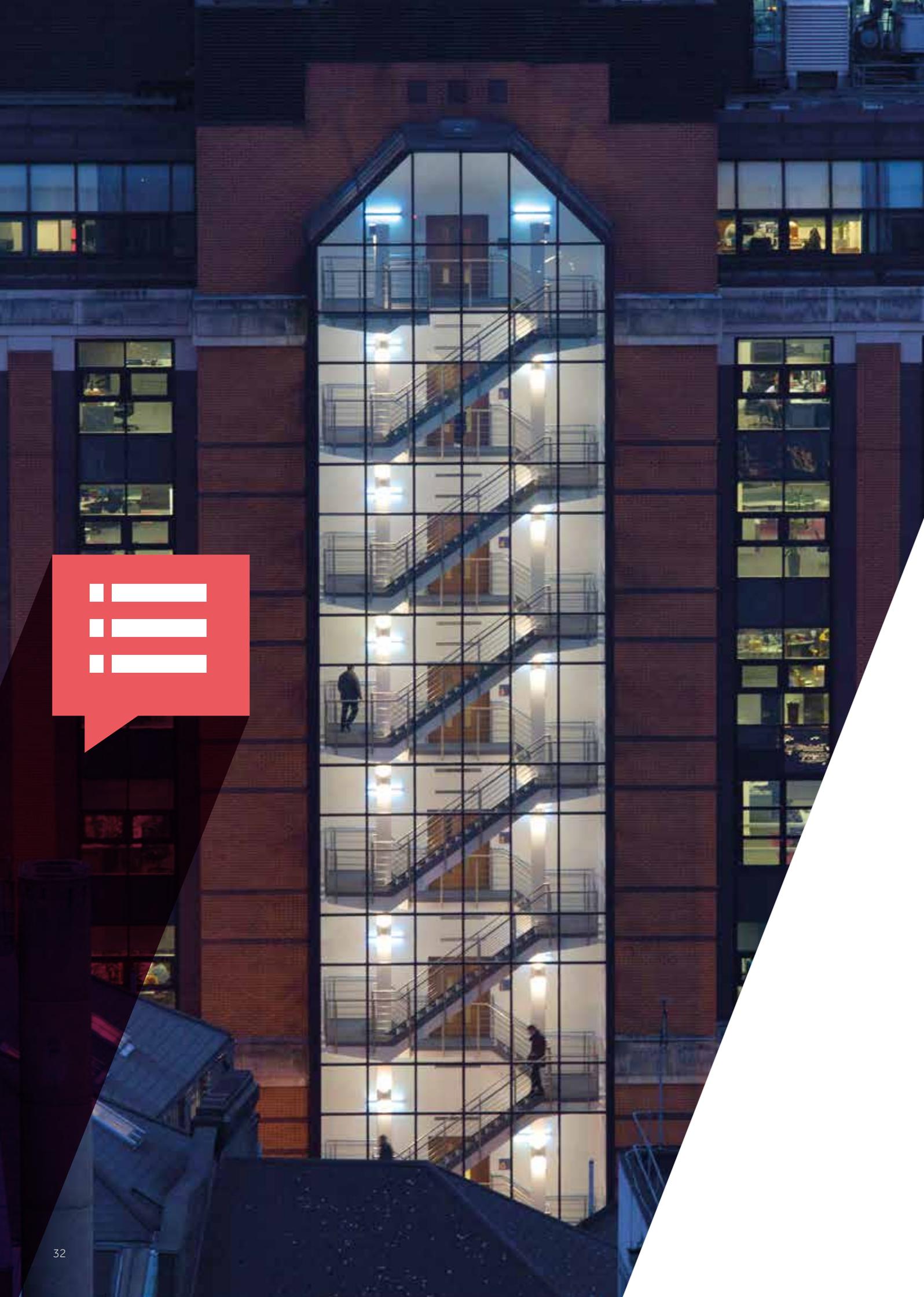
- **Low financial capability:** Consumers' financial skills and ability to make well-informed decisions could be stretched by increasingly complex financial choices.
- **Consumer vulnerability:** The financial capability of consumers in vulnerable circumstances can be made worse by the distress of their circumstances – this can impair their cognitive abilities and financial resilience.²⁷ This has the potential to lead to consumer protection risks where firms don't treat consumers fairly.

While simplification and standardisation of products and services may appeal to consumers, it also risks excluding some consumer groups and the inappropriate treatment of legacy customers. This raises questions about whether simplified products truly meet consumers' needs, especially those of specific smaller customer groups. In some cases, firms' processes and procedures for products and services may not appropriately consider the effect on consumer access, particularly for vulnerable consumers. In addition, firms may not fully assess the impact of their decisions on access, particularly for vulnerable consumers. Poor financial literacy can make it difficult to compare products, which may limit the effectiveness of new innovative solutions in the market.

Other long-term risk to our objectives

Over time, the increase in non-bank payment services could mean consumers become more familiar with unregulated entities providing access to financial services through the payments chain rather than traditional banks. This could make it more difficult for traditional firms to cross-sell to their consumers as brand loyalty is reduced. Existing firms could respond by adjusting their business models in ways which lead to poor consumer outcomes. In addition, fragmentation of payment services across new entrants could make credit assessments more difficult for lenders in the absence of data sharing which could lead to consumer protection risks.

²⁷ 'World Economic Forum (WEF) Global Agenda Council on Ageing Symposium', Age UK.



How we decide our priorities

The way we regulate is underpinned by our assessment of harm and public value. Our Risk Outlook analyses the external environment and focuses on overarching trends and medium to long-term risks. We address and mitigate the more pressing and immediate issues we identify, and monitor closely longer term issues. We also undertake further analysis of the harm in each of the markets and sectors we regulate. The results of this work are our Sector Views, which we are publishing for the first time along with Our Mission and this Business Plan.

Our Sector Views analysis is updated regularly and is developed in four stages:

- **Understanding the sector:** We define the size and scope of each sector, identifying the consumer need it meets. We map the products and providers in the market, and look at market structures, competition and business models.
- **Monitoring intelligence:** We gather qualitative and quantitative data, as well as FCA intelligence on what is happening in the markets. We consider this in the context of outside factors that might influence the sectors, such as macroeconomic, technological, social and policy changes. We also consider the relationships between the sectors under review and other sectors. This gives us as complete a picture as possible of the key developments.
- **Assessing sector performance:** We then analyse what the data and intelligence are telling us. We look at how the sector is performing for consumers and firms, the role of competition and the impact of market-wide forces.
- **Identifying the key issues:** Finally, based on our assessment, we identify the key issues for the sector and begin to prioritise them based on the actual or potential harm they cause.

We also assess how markets are interacting with each other as part of the wider financial landscape. We identify cross-cutting issues, which are either shared by different sectors, or begin in one sector and affect another.



We concentrate our resources on the markets and firms most exposed to risks that may create consumer harm, affect market integrity or where competition is poor and does not work in consumers' interests.



Deciding our priorities

In an ideal world we would be able to mitigate all the harm we detect. In reality, we have to make choices and prioritise our work. We apply our resources to the areas where we judge potential or actual harm is greatest, where we can have the most impact and deliver the greatest public value and by using our principles of good regulation.

We concentrate our resources on the markets and firms most exposed to risks that may create consumer harm, affect market integrity or where competition is poor and does not work in consumers' interests.

Sector Views play an important part in our work, helping determine our priorities for a sector, our resourcing decisions and our operational plans. We review and compare all the issues we have identified in all sectors and across sectors. We then consider their relative importance and urgency, and identify the most suitable and effective regulatory tools to address the issue.

We also use our ongoing work of developing policy, reviewing competition, authorising and supervising firms and making and enforcing our rules, to support our delivery of priorities. Our day-to-day programme of work is crucial to achieving our outcomes. We also need to keep sufficient oversight of all sectors to support the right behaviour and practices and rapidly crack down on poor behaviour when needed.

Our priorities

Our analysis identified the most important issues in each of the sectors, as well as six cross-sector priorities.

These will be the priority areas for our discretionary work over the next year. They clearly do not represent all our work, and we will use them as the basis for our decisions on thematic work and market studies. Our core, ongoing work and engagement with firms will also support the way we deliver against these priorities.

The following are our cross-sector priority areas:

Our cross-sector priorities

- Firms' culture and governance
- Financial crime and anti-money laundering (AML)
- Promoting competition and innovation
- Technological change and resilience
- Treatment of existing customers
- Consumer vulnerability and access to financial services

The cross-sector issues are inevitably long term. They are complex, often endemic, issues that we expect we will continue to address in future Business Plans. At the same time, we ensure that our prioritisation processes are flexible and that our governance processes are robust and provide adequate challenge. This allows for changes, both in-year when unexpected issues arise and to our longer-term priorities.

We have made some changes to the cross sector priorities from last year's Business Plan. We have split our 'Innovation and Technology' priority into two – 'Promoting innovation' and 'Technological change and resilience'. This will help us provide more clarity to firms and consumers on the distinct issues that are unique to each. Our work under the 'Promoting innovation' priority will focus on increasing competition through innovation and removing barriers to entry, while our 'Technological change and resilience' priority will address operational resilience, and cyber-attacks. We have also added a new priority area, 'Access and vulnerability' which, in line with our Mission, focuses on vulnerable consumers and the ability to access financial services.

We divide the financial markets we regulate into the following seven sectors:

The sectors
• Wholesale financial markets
• Investment management
• Pensions and retirement income
• Retail banking
• Retail lending
• General insurance and protection
• Retail investments

This year's Business Plan gives details on all of them and sets out our view and strategy for each, in the 'Our Sector Priorities' chapter.

We have included the sector-focused priorities from last year – Pensions and Wholesale Financial Markets – in the section covering specific sectors. The 'Advice' priority from last year, which largely addressed investment advice, is now covered in the 'Retail investment' sector.

How our priorities support our objectives

All of our work is done to support our statutory objectives.

Our ongoing activities and our priorities all focus on advancing at least one of our objectives and often advance more than one. For example, work on fraud and scams advances both our 'consumer protection' and 'market integrity' objectives.

Table 1 shows the main statutory objective that each of our cross-sector priorities advances. Our work within sectors is varied and advances all objectives.

Table 1

Cross-sector priority	Main statutory objective
Financial crime and anti-money laundering (AML)	Market integrity
Firms' culture and governance	Consumer protection
Promoting innovation	Promoting competition
Technological change and resilience	Market integrity
Treatment of existing customers	Consumer protection
Consumer vulnerability and access to financial services	Consumer protection

Our cross-sector priorities

Firms' culture and governance

Our focus on culture and governance in financial services and its impact on individual and firms' conduct is a priority. We will continue to promote the right cultures, behaviours and effective governance across the industry to deliver appropriate outcomes for consumers, markets and competition consistent with our objectives.

Culture is the product of a number of different drivers within firms, and is shaped by many influences that drive the behaviour of everyone in an organisation. The 'tone from the top', incentive structures and the effectiveness of management and governance all contribute to the overall culture of a firm, along with many other things.

Firms should own and manage their cultures at all levels and are responsible for identifying and managing the risks created by the drivers within their firms.

We expect firms to have effective governance arrangements in place to identify the risks they run – with a strategy to manage and mitigate those risks to deliver appropriate outcomes to consumers and markets. While the way firms design their governance arrangements provides an infrastructure for how they are run, our focus is on the effectiveness of those structures.

Firms' senior managers have a crucial role in demonstrating that they are accountable and responsible for their part in delivering effective governance. This includes taking responsibility, being accountable for their decisions and exercising rigorous oversight of the business areas they lead.

Boards have a critical role in setting the 'tone from the top'. We expect them to take responsibility for their firm's culture and its key drivers, ensure culture remains high on the agenda and that an appropriate culture is embedded throughout the firm at all levels. Senior managers need to ensure that their firm's business processes, people and drivers of culture support and reinforce the culture they want to embed.

This should, over time, result in improved culture and governance in the industry. It should also promote public confidence that firms have the right people in the right roles, working in the interests of consumers and markets.

Outcomes we seek

- Firms' culture and governance deliver appropriate outcomes for consumers and markets, and effective competition in the interest of consumers.
- Firms develop a culture of accountability at all levels and senior individuals are fully responsible and accountable for clearly defined business activities and material risks.

- Senior managers can explain principles of appropriate conduct towards consumers and markets and incorporate them throughout their business.
- Firms understand and can explain their cultures, including what drives their behaviours. They proactively identify the risks their behaviours pose to delivering appropriate outcomes and act to address the drivers of these risks using appropriate systems and controls to create a culture that works in the long-term interests of the firm, its customers and market integrity.
- Firms take steps to proactively identify and address issues when things go wrong, and can demonstrate that they learn from these events.

Issues

- **Poor cultures** in firms drive behaviours that deliver inappropriate outcomes for consumers and markets.
- **Firms' strategies, business models and governance arrangements** are not aligned with appropriate conduct.
- **Incentive structures and performance management** do not reward behaviours that act in the long-term interests of consumers and market integrity.
- **Weak governance** creates poor oversight of risks to consumers and market integrity risks in how firms are run.
- **Lack of accountability** results in weak focus from senior management on risks to consumers and market integrity.

Our key planned activities

Our focus continues to be on the most significant drivers of behaviour. These include senior management accountability and remuneration, and the steps firms and their senior managers take to address any risks caused by their behaviours. We are interested in the direction of travel of firms' cultures and whether indicators suggest that progress is being made. We will continue to support and drive cultural change across the industry.

Accountability and governance

The key aims of the Senior Managers & Certification Regime (SM&CR) are to strengthen individual accountability at the most senior levels of relevant firms and improve their standards of conduct at all levels. We expect firms and their senior managers to apply the spirit, as well as the letter, of the regime.

To date, the SM&CR applies to deposit takers and dual-regulated investment firms. Firms already under the SM&CR have been undertaking fitness and propriety checks on all relevant individuals under the Certification Regime. Those firms currently in scope for the SM&CR are also expected to comply with the notification and training requirements to apply the conduct rules to all staff apart from ancillary staff. There is also a revised framework for insurers to raise standards of individual conduct, and additional rules that will apply more widely across financial services.

In 2017/18, we will continue to embed the SM&CR in our supervisory approach and processes, and focus on how the SM&CR is integrated into the running of deposit takers and PRA-designated firms. Our authorisation work at the gateway also puts significant emphasis on the most senior individuals in firms, and we ensure our pre-approval

processes are proportionate and dependent on the risks that the individual's role and the firm pose to our objectives.

The SM&CR provides clarity for both firms and regulators about each senior manager's responsibilities. We will continue to use firms' responsibilities maps and individual senior managers' statements of responsibilities throughout the regulatory lifecycle. This includes when we approve and supervise individuals and firms and consider enforcement. These tools will further help us to identify and assess key senior individuals' management and governance arrangements.

We will also use these tools with relevant firms as part of our proactive work with them, including to shape discussions about management and governance arrangements.

We will also continue to develop our policy on designing and implementing an accountability regime for all FSMA firms, including further developing the regime for insurers. We will consult on the accountability regime for all FSMA firms in 2017 and complete our preparation to implement the regime from 2018.

Our focus for the new accountability regime for all FSMA firms is to deliver a regime that is simple, proportionate and clear. We want the new regime to be simple and practicable for firms to understand and implement, and for the FCA to oversee and regulate. We plan to tailor the new regime to reflect the different risks, impact and complexity of firms. Across the industry, we want to be clear how the different components of the regime apply to different types of firms.



Senior managers need to ensure that their firm's business processes, people and drivers of culture support and reinforce the culture they want to embed.



Remuneration

We have improved our Remuneration Code for dual-regulated firms (firms that are regulated by both the FCA and the PRA). Our aim here is to encourage more effective risk management and better align individual decision making with good standards of conduct.

We want to ensure that remuneration policies and practices promote the link between risk and individual reward, discourage excessive risk taking and short-termism, and encourage sound and effective risk management. This in turn will support positive behaviours and a strong and appropriate culture within firms.

We will continue to review our regulatory framework that governs remuneration, including helping firms to understand and implement remuneration requirements. We will continue to review firms' approaches to implementing the regime to ensure these meet regulatory requirements and our wider objectives.

Supervision

As a firm's culture is influenced by many different factors, we cannot prescribe what it should look like, nor do we believe that every firm should have the same culture.

We will continue to use a range of supervisory tools and methods to work with firms on issues relating to the drivers of culture that are of interest to us as a regulator, demanding high standards of conduct and ensuring firms' management keep appropriate culture as a top priority.

A focus of our proactive multi-firm work will be on culture and governance issues, and will specifically look at how relevant firms have embedded the certification regime.

Communications

We want to be transparent about the way we look at culture in firms. We will continue to share our expectations and views on culture so our stakeholders understand our approach and how it fits within our objectives. We will also continue to engage with external stakeholders to educate them about our expectations, and support and participate in external initiatives on culture in financial services.

Measures of success

Over the medium to long term:

- Senior managers can demonstrate they are accountable for clearly defined business activities, and there is a culture of accountability at all levels in all relevant firms.
- Firms apply robust, and comprehensive remuneration measures to their remuneration policies and practices, based on actual loss and harm.
- Firms can demonstrate that they act appropriately on whistleblowing intelligence.
- There is a decrease in the number of material risks we identify that involve culture.

Our cross-sector priorities

Financial crime and anti-money laundering

The UK financial system is a major global hub for investment and economic activity. However, this scale is also attractive to criminals and terrorist organisations seeking to hide the proceeds of crime. We seek to make this a hostile environment for criminal money.

We need appropriate safeguards to prevent financial crime, while ensuring they are proportionate, operate efficiently and minimise any unintended consequences of regulation. We also want to reduce and prevent the harm caused by scams and increase consumer awareness of the dangers of fraud.

These are all areas where partner agencies have responsibilities and a vital role to play. We will collaborate with law enforcement partners and other agencies in our work on anti-money laundering (AML), scams and other types of financial crime, with actions being taken by the appropriate organisations.



We need appropriate safeguards to prevent financial crime, while ensuring they are proportionate, operate efficiently and minimise any unintended consequences of regulation.



Outcomes we seek

- The UK financial system is a hostile sector for money launderers, as law enforcement agencies and regulators use intelligence effectively to take early action that prevents money laundering.
- The unintended consequences of AML regulation, such as excessive delay in opening accounts, are minimised.
- Firms' AML processes do not exclude people unfairly or unreasonably from using financial services.
- AML requirements are proportionate and operate efficiently.
- Harm to consumers from scams is reduced because:
 - we help consumers to spot the warning signs and avoid scams, including pension scams
 - we take action against those unauthorised firms and individuals who perpetrate scams
 - we work with firms to tackle concerns about bank transfer fraud



We will support individuals who whistleblow to the FCA, and ensure that we provide them with the anonymity they need.



Issues

- **In the search for profit and growth.** firms may change the risk criteria they use to assess new clients, leading to weaker checks and controls.
- **Higher costs and falling profits** may see firms cut investment in systems and controls. The growth of digital tools increases the risk of online financial crime and cyber-attacks, although new technology may allow firms to develop stronger systems and controls.
- **Financial crime requirements,** and other factors including reduced profitability, may cause banks to de-risk²⁸ their product ranges inappropriately. This may make it difficult for certain groups of people or businesses to access financial services.
- **Consumers may become more vulnerable to fraudsters.** Releases of pension funds under the pension reforms are being targeted by scammers, while bank transfer fraud is increasing.

Our key planned activities

Anti-money laundering

In 2016 we rolled out our Financial Crime Annual Data Return, and we will analyse the early responses to make sure we are focusing our supervision on the right firms. Where firms have poor AML controls, we will use our enforcement powers to impose business restrictions to limit the level of risk, provide deterrence messages to industry, or both. We will generally use our civil powers, but if failings are particularly serious or repeated we may use our criminal powers to prosecute firms or individuals.

We will also refer cases to other law enforcement agencies where we identify suspected money laundering.

We will continue to use intelligence, including from whistleblowers, to prevent money launderers using the financial system. We will support individuals who whistleblow to the FCA, and ensure that we provide them with the anonymity they need.

We will continue to work closely with the Treasury on AML policy issues as they transpose the 4th Money Laundering Directive (4MLD) into UK law by June 2017. We are also working with the Treasury on negotiating the EU proposals to make revisions to 4MLD to strengthen the fight against terrorism. We will also continue our work with the European Supervisory Authorities on drafting guidance to support 4MLD.

The Financial Action Task Force (FATF) is a global inter-governmental body that sets standards for combating financial crime and related threats to the integrity of the international financial system. We will continue to be a major participant in the FATF, which will carry out a mutual evaluation review of the UK from late 2017. We will continue to review and refine our AML supervisory approach to demonstrate to FATF that it is effective.

We will continue our due diligence on firms and individuals applying for authorisation and our proactive supervisory assessments of firms whose business models present a higher inherent risk of money laundering.

²⁸ De-risking refers to banks withdrawing or failing to offer banking facilities to customers. There is a perception that this is driven by banks' concerns about the money laundering and terrorist financing risks posed by certain types of customers.

Our new AML watchdog role

There are many bodies in the UK with responsibility for financial crime regulation and compliance.

To ensure consistency and quality, and to drive up standards across all AML supervisory bodies in the UK, the Treasury has proposed that the FCA is responsible for reviewing the quality of AML supervision carried out by professional bodies like the Solicitors Regulation Authority and the Institute of Chartered Accountants in England and Wales. We are due to be given formal powers to do this towards the end of 2017, and will become a 'supervisor of supervisors' called the Office for Professional Body AML Supervision (OPBAS) within the FCA. We are currently working with the Treasury to agree the details of how it will operate in practice. This work will be funded through a new fee on the professional body supervisors.

Proportionate and effective response to de-risking

We know that de-risking by banks is causing problems for some groups of consumers. While we do not control this process, we are undertaking work to help address the issue. We published our report on the nature, scale and drivers of de-risking in May 2016. We continue to work with the banking industry to help firms improve the way they identify money laundering risk, as well as how they communicate with their customers.

We are also undertaking our own work to foster innovation and reduce cost in AML compliance, deliver a global response to de-risking, and improve the effectiveness of AML supervision. We will also publish a report on the work we have commissioned on how new technology can make AML processes more efficient

and less onerous for firms and customers alike, reduce financial exclusion and encourage easier switching between financial services providers (see 'Promoting innovation' for more information).

Fraud and scams

We will focus on action against firms and individuals who perpetrate scams. We have a range of enforcement actions to tackle those engaging in unauthorised business. These include civil court action to stop activity and freeze assets, insolvency proceedings and, for the most serious cases, criminal prosecution.

Only a limited number of investment scams fall within our remit. So effective coordination with other agencies and a continued focus on prevention, including better consumer education, is critical to achieving long-term success in this area. We will coordinate our efforts across our supervisory, intelligence and enforcement functions in our work on scams, particularly those that target consumers' pensions. Prevention, detection and pursuing those undertaking pension scams are FCA priorities. We will also continue our ScamSmart campaign to help prevent consumers falling victim to investment and pension fraud.

Our ScamSmart communication campaign aims to help protect consumers from falling victim to investment fraud. We will run another phase of the campaign, including advertising. This will further increase awareness of the risk of investment fraud among our target audience and ensure they get frequent reminders of the risk of scams. We will also continue to monitor and improve the effectiveness of our online tools.

We are a member of the Government's Joint Fraud Taskforce, launched in February 2016, which brings together law enforcement agencies, firms and regulators to better identify and respond to fraud.

Measures of success

- Over the medium to long term, there is an improvement in firms' AML controls, measured through findings from our routine AML supervisory work.
- Over the medium to long term, there is an improvement in the perception of the UK's AML regime from international assessors and overseas authorities.
- AML requirements are proportionate and operate efficiently.
- Firms' AML processes do not exclude people unfairly or unreasonably from using financial services.
- There is increased consumer awareness and understanding of scams and techniques used by fraudsters.
- There is greater use of our online resources to help consumers avoid scams.

Our cross-sector priorities

Promoting competition and innovation

New types of financial technology (known as 'FinTech'²⁹) continue to drive change and encourage innovation in the financial sector. FinTech can sharpen competition and reduce overheads, potentially offering consumers better value for money and easier ways for firms and customers to engage with each other. But if not managed well, it can also introduce new risks into the financial system, or heighten existing ones.

Our approach is to sustain a regulatory environment where consumers and firms can grasp the opportunities of competition while maintaining consumer protection and market integrity. 'RegTech'³⁰ – technology that makes it easier for firms to comply with regulation – can significantly help both regulators and the regulated.

Outcomes we seek

- Innovation encourages competition to deliver better value for money and better service for consumers of regulated financial services.
- Innovation drives markets to become more efficient, with lower process and transaction costs.
- Firms manage the risks of innovation, ensuring it does not jeopardise consumer protection or the integrity of the financial system.
- RegTech leads to more efficient and effective regulation and compliance.

Issues

- **Competition cannot develop effectively**, and might be stifled by incumbent firms through business models, and commercial and policy routes.
- **Innovation is used as a pretext** for non-compliance.
- **Technology businesses new to the financial sector** do not understand their regulatory responsibilities.
- **FinTech business models shift risk from financial firms to consumers** without consumers fully understanding the implications or having adequate safeguards.
- **Inflexible or unresponsive regulation** stifles opportunities for competition.
- **Regulation does not keep up** with new compliance and reporting technologies.

²⁹ 'FinTech' is the term that describes the intersection between finance and technology. It can refer to technical innovation applied in a traditional financial services context or to innovative financial services that disrupt the existing financial services market. InsurTech is also used sometimes to describe this intersection. It is a part of FinTech that focuses on innovation and revitalisation in the insurance sector.

³⁰ 'RegTech' is the adoption and use of technology to help financial services firms to understand and meet their regulatory requirements more efficiently or effectively.

Our key planned activities

Encouraging innovation, competition and new entrants to the market through Project Innovate

Project Innovate is the FCA's initiative to regulate in a way that fosters the benefits of innovation. Our aim for 2017/18 is to find ways to further improve Project Innovate's value and impact through the activities below.

Direct support for innovation businesses

We will continue to provide one-to-one assistance to innovative businesses in regard to the regulatory implications of their expected innovations as quickly and frankly as possible. The c. 350 firms we have helped in the past two years tell us this approach is valuable and we will continue it in 2017/18.

Regulatory sandbox – a safe space for innovation

Our regulatory sandbox gives businesses the opportunity to test the commercial and regulatory viability of their innovative concepts before they invest more heavily in them, while providing safeguards for consumers. As well as supporting businesses to pilot innovative products and services that can benefit consumers, the sandbox gives us an understanding of the opportunities and risks that innovation can create.

Automated advice

We set up our Advice Unit in 2016. We will continue to provide bespoke regulatory feedback to businesses planning to offer automated advice to the mass market ('robo-advice') as this could make financial advice available to more consumers.

We will also publish resources to help firms developing robo-advice services, using the information and insight from our Advice Unit's work with individual firms to date.

We will also explore the scope of extending this approach to other sectors.

International engagement

The work of Project Innovate already provides a world-leading example of promoting innovation by a regulator, which has been adopted in many countries. We will continue to publicise and explain the innovation-friendly benefits of UK regulation to FinTech clusters around the world and build mutually productive relationships with FinTech regulators in key jurisdictions. These relationships will create benefits and synergies for firms looking to introduce new products and services into more than one market. At the same time, consumers and the markets will benefit from the transfer of ideas and innovation between jurisdictions.

Regional engagement

In addition to engaging internationally we are also maintaining our close ties with the FinTech community based in London by directly engaging with firms, accelerators, trade bodies and thought leaders. We will continue to host themed weeks on specific areas of innovation, which is a valuable way of learning about developments and trends in innovation as well as hearing about regulatory uncertainties. We will also strengthen our domestic relationships through greater engagement with regional and Scottish FinTech clusters.

Improving compliance while reducing costs

We want to encourage RegTech innovation and adoption to increase firms' compliance with regulation while reducing the costs. We also want to foster innovation that benefits consumers and ensures their current and future needs are met affordably and fairly.

We will continue to work with the academic community and technology industry contacts to increase our understanding of technology trends and developments, and what they may mean for us as the regulator and for the firms we regulate. We will engage firms and other market participants on the challenges we identify, both experienced by the FCA and by firms, and seek collaboration to develop responses to those challenges.

Our priorities for 2017/18 under these aims include:

Regulatory reporting

Innovative RegTech technology can help firms interpret the FCA Handbook and submit the required regulatory information, in more economic, efficient and effective ways. We will continue the programme of work we began in 2016 to reduce firms' compliance costs by encouraging the industry to drive forward the development and adoption of technologies that can unlock the efficiency and effectiveness of regulatory reporting.

Extending access to financial services

Consumers can find it difficult to access financial services for a number of reasons and we believe there are opportunities for RegTech to help. In 2017, we will undertake

work with the Money & Mental Health Policy Institute to encourage technical innovation in products and services for consumers with mental health issues. This follows our TechSprint event in April 2016 where innovators explored potential technical solutions to access problems in financial services.

Real-time monitoring and surveillance

We will hold further TechSprints, discussion forums including roundtables, undertake specific CFIs and collaborative research, as well as test a series of new types of engagement, focusing our activities on the challenges that firms face, and are expected to face, in the near and medium term.

We will begin a new initiative looking at how near and real-time compliance monitoring and surveillance technologies can potentially reduce the regulatory burden. Initially we expect to focus on financial crime and the role technology could play in helping firms meet their 'know your customer' (KYC) and AML obligations.

New Bank Start-up Unit

New banks are a key part of bringing innovation to the sector. They do this either through the service they provide, the customers they target, the products they sell or the technology they use. The New Bank Start-up Unit was launched in January 2016 as part of our continued efforts to reduce barriers to entry to the banking sector. It is a joint initiative venture between the FCA and the PRA and helps new banks to enter the market and through the early days of authorisation. Through the Unit we provide new banks with the

information they need to help them navigate the process to become a new bank, as well as with focused supervisory resource during the early years of being authorised.

During 2016 the New Bank Start-up Unit also hosted two seminars and ran a number of events, which were attended by 250 representatives from prospective new banks, newly authorised banks, overseas regulators, trade associations, Government departments and consultancy firms. Their feedback has been positive and we will run further targeted events in 2017/18.

Throughout 2017/18 we will continue to offer the assistance and guidance that firms new to the sector need in order to stimulate competition and drive innovation to promote better outcomes for consumers.

Measures of success

- Positive feedback from those receiving direct support and sandbox participants.
- New market entries from firms involved with Project Innovate.
- Cooperation Agreements with regulators in key FinTech jurisdictions.
- Increased interest and innovation in RegTech within the financial services industry.

Our cross-sector priorities

Technological change and resilience

Technology plays a pivotal role in delivering financial products and services, and firms are adopting newer and evolving technologies. There is an increasing demand for technology to meet firms' business needs and support their strategies, while at the same time there is an increased level of cyber risks.



We have created a dedicated Cyber Specialists Team to oversee the way that firms we regulate manage cyber risk.

Technology brings opportunities but also risks. We have a key role to play in ensuring new technologies are safely adopted. We also work with firms so that existing technology and systems become more resilient to both cyber-attacks and outages, safeguarding consumers and markets, and building confidence in the effectiveness of financial technology.

- Firms perform robust testing and evaluation.
- Firms deliver proportionate and timely redress when consumers suffer loss or inconvenience.
- Firms build and enhance their capability to defend against, and respond quickly and effectively to, cyber-attacks.



Outcomes we seek

- Firms recognise that 'technological change and resilience' encompasses the need for robust processes, adequate resourcing and effective governance.
- Firms' technology is aligned to, and properly supports, their current and future business strategy, enabling ongoing innovation that meets consumer and market needs.
- Firms increasingly consider the importance of resilience and risk of cyber-attacks when building and developing their IT systems and processes.
- Firms improve their capabilities in identifying and addressing ongoing resilience, as well as managing maintenance and changes to their IT estates effectively.

Issues

- **Vulnerabilities in the design and management of systems and infrastructure.** This applies both to the build of new systems and weaknesses within existing IT estates, leading to increased outages, data losses and risk of cyber- attack.
- **Reliance on complex legacy systems.** This is particularly an issue in critical areas such as payments, with firms not planning sufficiently to ensure these systems can meet future demands. The implementation of ring-fencing legislation may exacerbate this risk if not well managed.

- **Continued pressures on margins, leading to increased outsourcing and offshoring** with resultant risks over the oversight and control of key functions and an increasingly complex chain of third-party relationships.
- **Cyber-attacks are increasing and pose risk to consumers and markets.** Some attacks will be successful and firms may not have adequate defences or effective plans to identify and respond to them.
- **Adoption of new technologies** such as cloud, new payment technologies, distributed ledger (blockchain), and open access data could lead to security or structural weaknesses and thus increased outages and risks to oversight and control.

Our key planned activities

Enhancing capabilities and keeping pace with developments

We are building our own expertise in resilience and cyber, continuing to develop and evolve our regulatory tools and increasing our

engagement with individual firms and other stakeholders such as trade and other industry bodies.

We will engage with the industry to regularly exercise a collective (firm and authorities) response to a range of scenarios that might cause a major operational disruption (see case study 1).

We continue to work with both UK and international regulators and supervisory authorities. Recent events have demonstrated that risks, events and outages are not confined to the UK. So active involvement with, and the ability to influence discussions in, international forums remain essential.

Safe adoption of new technology

The development and adoption of new innovations such as cloud and blockchain can potentially provide considerable benefits. These include increased functionality, greater competition and improved efficiency and speed of processing – all of which may ultimately reduce costs for the consumer.

As shown by our Guidance on Outsourcing to the Cloud & Other Third Party IT Services, we will continue to improve our understanding and, where appropriate, proactively communicate our views, working alongside our Project Innovate and RegTech initiatives.

Operational resilience

Firms' adoption of newer technologies and their reliance on complex infrastructures increases the potential for problems and outages of key systems.

The FCA, in conjunction with the Bank of England and the Treasury, will continue to engage with firms when outages of key systems or cyber-attacks occur, particularly where there is significant consumer or market impact. The FCA will usually lead the initial response because of the customer or market impacts that are identified first in most incidents. We will work closely with, and use the expertise of, the authorities and other agencies, such as the National Cyber Security Centre and the National Crime Agency,

Case study 1: Testing operational resilience across industry

Scenario-testing is a valuable way for firms, institutions, regulators and other authorities to assess how well they respond to a range of situations that might cause a major operational disruption. A number of authority and industry groups have been set up to oversee, design and deliver a strategy and programme to test operational resilience. This group includes the Bank of England, PRA and FCA. The programme involves running tailored and targeted exercises every year and a simulation exercise in alternate years. These exercises rehearse how well the industry and authorities' arrangements work individually and collectively to deal with major operational disruption.

Over 2016, building upon previous exercises, the group rehearsed further scenarios in both the retail and wholesale sectors. The exercises identified key pinch points and demonstrated how promptly and collaboratively all major stakeholders can act in those situations. The ongoing improvement of effective communications between authorities, government agencies and the wider industry will continue to be a key area of focus in the planning of future exercises in 2017/18.



Case study 2: An international toolkit for cyber resilience

The Bank of England's Financial Policy Committee has made recommendations on cyber risk, most recently in 2015. In response, our Cyber Specialists team worked closely with both the PRA and specialist cyber agencies to develop a practical cyber resilience toolkit. We have subsequently used this toolkit successfully within many firms across different financial services sectors. The benefits of the toolkit include the improved overview it has given us of these firms' cyber-resilience capabilities, without putting disproportionate burdens on the firms themselves. We are now working with these firms to understand how they are improving their cyber resilience to emerging and evolving cyber threats. We plan to use the toolkit across a much larger number of financial institutions over the course of 2017/18.

Given the global nature of many financial institutions and the international scope of cyber security, we have also been heavily involved in developing international best practice and guidance. We have, for example, been a key contributor to the development and publication of the 'Committee on Payments and Market Infrastructure – International Organisation of Securities Commissions Guidance on Cyber Resilience for Financial Market Infrastructures' and the 'G7 Fundamental Elements of Cyber Resilience for the Financial Sector'. These provide guidance on how to manage cyber risk effectively and explain the core risk management disciplines that both financial market infrastructures and the broader financial sector should use. We will continue to play a leading role on the international stage to help further develop best practices and implementation in cyber resilience across the industry.

Additionally, firms are increasingly outsourcing to a limited range of providers, which increases the number of firms potentially affected by a provider's technical failure. We will continue to assess, act on and communicate our expectations of effective resilience to firms and the industry. We will also work with firms to address weaknesses. We have seen some evidence of overall improvement in firm's response capabilities, as well as customer communications in the last year. But there remains room for improvement and we will continue to build upon this work in 2017/18.

Cyber risk

We have created a dedicated Cyber Specialists team to oversee the way that firms we regulate manage cyber risk. We will continue to undertake a significant amount of work in this area over the course of 2017/18 (see case study 2). We want firms to learn the lessons from both successful and unsuccessful cyber-attacks. To help facilitate this, we

will establish cyber coordination groups across five sectors to bring firms together in secure and trusted groups to provide a platform to share experiences and foster innovation.

Joining up other FCA initiatives

We will also look at resilience risks in other FCA initiatives. These include ring fencing, where significant restructuring could affect resilience. Competition and Markets Authority (CMA) recommendations to increase consumer information on resilience so they can consider this when choosing providers, and in the Payment Services Directive II, which aims to increase competition in payment services.

Measure of success

Over the 2017/18 Business Plan period:

- Perform technology and cyber capability assessment on 100% of firms considered 'high impact' if disruption were to occur in the financial services sector.

- Positive feedback from participants in our Cyber Coordination Groups.

Over the medium to longer term;

- Improved reporting by firms to the FCA of IT resilience incidents and cyber-attacks.
- Improved risk scores in our technology and cyber supervisory assessments of firms.
- Improved firms' resilience as shown in industry-wide exercises to test responses of firms to major operational disruption.
- Reduction in consumer detriment caused by IT resilience incidents and cyber-attacks.

Our cross-sector priorities

Treatment of existing customers

We continue to see firms' treatment of existing customers as a priority this year. We consider that there are further improvements to be made in competition and the basic standards afforded to consumers.³¹

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We would like existing customers to enjoy the benefits of increased competition and innovation.

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Our aim is to ensure that closed book customers do not receive less attention than new customers, and are kept well informed about the products they are invested in, including performance and charges.

An example of our continuing focus is our work with the closed book customers of life insurance firms. Following our thematic review findings, published in March 2016, we published guidance setting out our expectations that firms should proactively identify poor outcomes for back book consumers and take steps to address them.

Another example is from the general insurance add-ons market study and value measures pilot.³² By publishing these pilot data, consumer groups and market commentators will have commonly available indicators of value for insurers, which help to assess products. We expect that stakeholders' use of the published data will improve transparency in these markets and influence both consumer and firm behaviour, incentivising firms to improve the value their products offer to consumers.³³

Issues in the way existing customers are treated occur in a number of sectors and in different ways, and we therefore address them on a sector basis.

Outcomes we seek

We would like existing customers to enjoy the benefits of increased competition and innovation by firms in products and services, particularly:

- Firms give more information to customers on renewal in the relevant sectors, making pricing more transparent.
- There is greater product choice and availability.
- Barriers to switching or exiting are removed.
- Firms pay due regard to the interests of their existing customers and actively engage with them to give them a good service and improved outcomes.
- Firms actively compete to retain customers rather than take loyalty for granted.

31 December 2016: www.fca.org.uk/publications/finalised-guidance/fair-treatment-long-standing-customers-life-insurance-sector; Q&A: <http://recmgmt.is.fsa.gov.uk/livelink/livelink?func=ll&objaction=overview&objid=43621069>; www.fca.org.uk/publication/finalised-guidance/fg16-8.pdf; March 2016: www.fca.org.uk/publication/thematic-reviews/tr16-02.pdf

32 www.fca.org.uk/publications/data/gi-value-measures-pilot

33 www.fca.org.uk/news/press-release/financial-conduct-authority-publishes-general-insurance-value-measures-scorecard



Issues

- **Tougher economic conditions** may lead to firms seeking to 'manage' back book customers into more expensive/default products.
- **A growing number of over-indebted mortgage holders** and those with limited access to credit.
- **A future rise in interest rates** and the impact of long-term negative real rates may make it harder for borrowers, including those already in payment difficulties, to repay. If credit conditions tighten this can leave higher risk consumers with limited options.
- **Firms may restructure products, bundling together** add-on services to make comparison difficult or lock borrowers into higher rates.
- **Firms may apply unjustified exit or switching fees**, which reduce competition.
- **Consumers' weak bargaining position** could give Investment Management firms little incentive to compete on value for money.

Our key planned activities

We approach issues relating to existing customers on a sector basis. So work on existing customers is covered under each of the sectors. Examples include:

- Shopping around and switching [Pensions and retirement income].
- Wake-up packs [Pensions and retirement income].
- Our response to the CMA review of retail banking [Retail banking].
- Work on the strategic review of retail banking business models [Retail banking].
- Cash savings market study remedies [Retail banking].
- Firms' pricing practices [General insurance & protection].
- Maturity of interest-only mortgages [Retail lending].
- Customers with long-term mortgage arrears [Retail lending].
- Debt management sector review [Retail lending].

Measures of success

Over the medium to long term we would like to see an upward trend in existing customers' perception of:

- Choice of products.
- Comparison between products and services.
- Ease of switching.

Our cross-sector priorities

Consumer vulnerability and access to financial services

People can become vulnerable at any time in their lives, and vulnerability can be temporary, sporadic or permanent. At any one time, there are substantial numbers of vulnerable consumers in the UK, and we need to ensure markets work well for them.

Financial services are essential for people to fully participate in UK society, from being paid their wages to how they pay their utility bills. Increasingly, people and households are expected to take responsibility for their own financial well-being and decisions. These decisions are increasingly more complex, and we believe that a market where consumers never make poor choices is not feasible. Our focus is on ensuring the appropriate degree of protection for consumers. What is appropriate will depend to a large extent on the capability and circumstances of consumers, the sales environment and the complexity of the product or service. We also believe we should take steps to make clearer to consumers the degree of protection we can, and cannot, give them.

Our research on consumer vulnerability identified³⁴ that much of the consumer protection legislation is underpinned by the notion of the average or typical consumer, and what that typical consumer might expect, understand or how he will behave.

However, consumers with vulnerable characteristics or in vulnerable circumstances may be significantly less able to represent their own interests, and are more likely to suffer harm than the average consumer.

Further research on access to financial services³⁵ highlighted how consumers may be financially excluded from benefits that technology can create. Problems can deter consumers engaging in the first place, making it difficult for them to research the market and choose products.

Obstacles created at the application stage make it hard to use and switch products or to get help with any of these issues. An added problem is that access issues are often multi-dimensional so that consumers often have to deal with several barriers and at different stages of the journey.

Financial services need to be able to adapt to the changing circumstances of real life, rather than being designed for the perfect customer who never experiences

³⁴ Occasional Paper No. 8: Consumer Vulnerability – www.fca.org.uk/publications/occasional-papers/occasional-paper-no-8-consumer-vulnerability

³⁵ Published in Occasional Paper No. 17: Access to Financial Services in the UK – www.fca.org.uk/publications/occasional-papers/occasional-paper-no-17-access-financial-services-uk



difficulty. Vulnerability and access can affect people's interaction with any consumer market, but it is particularly challenging in the context of financial services due in part to the long-term nature of commitments, and the complexity of products and information.

We developed the following definition to guide our work in this area:

Access is the ability of consumers to engage with and use the financial products and services they need over their lifetime. There is growing understanding that consumers' ability to access these services helps to improve market integrity, drive competition and promote financial stability and economic growth.

Vulnerability occurs when someone, due to their personal circumstances, is especially susceptible to detriment, particularly when a firm is not acting with appropriate levels of care. People can become vulnerable at any time.

Outcomes we seek

The over-arching principle of fair treatment is important wherever consumers interact with financial services firms, and in particular when consumers are vulnerable. We want to see harm to consumers reduced by:

- Firms being able to recognise when consumers are or may become vulnerable.
- A more flexible and tailored response being provided for consumers when they become vulnerable.
- Firms developing innovative financial products that are clear, easy to understand, and easy to access.
- The costs of products and services being clear and transparent.
- Firms treating customers fairly when they take business decisions that will affect access.

Issues

- Societal and technological changes have increased the scope and sophistication of financial services. Their critical importance also affects consumers who are less capable of understanding these services and those who are or may be vulnerable.
- Some firms do not appropriately recognise when consumers become vulnerable.
- Processes and procedures in some firms do not consider how vulnerable customers should be treated.
- Firms' business decisions do not take appropriate account of impact on access.

Our key planned activities

Our Mission

Our *future Mission* proposed that the FCA would focus particularly on vulnerable consumers, and asked for feedback on this question. The final Mission document states that consumers in vulnerable circumstances are more susceptible to harm and generally less able to advance their own interests. So we will prioritise consumers who are unable to shop around over consumers who can shop around but choose not to do so. In particular, it reiterated that:

- Understanding vulnerability should be part of our intervention framework, not a separate process.
- Vulnerable consumers are more susceptible to harm, and often less able to represent their own interests.³⁶ As a result, harm they experience is often under-represented.
- To redress this imbalance, we will try to identify how important competing FCA priorities are to vulnerable consumers ('vulnerability mapping'). This should allow us to judge when we may act to prevent harm to vulnerable consumers, including in cases that might not otherwise be prioritised.
- To apply 'vulnerability mapping' we need more information about who might be vulnerable within markets. As a first step towards developing this information, we will publish our 'Consumer Approach' document in the summer which will consider this in more detail.

- In many cases, the best tool to reduce harm to vulnerable consumers may be with others. We will therefore work with third parties to improve outcomes. eg convening public sector organisations, charities, consumer groups and industry.

Consumer Approach

Following on from the Mission, we are developing our vision for consumers as part of our forthcoming 'Consumer Approach' document, which will set out how we meet our consumer protection objective over the next 3-5 years.

Our 'Consumer Approach' document will consolidate our current and previous research on consumer needs, attitudes and behaviour, as well as draw on external evidence. This paper will present an overarching FCA strategy for addressing the needs of UK consumers and will draw together separate strands of work with a consumer focus, including results from our Financial Lives Survey, Consumer Expectations qualitative research and other insights from around the FCA. It will also provide a baseline for reviewing progress and measuring change.

Sector-based work

The FCA has completed significant work to understand the needs of consumers in vulnerable circumstances and the needs of consumers struggling to access financial services. Our Mission highlights these as areas where we will continue to work with firms to make sure they treat customers fairly when they take business decisions

that affect the financially vulnerable or those trying to access financial services. This could include making changes to after-sales services or addressing the needs of those paying high, sometimes unaffordable insurance premiums (for example, consumers who have, or have had, cancer).

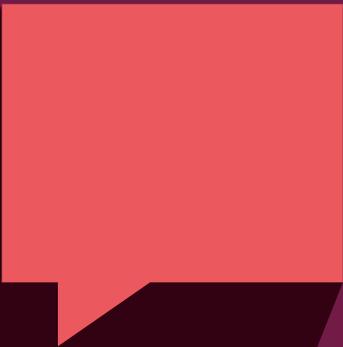
Many of our planned activities within the different sectors focus on vulnerability and access issues. For example, much of our work in the Consumer Credit sector focuses on vulnerable consumers. This includes our continued focus on high-cost credit and overdrafts.

In the mortgage sector, we will be looking at customers with long-term mortgage arrears, and at interest-only mortgages approaching maturity. We are also continuing our focus on preventing scams, especially relating to pensions, in which vulnerable consumers are often the target of scammers. Our work on innovation also looks at how new products and services could benefit vulnerable consumers and increase access to financial services.

Measures of success

Our 'Consumer Approach' document will set out in greater detail how we will measure the success of our work on consumers, including access and vulnerability. We will also use this paper as a baseline of consumer experiences in 2017, against which we can measure the effects of our actions.

36 FCA, Occasional Paper Number 8, p.6.



Many of our planned activities within the different sectors focus on vulnerability and access issues.



Our sector priorities

We divide the financial markets we regulate into seven sectors. This section explains our approach to each of these sectors and our priority activities in each.

Our approach for each sector focuses on the next 3-5 years and sets out what we want to achieve over that time. The priority activities in the Business Plan focus on our key activities for next year. This is based on our Sector Views analysis, which assesses each sector in detail, identifies the most important issues we need to address and the best tools we can use to do so.

Our sector priorities

Wholesale financial markets

Clean and effective wholesale financial markets in which competition works well, are vital to the UK's economic prosperity. Globally, they provide access to financing for firms and governments, and investment opportunities for retail and institutional investors. They also enable participants to manage financial and other risks over the long and short term. Their effectiveness relies on them being, and being seen to be, fair, transparent and efficient.



Market structure and firm business models are having to adapt.



These markets are diverse, ranging from the primary issuance of debt and equity and the operation of trading venues to the over-the-counter sale of complex derivatives. They are also dynamic and are going through a period of unprecedented challenge and significant change, driven by interrelated technological, regulatory and macroeconomic factors. As a result, market structure and firm business models are having to adapt.

We will continue to monitor the effects of changes on wholesale markets and take action if needed.

We will implement significant reforms that advance resilience, integrity and competition within wholesale markets through MiFID II. We will continue to focus on ensuring that firms effectively manage their conflicts, assess their risk and act in their clients' interests. Given the fast pace of technological change and rising risks of disruption, we will focus greater attention on technology and resilience. Preventing, detecting and punishing market abuse is also a high priority for us.

Outcomes we seek

- There are clean, effective and competitive wholesale financial markets that enjoy the confidence of all who undertake market activity in the UK.
- Key market infrastructure remains resilient.
- There is growing cross-industry collaboration on cyber risk.
- The monitoring and surveillance capability of the FCA, market participants and market infrastructures to detect, disrupt and deter market misconduct is strengthened.
- There is increased efficiency and effectiveness of primary markets to ensure they meet the needs of issuers and investors.
- Both corporate and individual market participants take responsibility for their part in maintaining clean, fair, effective and competitive markets. Firms and individuals understand the standards and rules that apply to them and are held accountable for their conduct.

Issues

- **Firms fail to manage their conflict of interests** effectively.
- **Firms fail to identify and manage market abuse risks** effectively.
- **Firms fail to manage financial crime risk** effectively.
- **Effective competition is undermined** by the abuse of market power in some areas.
- **Increased electronic and digital services and systems** in some markets and changing business models within firms, including outsourcing of critical functions, results in resilience and cyber risks in some markets.
- **Markets fail to provide a good environment for issuers to raise finance**, investors to enter and exit investments, and participants to manage risk.

Our key planned activities

Preventing market abuse

The EU's Market Abuse Regulation (MAR) took effect on 3 July 2016. Among other things, the regulation enhances, harmonises, and widens the application across the EU of existing rules prohibiting insider dealing and providing for the disclosure of inside information and dealings by Persons Discharging Managerial Responsibilities. The new regulation applies to a wider range of markets and securities, and aims to increase the integrity, confidence and protections within the EU's capital markets.

From January 2018, the Markets in Financial Instruments Regulation (MiFIR) will require firms to report to us a wider range of information about their trades, and for more asset classes.

This information will significantly increase the effectiveness of our market abuse work.

We will continue to work to embed and prepare for these new regimes, in order to deliver the most-effective response to the threat that market abuse poses to our markets.

Advancing resilience, integrity and competition in wholesale financial markets

MiFID II presents a comprehensive set of reforms, which take effect from 3 January 2018. These reforms will improve competition, consumer protection and market integrity across retail and wholesale financial markets.

We will ensure the new regime is implemented effectively, and realises the potential of the legislation to change markets significantly for the better. We will continue to develop our own capabilities to supervise these requirements, and will also continue to work closely with firms to ensure that they are prepared for these changes.

Effective competition in investment and corporate banking

In 2016 we completed a market study on investment and corporate banking services, focusing on primary market and related activities in the UK. We looked at issues around choice of banks and advisers for clients, transparency of the services that banks provide, and bundling and cross-subsidisation of services.

We found that participants in these markets generally use a 'universal banking' model, which involves the contractual cross-selling and cross-subsidisation of services. While many clients, particularly large corporates, feel this model works well, we found that some practices could hinder competition, especially for smaller clients.

39%

of OTC interest rate derivatives trading are made in the UK.

We considered a range of interventions and proposed that certain restrictive contractual clauses should be prohibited. We have developed a targeted package of remedies to address these concerns and to ensure competition takes place on the merits of the services provided. We will continue to implement these remedies in 2017/18.

Overseeing primary and secondary markets

The UK is a leading global centre for issuing and trading securities with issuers from almost every sector, and a broad range of investors, operating in UK markets.

We oversee primary and secondary market activity. Our aim is to be proportionate, risk-focused and forward-looking by educating the market and using a range of tools and techniques. Our rules help us protect market integrity by ensuring high standards of market practice and the appropriate level of disclosure by firms. In primary markets, we focus on transaction documents, corporate disclosures, and the sponsors that bring issuers to market. We ensure that these market participants comply with relevant EU and domestic prospectus, listing and disclosure rules. In secondary markets we focus on identifying, investigating and preventing market abuse across a wide range of assets and markets. We will continue to adapt our approach to respond to market developments and new regulations, such as the EU's Market Abuse Regulation and MiFID II.



We will continue to work to embed and prepare for these new regimes, in order to deliver the most effective response to the threat that market abuse poses to our markets.



Effectiveness of primary markets

Primary capital markets play a key role in supporting the wider economy by bringing together investors seeking appropriate opportunities to earn a return on their investments, and issuers wanting to access deep and liquid pools of capital to finance their businesses.

We committed in our 2016/17 financial year to a review of the UK's primary markets, and in the year ahead we will make and implement final policy statements and potentially consult further on a number of the possible changes that we identified through this review. One of these areas is reform to the Initial Public Offering (IPO) process to improve the flow of information to investors, on which we made proposals in a Consultation Paper (CP) published in March. A further Discussion Paper (DP) and CP published in February respectively present for debate and propose reforms to areas of the Listing Rules and broader primary markets regimes to ensure these continue to be effective in meeting the needs of issuers and investors. We will progress these discussions and make appropriate rule changes during 2017.

In April 2016 we published a report on the work and recommendations of the Debt Market Forum. This was a body of debt capital markets experts convened by the FCA to make recommendations on practical improvements that could be made to UK listed primary debt capital markets. In the year ahead we will undertake a survey of market participants to assess the impact of the Forum's recommendations and whether we need to make further improvements to our primary market operations. The issue of whether the UK needs a multilateral trading facility focused on the issuance of wholesale debt, identified in the Debt Market Forum, is one of the issues on which wider stakeholder comment is invited through this year's DP on the effectiveness of primary markets.

Throughout the year, we will continue to contribute to EU work to introduce a Securitisation Regulation and to update existing EU provisions for prospectuses. Where appropriate, this will include providing input to the negotiation of the overarching legislative framework and working within the European Securities and Markets Authority (ESMA) to develop detailed implementing measures. We will also consider whether changes to our regime should be made to take account of the forthcoming EU Shareholder Rights Directive.

Supervising exchanges and administrators of benchmarks

We supervise recognised investment exchanges for both conduct and prudential issues. We aim to ensure that, through their primary and secondary market services, they promote fair, orderly and efficient markets that are open to competition and operate in the interests of market participants. These groups are international and diverse and our supervisors actively engage with other regulatory authorities, including the Bank of England, which supervises central counterparties, and financial market regulators in other jurisdictions.

We also supervise the administrators of eight regulated benchmarks, and the submissions of the 20 banks which contribute to setting the LIBOR rate. Our aim is to ensure that benchmarks are reliable and have integrity so that markets can trust the rates that are set. From 1 January 2018, under the EU Benchmark Regulation our regulatory remit will broaden. We will regulate a far greater number of benchmarks and their administrators to ensure that benchmarks are robust and reliable and to minimise conflicts of interest in benchmark-setting processes.

Enhanced resilience to technology and cyber risk

We have concerns about the resilience of firms' systems to cyber risks, especially given the significant pace of technological change. We cover our work in these areas in detail in the cross-sector priority section of the Business Plan, in the 'Technological change and resilience' chapter.

Improved culture, accountability and governance

Improving culture, accountability and governance are priority areas for us. We have introduced the '5 Questions' strategy for wholesale banks, which is designed to prompt individual firms to identify and address conduct risks wherever they arise throughout the firm. Details of our firm supervision and other work in these areas are provided in the cross-sector priority section of the Business Plan, in the 'Firms' culture and governance' chapter.

UK is the largest global exporter of financial services accounting for a

\$97bn

trade surplus in Financial Services in 2015.

Our sector priorities

Investment management

The investment management sector acts on behalf of individuals and institutions who want to increase the value of their assets or generate future income through investments. The sector manages nearly £7tn of collective, institutional and individual assets, and over three-quarters of UK households with occupational and personal pensions use the services of asset managers. Our focus is on making competition work well in this market.

The size of this sector is significant and has a direct impact upon consumers, either through their retail investments or their pension funds. So it is essential that competition in this sector works effectively and this remains a priority area for us. Because of its increasingly important interaction with other wholesale participants, we also see the sector playing a key role in upholding overall market integrity and contributing to financial stability.

We want to ensure that competition is working effectively, and that investment management firms deliver good consumer outcomes with products that offer value for money. We will focus on the conduct of firms to ensure that markets remain clean and resilient.

Outcomes we seek

- Firms act in the best interests of their investors and earn customer trust.
- Investors reward firms that act in their best interests.
- Investment management products deliver value for money.
- Investors understand the objectives of the funds they are investing in.
- Funds report their performance against appropriate benchmarks.
- Fund managers implement available liquidity management tools when they face investor redemptions and/or valuation issues, and manage conduct risks effectively.
- Fund managers remain responsible participants in the wholesale markets.
- Critical service providers, particularly custody banks, achieve acceptable levels of operational resilience.

Issues

- **Weak price competition** may mean investors pay too much for investment management services.
- **Weak governance** may lead to poor product design and weak oversight of portfolios.
- **Unidentified or poorly managed conflicts of interests** might cause harm to portfolio operators and end-investors.
- **Poor advice from investment consultants** might result in institutional investors making investment decisions that do not meet their needs.
- **Poor liquidity management** in investment funds creates risks of consumer detriment or wider disruptions to the financial system in stressed market conditions.
- **Disorderly failure of investment portfolios and market abuse** could disrupt trust in the financial system.
- **Providers of critical services to the sector**, including custody banks, may not be able to meet current service standards or ensure continuity of service.

Our key planned activities

Asset Management Market Study

In 2016 we published the interim report to our Asset Management Market Study, which looked at whether competition is working effectively in this sector. We found that price competition is weak in a number of areas and that, despite a large number of firms in the market, the asset management industry has seen sustained high profits over a number of years. In addition, investors are not always clear what the funds' objectives are and fund performance is not always reported against an appropriate benchmark.

We have also found concerns about the way the investment consultant market operates.

Our interim report proposed a significant package of remedies to make competition work better and to protect those least able to actively engage with their asset manager. These remedies include:

- Introducing a strengthened duty on asset managers to act in the best interests of investors, including reforms to hold asset managers to account for how they deliver value for money.
- Introducing an all-in fee so that investors can clearly see what is being taken from the fund.
- Introducing a number of measures to help retail investors identify which fund is right for them. These include requiring asset managers to be clear about the objectives of the fund, clarifying and strengthening the use of benchmarks and providing tools for investors to identify persistent underperformance.
- Making it easier for retail investors to move into better value share classes.

- Requiring clearer communication of fund charges and their impact to retail investors, both at the point of sale and in ongoing communication.
- Requiring increased transparency and standardisation of costs and charges in the information given to institutional investors.
- Exploring the potential benefits of greater pooling of pension scheme assets.
- Requiring greater and clearer disclosure of fiduciary management fees and performance.

We will publish the final report in Q2 2017, and consult on proposed remedies and interventions.

Fund liquidity strategy

We will continue to participate in the ongoing debate with national and international authorities around the liquidity management of funds, highlighted by some firms suspending open-ended property funds after the EU referendum vote in June 2016.

Our Discussion Paper on the liquidity management in open-ended funds sets out for debate the risks and tension associated with funds that offer daily redemption terms, while managing assets that are not revalued on a daily basis.

Following stakeholder feedback we will review our policy options and the available tools that asset managers have to manage liquidity when facing redemptions and valuation issues, and assess how adequate they are in managing conduct risks and addressing financial stability concerns.

This work should ensure that liquidity management in funds allows for a fair treatment of all customers, including those who remain invested, and does not amplify disruptions to the financial system in stressed market conditions.

Custody banks strategy

Custody banks provide critical support services to the funds industry and trading activities, which require them to be accurate, secure and resilient.

We are planning a number of interventions in this sector. We will continue our work to ensure firms meet our CASS standards governing the safekeeping of client assets, we will support the PRA's work to map and evaluate critical infrastructures in firms, we will evaluate custody banks' resilience and resistance to cyber-attacks, and we will evaluate the quality of product governance and controls at firms.

£7tn

of collective institutional
and individual assets managed
by the sector.

Our sector priorities

Pensions and retirement income

The outlook for UK consumers' ability to save more for their retirement, and generate a stable and adequate retirement income remains challenging. The reasons for this include low levels of wage growth, declining ability to save, increased levels of household borrowing and reduced investment returns. This is exacerbated by a rise in less secure forms of employment which reduces consumers' ability to regularly contribute into a pension scheme. The UK's ageing population and the gradual increase in life expectancy also mean that people will need to fund increasingly longer retirements.

To generate adequate income in retirement, consumers might need to increase their contributions and work for longer. Pension providers may place greater focus on costs and value for money to offset the decline in investment returns.

The pensions and retirement income sector has gone through major changes over the last two years, with the Government's introduction of the pensions reforms in 2015. The market has been adapting to these changes, and our regulation of the market has focused on embedding the reforms and making sensible adjustments to our rules to support the reforms. We introduced rules to ensure we protect consumers and that firms were clear about our expectations in the new environment. We also started work on the Retirement Outcomes Review, which assesses how competition is developing in the retirement income market.

With the reforms now bedding down, we will focus in the future on how people access their pension savings ('decumulation') following the reforms. We will also be focusing on non-workplace pensions and continue to educate consumers about pension scams. Alongside these we will also develop and publish a strategy for the sector.

Later in 2017 we will publish our findings from the Retirement Outcomes Review.

Given its impact on the lives of so many people, we are particularly proactive in this sector, both implementing Government initiatives and undertaking our own work.



Outcomes we seek

- Advice, guidance and information given to consumers meets their needs and they know how to find it. There is increased competition and innovation in the sector, particularly in decumulation products that offer good value for money.
- Firms offer products and services that are better value for money for consumers, and actively and honestly compete to keep them.
- There is reduced harm to consumers from investment scams.
- We provide proportionate regulation that supports innovation and competition for consumers.

Issues

- **Consumers cannot or do not want to get adequate advice** and guidance to make the best choices for saving for, and funding, their retirement.
- **Relatively few new service providers** entering the market, consumer inertia and poor consumer understanding reduce competitive pressure.

- **Consumers cannot assess and compare pension products** as information on product features and costs is hard to understand.
- **Pension freedoms and other changes** mean consumers are at greater risk of being targeted by a range of different scams.

Our key planned activities

Pensions strategy

We will publish a strategy for the Pensions sector, setting out our regulatory approach to this sector. As part of this, we will reflect on our current work through our supervision, policy and competition projects and consider the impact of related workstreams, such as the Asset Management Market Study, on this sector. Our strategy will also explain how we work with other regulators and Government to further our objectives and identify areas where further progress is needed.

Retirement Outcome Review

We launched the Retirement Outcomes Review in July 2016 to assess the impact of the pension reforms on competition in the retirement income market.

It reviewed how consumers make choices to access their pension savings without using an adviser and whether they were shopping around and switching to products that better meet their needs. It also looked at how firms have changed their business models and the impact of these changes on competition along with other factors such as the pace of regulatory change.

We will publish an interim report in summer 2017, followed by the final report at the beginning of 2018. These reports will identify our findings and propose a package of remedies to improve competition to benefit consumers.

Taking drawdown without getting advice

The Review will look at what steps we can take in the future to help consumers who do not get advice. We also need to look at how firms are complying with the existing rules, including whether they are providing adequate information to enable consumers to make an informed decision.

66%
of workers are
now members of a
workplace pension

(The Pensions Regulator)



We will review the sales processes and ongoing communications of a sample of firms making non-advised drawdown sales since the pension freedoms were introduced. We will assess whether firms are complying with our rules by giving customers adequate information to make an informed decision when they decide to draw down their pension. We will also examine if firms give their customers adequate post-sale information to enable them to continue to make decisions that support good outcomes.

Shopping around and switching

In November 2016, we proposed requiring annuity providers to tell their customers how much they could gain from shopping around and switching provider before they buy an annuity. Depending on the results of this consultation exercise, we will introduce new rules in this market.

We will also complete our work on how consumers react to 'wake-up' packs, which are sent to consumers approaching retirement to encourage them to take action. We will analyse the effect these packs have on consumers' decisions to use their pension savings and use the findings to decide if we should take action to improve these customer communications.

Non-workplace pensions

We will undertake initial discovery work to find out if the non-workplace pensions market is sufficiently competitive to work effectively in consumers' interests.

Workplace pensions

We will continue to work closely with the Department for Work and Pensions (DWP) to consolidate and review the improvements in value for money achieved so far in the workplace pensions market.

A dashboard to give consumers the full picture

Both the Financial Advice Market Review (FAMR) and our Retirement Income Market Study recommended the creation of an online pensions dashboard so that consumers can view all their lifetime pension savings in one place.

The Government has committed to ensuring the industry designs, funds and launches a pensions dashboard by 2019.³⁷ We will provide relevant help to firms as they develop the dashboard.

Raising awareness of and tackling pensions scams

We will undertake the next phase of our ScamSmart campaign to reduce both pension scams and the number of consumers falling victim to them.

To complement ScamSmart, we will also look at ways we can work with Government, other regulators and consumer organisations to create effective messages to help consumers understand fraudsters' techniques.

We will also consider if legislative or rule changes are needed to close any loopholes that scammers currently exploit and to further deter fraudsters.

³⁷ www.gov.uk/government/uploads/system/uploads/attachment_data/file/508193/HMT_Budget_2016_Web_Accessible.pdf

Our sector priorities

Retail banking sector

There are over 72 million active personal current accounts in the UK, with retail deposits of over £1.55tn, comprising current accounts, savings products and SME banking.³⁸ As the sector acts as consumers' main gateway into financial services, it is imperative that it is accessible, secure, trusted and that competition works well.³⁹

Retail banking business models face pressure from legacy regulatory and systems issues and from innovations to their core payments role.

Technological and societal change will affect both the size and look of the market over the next decade. Competition is still relatively weak as the sector remains characterised by low consumer engagement and low levels of switching. This reduces incentives for existing firms to compete and creates barriers to expansion for challenger firms, resulting in less innovation and higher consumer costs.

As well as these challenges, the sector faces major structural change because of new regulation. This includes ring-fencing, Payment Services Directive 2, the advent of 'Open Banking' and cultural change, including the SM&CR. Given the significant scale and pace of change in retail banking, we will focus on the implementation of these significant market interventions to enable firms to embed these changes effectively and minimise implementation risks.

Outcomes we seek

- Cultural transformation programmes in firms improve customer focus and reduce the risk of firms treating customers unfairly.
- Innovation that benefits consumers is introduced to the market, while maintaining security, resilience and integrity.
- Consumers have appropriate access and effective choice.
- Firms' systems are resilient and secure, and minimise disruption to consumers.
- The legal separation of banks as part of ring-fencing does not negatively affect consumers, market integrity or effective competition.
- Firms have proportionate and effective anti-money laundering (AML) controls.
- There is a decrease in banking fraud.
- Consumers and firms have faith in the integrity of the market.

³⁸ <http://bankofeng.uk/FoVI30aIAY1>

³⁹ We define the retail banking sector as payments and deposits for individuals and SMEs, covering personal and business current accounts, personal and business savings, and regulated payment services such as merchant acquiring, electronic money and money transmission.



Competition is still relatively weak as the sector remains characterised by low consumer engagement and low levels of switching.



Issues

- **Weak competition** in retail banking results in existing firms retaining their position as they have limited incentives to improve quality and price.
- **Low levels of cultural change** might mean firms do not adequately consider the interests of their customers or treat them fairly.
- **Insufficient operational resilience due to legacy IT systems** might result in service disruptions and make firms more vulnerable to cyber attacks.
- **Poor controls mean that firms might fail to identify and adequately manage money laundering risks** and consumers might become vulnerable to fraudsters.
- **Firms are de-risking** and making efforts to cut costs, resulting in some consumers being unable to access the services they need.
- **Implementing ring-fencing creates a number of operational challenges** for banks and may also lead to increased risks to consumers as banks change their business models.
- **Firms may need to revise and adjust their business models**, potentially increasing risks to consumer outcomes, market integrity and competition.

Our key planned activities

Strategic review of banking business models

The retail banking business model spans multiple product lines and the actions of firms in one market can affect consumers in another. The scope of the CMA's market investigation focused on the supply of retail banking services to personal current accounts and to small and medium-sized enterprises and did not look holistically at market outcomes in the retail banking sector. In 2017/18 we will launch discovery work to examine the business models used in the retail banking sector, focusing on the links between different parts of the business and their relative profitability. This work will include the impact of free-if-in-credit banking, for example, its effect on different groups of consumers. We will use the analysis to deepen our understanding of the impact of emerging developments, and to enhance our approach to current and future regulation of retail banks.

Improving competition in the sector

In November 2016, we published our response to the CMA's final report on its investigation into competition in the retail banking market. We committed to undertake research into measures designed to: improve transparency for overdraft users, improve service information indicators, and prompt increased customer engagement.



We will continue to work with firms and other stakeholders to research what interventions may be needed and to design them to be effective. We will ensure that this work remains aligned with the broader set of CMA remedies, as well as our own work on high-cost credit and overdrafts, and the wider work on the strategic review of retail banking business models.

We continue to consider steps to improve the treatment of long standing customers in the cash savings market. In addition to new rules that came into effect in December 2016, we published the third and final set of data under our Sunlight remedy .

We are evaluating the effectiveness of this remedy and are considering whether to introduce this disclosure into Handbook rules. We will align any further action with other potential service indicators.

Given our continued concerns about the treatment of long standing customers, we may need to look at what other actions are needed to achieve more effective competition.

The British Bankers' Association, the Building Societies Association and Tax Incentivised Savings Association agreed that a minimum of 80% of cash ISA transfers will be carried out within seven working days and committed to carry out a study on improving this further. The industry will publish details of its performance against the target quarterly, starting in April 2017. The FCA will continue to work with industry on improving the speed of transfers and also consider the need for any broader regulatory intervention across the savings account market to improve switching.

Ring-fencing

After the financial crisis, the Government decided to ring-fence core banking activities from other activities. This is to protect retail banking from unrelated risks elsewhere in the bank group or shocks affecting the wider financial system. The rules introduced require major banks to separate their retail and wholesale activities into two distinct legal entities by 2019. This will change banks' business models and cost structures, and may change market dynamics.

The PRA is the lead regulator for implementing ring-fencing and is responsible for supervising banks' compliance with the rules. We have key responsibilities for implementing the regime effectively and are working with the PRA, the Bank of England, the Treasury and the larger



We remain concerned about operational resilience, particularly legacy IT systems and banks' defences against cyber-attacks.



UK banks to support it. In 2017/18, we will continue work with banks to ensure they are appropriately mitigating risks arising from changes to their business models and structures that may affect their customers or the wider market. This includes clearly communicating changes to customers, particularly any new account details that may be required as a result of restructuring. We will be reviewing revised governance arrangements and operating models, including technology changes, against our accountability, controls and resilience requirements. We will also, in collaboration with the PRA, engage with the wider banking and payments industry to ensure payments changes made as a result of ring-fencing are well managed.

Payment Services Directive 2

The Payment Services Directive 2 (PSD2) came into force in January 2016, and will need to be implemented by January 2018. It introduced new rules to increase competition in the retail banking and payments markets. These rules should strengthen consumer protection, extend regulatory scope, enhance the security of the sector and open access to payment account information to third parties, such as account aggregators.

Following the Treasury's consultation on the UK implementation of the Directive, we are consulting on our approach to implementing the directive, continue to work with European agencies to develop the necessary Regulatory Technical Standards and Guidelines, and identify how we supervise firms. We will also continue to work with firms and other stakeholders to assess how prepared they are to achieve compliance.

In parallel to PSD2, we will continue to work as an Observer on the Open Banking Implementation Entity. While this body was established by the CMA to deliver an open API standard for personal and business current accounts, the work provides an opportunity to deliver a market-wide solution for firms that will have to provide access (with customers' consent) to account-level data and functionality in order to comply with PSD2.

Senior Managers and Certification Regime

The SM&CR came into effect in March 2016. The regime focuses on enhancing individual accountability at the most senior levels in deposit takers and PRA-designated investment firms, and raise their standards of conduct at all levels.

In 2017/18 we will focus our work on firms that have not been able to meet this timetable, as well as on how firms have embedded the regime. We will particularly examine how the regime has been embedded during firms' business planning and how their business strategies take into account customer outcomes.

We will also look at third-party outsourcing of oversight and management, and how the firms that undertake this work are implementing the regime.

We cover our work on SM&CR in more detail in the cross-sector priority section of the Business Plan, under 'Culture and governance'.

Financial crime and IT resilience

We remain concerned about operational resilience, particularly legacy IT systems and banks' defences against cyber-attacks. We also continue to have concerns about financial crime risks in the retail banking sector.

We cover our approach and planned work on these areas in the cross-sector priority section of this Business Plan, in the 'Technological change and resilience' and 'Financial crime and AML' sections.

Payment Protection Insurance (PPI) redress

The current complaints framework and our supporting supervisory work has so far resulted in over £24.5 billion redress being paid to customers.

In March 2017, we published a Policy Statement⁴⁰ which introduces a PPI complaints deadline accompanied by an FCA-led communications campaign. The relevant rules will come into effect in August 2017 and if consumers want to make a complaint about PPI they must do so before 29 August 2019.

The accompanying communication campaign will launch at the end of August 2017 and will run over the two years to raise awareness and understanding of PPI and prompt consumers to make a decision about whether to complain before the deadline. We will be assessing at regular intervals how the campaign is performing over the period and make any necessary changes in response to our findings.

Our Policy Statement also introduces new rules and guidance on how firms should handle complaints about undisclosed high commission, in light of the Supreme Court decision in *Plevin v Paragon Personal Finance Limited*.⁴¹ These will come into effect on 29 August 2017.

We will be working with firms in the period before the new rules and guidance come into force to ensure that they are adequately prepared, and will be monitoring firms closely over the following two years to ensure that consumers receive the redress they are due in a timely manner.

72m
personal current
accounts, with retail
deposits of £1.55tn

(December 2016)

⁴⁰ PS17/3: Payment protection insurance complaints: feedback on CP16/20 and final rules and guidance.

⁴¹ The Court ruled that the lender's failure to disclose the large commissions payable out of the consumer's PPI premium made their relationship unfair under s140A of the Consumer Credit Act 1974.

Our sector priorities

Retail lending

The retail lending sector exists to meet the borrowing needs of consumers. It is broadly split into mortgages and consumer credit, and covers everything from credit for day-to-day expenses to buying property. Increasing levels of household borrowing mean that these sectors remain a priority for us.

The mortgage market has seen significant change as a result of the mortgage market review. Within the market there are a number of areas where consumer outcomes could still be improved, which we will continue to address.

We are also working with firms in the consumer credit sector to help them understand and adapt to our regulatory regime and to raise standards overall. We are also intervening to tackle the highest levels of consumer harm in the riskiest sub-sectors, along with focusing on evolving business models and the competitiveness of the sector.

Outcomes we seek

- Consumers can get products and services that are suitable, affordable and right for their circumstances.
- Consumers have appropriate protections and redress. Consumers get clear information about product features and are able to compare between products and services. Both firms and consumers behave responsibly so that loans can be repaid even if the economic environment changes.

- Firms take appropriate account of consumers' individual circumstances when they are in financial difficulty.
- Firms compete on what matters to consumers, including price, product and service features, and innovate accordingly.
- Firms' business models are suitable, sustainable, and consider the interests of consumers. Consumers are engaged in the market, and actively shop around and switch between providers to get the best deal.

Issues

- **Consumers in financial difficulty** may be treated unfairly by firms.
- **Inadequate affordability assessments** may result in consumers not being able to repay.
- **A lack of clear information and too much complexity** may hamper consumers' ability to compare and assess options.
- **Existing consumers may suffer** financial or other detriment through poor firm conduct.



- Some consumers who can afford credit may have trouble accessing products or services.
- Firms' business models and culture pose risks to consumers.

Our key planned activities

Maturity of interest-only mortgages

Around 1.8 million UK home owners currently have outstanding interest-only mortgages (excluding buy-to-let), and many do not have an appropriate strategy to repay them. We will look at how firms treat borrowers whose interest-only mortgages are approaching maturity and their ability to ensure these customers are treated fairly. This will include those interest-only mortgages that are due to be repaid by 2020 – where borrowers have the least amount of time to find a solution.

Customers with long-term mortgage arrears

In 2008, 22% of properties in arrears were repossessed. In June 2016, this figure was just 2.7%. However, over the same period, the number of mortgages with long-term arrears of over five months rose from 49,000 in 2008 to over 61,500 in June 2016.

While firms are offering more forbearance to customers in financial difficulties, in some cases providing forbearance over a long term may not always be in the customer's best interests. This could be the case, for example where forbearance does not ultimately enable customers to pay their arrears, but only increases their debts. We will assess how firms are using forbearance and how well they are delivering fair customer outcomes, and take further action if needed.

Mortgage market study

In December 2016 we published the terms of reference for a market study looking at consumers' ability to make effective choices in the first charge residential mortgage market.⁴² The study focuses on whether tools, including advice, help consumers make effective choices, and whether commercial relationships work for consumers' benefit. We want to understand whether these consumer tools give them clear and adequate information to make an informed choice between products and services and know if they are getting good value for money.

We will publish an interim report in summer 2017, setting out our analysis and preliminary conclusions including any potential remedies. We will publish our final report in early 2018.

42 MS16/2 www.fca.org.uk/publications/market-studies/mortgages-market-study

1.8m
outstanding
interest-only
mortgages
(excluding
buy-to-let).

High-cost credit and overdrafts

We will continue to focus on high-cost credit⁴³ as it is a high-risk area that affects vulnerable consumers.

In November 2016 we issued a Call for Input, covering high cost products, overdrafts, the high-cost short-term credit (HCSTC) price cap, and repeat and multiple HCSTC borrowing.

We will look at all high-cost products to build a full picture of how these are used, whether they cause harm and, if so, to which consumers. We will then be able to decide if we need to intervene further. We will also review the overdraft market in detail following the CMA's review, which identified problems in the market.

We will also review the price cap on HCSTC loans which came into force in January 2015. We will look for evidence on whether the cap should be changed, and the impact on consumers excluded from HCSTC because of the price cap. We will publish our findings on the review of the payday cap in the summer of 2017.

Point of sale: Fees and charges

We are concerned that firms may impose inappropriate fees or costs on consumers or inappropriately sell credit at the point of entering into a transaction. We will explore whether the fees, charges or other costs paid by consumers are influenced by commission, or other remuneration, models operating between firms – such as lenders and brokers. We may also consider whether firms exploit a point of sale advantage to charge higher than normal fees, or to sell credit to consumers for purposes for which it may not be suitable.

Debt management sector review

We will continue to monitor the debt management sector to ensure that it is fit for purpose and that firms are treating their customers fairly, particularly those in vulnerable circumstances. This follow-up work will ensure that our standards are being met and maintained.

Motor finance

We are concerned that there may be a lack of transparency, potential conflicts of interest and irresponsible lending in the motor finance industry. We will conduct an exploratory piece of work to identify who uses these products and assess the sales processes, whether the products cause harm and the due diligence that firms undertake before providing motor finance.

Following the review we will assess whether and how to intervene in the market.

Credit card market study remedies review

Last year we published the final findings of our Credit Card Market Study. It found that many cardholders were in arrears, default or had persistent levels of credit card debt. We set out proposals for a set of remedies. As part of this we are currently consulting on proposed new rules designed to help consumers take control of their finances and avoid persistent debt and avoidable charges.

Once the remedies have been implemented, we will review their effectiveness and assess if we need to intervene further. We will also continue to work closely with consumer groups and industry to deliver changes to help consumers gain more control over their finances.

⁴³ High-cost credit includes payday loans, home-collected credit, catalogue credit, some rent-to-own, pawn-broking, guarantor and logbook loans. Other credit products – such as motor finance, credit cards, overdrafts and some instalment lending – may be high-cost, particularly for less creditworthy customers or depending on how they are used.

Our sector priorities

General insurance and protection

The general insurance and protection (GI&P) sector protects individuals and businesses against the cost of uncertain and often unpredictable events. Without the protection of insurance, many social and economic activities could not take place. It is vital that this market, including the wholesale market underpinning it, works well.

In recent years, our policy and supervisory work in this sector has focused on issues affecting consumers, particularly in the retail and commercial sub-sectors. Over the next three years we will monitor and review these issues to ensure that progress is made and sustained, and will intervene further if necessary.

We will also shift some of our focus from issues directly affecting individual and small and medium-sized enterprise (SME) consumers to market structures, incentives and distribution, and will begin discovery work on a number of key areas. Our work cuts across the GI&P sub-sectors.

Outcomes we seek

- Customers, including those with complex needs, are able to evaluate and access insurance products and services that are suitable for their needs.
- Claims are dealt with in line with customers' reasonable expectations of the performance of the products and services provided.

- Firms demonstrate consumer-focused culture and compete not only on price but on product features and services.
- Customers have trust and confidence in the firms they interact with and that their personal data and information will be used by firms in a fair and reasonable way.
- There is suitable governance and oversight of outsourcing arrangements and the wider distribution chain.
- Existing customers are treated fairly and inertia is not exploited.
- Firms have appropriate systems and controls to identify, mitigate and manage conflicts of interest and reduce the risk of financial crime.
- Insurers and intermediaries have adequate levels of capital to ensure products and services deliver in line with customers reasonable expectations.
- The UK general insurance sector is recognised globally for its high standards of market integrity.



We want to ensure that the wholesale insurance market is working well and fosters innovation and competition in the interests of a diverse range of consumers.



Issues

- **IT failures, data protection issues and risk of cyber-attacks** may lead to customer detriment.
- **Customers could choose unsuitable products** by focusing on headline price rather than on suitability.
- **Intense competition can lead to poor advice** and gaps between consumer expectations and reality.
- **Parts of the market have poor governance** and oversight of complex distribution chains, which may lead to poor consumer outcomes.
- **Vulnerable or high-risk consumers cannot access** general insurance products and services.
- **Firms do not have effective systems and controls** to mitigate issues of financial crime, conflicts of interest and inducements.
- **Small businesses (SMEs)** could purchase inappropriate cover for their needs, and underestimate the levels of cover required.
- **Wholesale market developments** may not improve market efficiency and consumer outcomes.

Our key planned activities

Market study on wholesale insurance market

We want to ensure that the wholesale insurance market is working well and fosters innovation and competition in the interests of a diverse range of consumers.

We will conduct a market study to assess how effectively competition is working in these markets, including how firms ensure practices do not create market integrity and conduct risks. Following the publication of this market study, we will consider appropriate remedial actions.

Value in the distribution chain

Our review into the effectiveness of governance and oversight of delegated authority outsourcing showed that the length of the distribution chain can potentially erode the value of a product or service in different sub-sectors.

We will conduct a further review to understand the end-to-end relationships in these distribution chains. The findings will help us decide whether, and what, further action is required in this sector.

Firms' pricing practices

In September 2016 we published our Feedback Statement on our Call for Inputs on Big Data in retail general insurance. We proposed specific discovery work to look at pricing practices in a limited number of retail general insurance firms. This will ensure we can gain a better understanding of how these developments are affecting the market. We will carry this out in 2017/18. We will look at how firms' pricing approaches and rating factors work in practice, as well as the drivers and the types of systems and data firms use to decide the final price to consumers.

Following this work, we will consider whether, and what, further steps need to be taken in this market.

Insurance Distribution Directive

The Insurance Distribution Directive (IDD) is a new EU legal framework for insurance distribution which, replaces the Insurance Mediation Directive.

The IDD regulates the activities of all distributors of insurance products. It states what information distributors should give their customers, imposes conduct of business and transparency rules and clarifies the rules for cross-border business. It also includes new requirements for selling insurance products that have investment elements, to ensure

a similar level of protection with other investment products that are regulated under MiFID II.

The IDD will become UK law by February 2018.

IT resilience

We have concerns about the resilience of firms' systems because firms often have complex and legacy systems. Complexity is increased by the rise in outsourcing arrangements and mergers and acquisition activity. This heightens the risk of operational risk issues affecting the ability of firms to provide the expected levels of service to customers and increases the risk of poor consumer outcomes.

The risk of compromise to the integrity of firms' systems, particularly where large volumes of personal and commercially sensitive data exist, is heightened by the increased likelihood of cyber-attack. Increasing digitisation exacerbates these issues and presents significant consumer protection and market integrity risks.

We cover our work on operational resilience in detail in the cross-sector priority section of the Business Plan.

Our sector priorities

Retail investments

The retail investment sector has been affected by a number of regulatory changes in recent years.

We will be focusing on completing the implementation of FAMR and MiFID and allowing the work to embed and take effect in the sector. We will also undertake projects to find out if there are specific areas of risks we should address now and in the future, particularly with investment platforms.

The Retail Distribution Review, which came into effect in 2013, made significant changes to the investment advice market. It required firms to clearly show how much consumers pay for financial advice and what they pay for. It also improved professional standards by increasing the minimum level of qualification for all investment advisers.

FAMR explored ways to encourage the development of a market to deliver affordable and accessible financial advice and guidance to everyone. It made a series of recommendations that are in the process of being implemented. MiFID II, which is currently in implementation phase, aims to make financial markets even more open, efficient, resilient and transparent, and to strengthen investor protection. The MiFID II new standards will come into effect in January 2018.

Outcomes we seek

- An increase in consumers' willingness to use and trust the sector.
- There is improved access to advice and guidance for consumers.
- Advisers provide outcomes for consumers.
- Focus from advisers on value for money for consumers, including the total cost of products and services.
- Transparent product features, risks and charges, lead to increased competition in the sector.
- Firms meet Client Asset (CASS) requirements.

Issues

- **Investors with modest means may lack access to, or awareness of, advice** that could benefit them.
- **Financial advisers may give insufficient attention to the total cost of investment products and of advice**, which results in poor value for money for consumers.



We will conduct a market study to explore how 'direct to consumer' and intermediated investment platforms compete to win new, and retain existing, customers.



- **Some self-directed investors are at risk of receiving products inappropriate for their risk appetite** and capacity or receiving poor value for money.
- **Firms do not always consider consumers' needs and outcomes appropriately** when they develop products, distribution propositions, and offer wealth management services.
- **Consumers are vulnerable to unexpected financial losses**, including scams and fraud, from behavioural biases and difficulties assessing information.
- **Some peer-to-peer and crowdfunding firms may not be complying with CASS requirements**, putting consumers' funds at risk.
- Consumers might receive **unsuitable investment advice**.

Our key planned activities

Financial Advice Market Review (FAMR)

FAMR launched in August 2015, as collaboration between the Treasury and FCA, in light of concerns that the market for financial advice was not working well for consumers. The aim of the review was to explore ways in which the Government, industry and regulators could take collective steps to stimulate the development of a market that delivered affordable and accessible financial advice and guidance to everyone, at all stages of their lives. FAMR's final report in March 2016 set out a number of recommendations intended to tackle the barriers to consumers accessing advice.

In March 2017, in response to recommendations in the FAMR report, we published a consultation

on proposals for further guidance on streamlined advice, fact finds and sales that do not involve a personal recommendation. FAMR identified each of these as areas where FCA guidance might further the aims of the review.

We will publish our final guidance later in 2017. We will also continue to monitor the growth of automated advice. Depending on the speed with which this area grows, we may decide to test the suitability of advice given by firms providing this kind of advice.

Assessing suitability of advice and disclosure

We will complete our project to identify the areas where problems in providing suitable advice and disclosure are most common. This project examines advice given to different consumers, different products and by different types of firms to assess its suitability for consumers' needs.

The work will tell us where firms might be providing good or poor advice. These findings will shape our future focus. They will also establish a baseline for the level of suitable advice and disclosure provided in the investment advice market, against which we may be able to measure any future interventions.

Investment platforms market study

The interim report for the Asset Management Market Study identified a number of potential competition issues in the investment platforms market. These included: complex charging structures, if platforms' investment tools enable effective choice and whether platforms have the incentives and ability to put competitive pressure on asset management charges.

We will conduct a market study to explore how 'direct to consumer' and intermediated investment platforms compete to win new and retain existing customers. The study will explore whether platforms enable retail investors to access investment products that offer value for money. When scoping the study, we will take into account relevant feedback we receive on the Asset Management Market Study. The investment platform market study will allow us to understand the causes of any competition problems in this market and assess what we can do to improve competition between platforms and improve consumer outcomes.

Auto advice

We intend to assess the developing market of automated advice models in the investment advice sector. We will monitor developments and review models that are already providing automated advice, as well as new entrants to the market. This will help inform our regulatory strategy.

Contracts for Difference

We want to ensure that Contracts for Differences (CFDs) are sold and distributed to a suitable target market and that retail clients are provided a proportionate level of protection. Our December 2016 consultation paper proposes a package of policy measures to limit the risks of CFDs and improve the conduct of firms. We will publish a Policy Statement later this year.

We will also undertake conduct follow-up work to address the risks in the CFD sector that we identified in previous thematic work. This work will focus on the failings we identified in the Appropriateness Tests we conducted. It will also review how providers and distributors meet their responsibilities under the

Responsibilities of Providers and Distributors for the Fair Treatment of Customers in the process of selling these products to retail customers.

Unsuitable advice on complex products

We will carry out further work to target those firms providing unsuitable advice about complex products.

Client assets rules

We have seen examples of peer-to-peer (P2P) and crowdfunding firms that are not aware of, and do not comply with client money requirements. Standards within the sector vary widely and we will continue to use our resources to promote compliance and minimise risks to consumers' funds. Examples of the activities we may undertake include direct engagement with firms to review approaches to client money, review of client assets audits and engagement with a firm's auditors.

Scams and fraud

Consumers falling victim to scams and fraud remains a priority for us. We cover our work in this area in the cross-sector priority section of the Business Plan, in the 'Financial crime and anti-money laundering' chapter.



We will be focusing on completing the implementation of FAMR and MiFID and allowing the work to embed and take effect in the sector.





Ongoing activities

We perform a large range of ongoing activities in support of our objectives. A great deal of our resources are devoted to these core activities.

Authorisation – gateway to operate in the financial market

We regulate approximately 56,000 firms. Firms that carry out 'regulated activities' have to be authorised or registered by us, unless they are specifically exempt, and must meet our threshold conditions before we allow them to operate in the market. Where we believe firms' behaviour may pose a significant risk to consumers or the market we work with them to raise their standards. Failing that, we stop them entering or operating in the market.

Our authorisations work

Our authorisation process can vary in terms of the level of our scrutiny, depending on the risks a firm poses to our objectives. For those that present significant risks, we use a high degree of scrutiny in our review of their business models, governance, systems and controls, culture and management. This means we are confident that they have the right leadership and practices to deliver good customer outcomes. We use proportionately less scrutiny to authorise firms that pose smaller risks to our objectives.

While we have now completed the vast majority of the authorisation programme for consumer credit firms (which transferred from the OFT), we expect applications for

authorisation from new consumer credit firms will continue over the course of the next year and beyond. Our Authorisations function is now responsible for supporting the life-cycle of consumer credit firms for issues including the variation of permissions, waivers and cancellations.

We receive a variety of different authorisations applications of varying complexity and resource requirements. Changes to various regimes mean also that future inflow may well vary in composition from previous years. On the whole we expect total volumes to edge down somewhat but the complexity of inflow to increase. We also expect to receive once again over 300,000 firm and consumer contacts.

Our Delivering Effective Authorisations initiative aims to ensure that we: enhance support for firms and individuals to help them to meet and maintain the standards required to achieve our consumer protection and market integrity objectives; foster competition by fully adopting a service mind-set, ensuring the authorisations process is transparent, timely and consistent; and improve operational efficiency and effectiveness by making better use of data and digital technology.

Promoting competition

Promoting competition in both wholesale and retail markets in the interests of consumers is a statutory objective and a vital part of our overarching objective to make markets function well.

Competition is essential to healthy functioning markets. It helps drive better outcomes for consumers and is essential for UK growth and global competitiveness. By ensuring markets are open, innovative and appropriately regulated, we aim to ensure that there are resilient and dynamic markets for financial services in the UK, in which consumers can participate with confidence.

Our aim is to provide consumers with information and give them assurance that there are appropriate safeguards if things go wrong. This way they can make meaningful choices when they choose financial products and services. This, in turn, drives competition and value. We need to ensure our rules give consumers an appropriate degree of protection without being a barrier to firms entering the market and expanding in it, or distorting competition. At the same time we also want to ensure that firms operate in a fair and competitive way, do not abuse market power or engage in anti-competitive agreements, and that market features do not hinder or distort competition.

There are three main ways in which we pursue our competition objective:

- Using competition analysis such as market studies to see how competition in different sectors is working for consumers.
- Using competition law to take action against anti-competitive practices.
- Ensuring that all our activities reflect our objective to promote competition in the interest of consumers, and that our

regulation does not unduly restrict or distort competition.

Market studies

These look at how firms and consumers behave in a specific sector to assess whether competition is working well for consumers. Since we were given our competition objective, we have used market studies and Calls for Input to analyse how competition works in different sectors. To date, they have covered a wide range of issues including asset management, credit cards, cash savings, retirement income, investment banking, general insurance and mortgages.

Our market studies help us understand the dynamics of competition and develop solutions to support market conditions that result in them working better. We have already started to implement remedies in the cash savings, general insurance and retirement income sectors to help ensure competition works better for consumers. We are currently considering interventions in the credit card, asset management, investment banking and annuities markets.

Anti-competitive behaviour

We have a broad range of tools to tackle anti-competitive behaviour, including formal investigations. They also include other tools such as notifying firms of potential areas of concerns so they can apply due diligence and assess if they are fulfilling their obligations under competition law. Working alongside the UK and EU competition authorities, we are in a good position to detect competition law breaches and to step in to take action quickly. In 2016/17 we opened our first competition enforcement case. We will continue to undertake competition cases in the future where we find evidence of competition law breaches.

How regulation affects competition

We want to understand the impact our rules have on competition, and amend them where necessary. We also want to find ways to support new market entrants and innovation.

Our main activities in this regard are Project Innovate and the Sandbox (see page 41) – these are vital not only for helping individual firms but also for understanding how new entrants experience regulation, and amending our approach as needed. It also helps us understand how developments such as open data standards or blockchain technology could improve competition in the sectors we regulate, and what regulation is needed to ensure such developments operate in consumers' interests.

We also routinely ask stakeholders in market studies whether regulation acts as a barrier to competition or innovation in their sector, and take action to address this where possible.

Supervising firms

FCA supervisors work with firms to improve their effectiveness in identifying and mitigating risks to our objectives. Ensuring that firms understand and meet our standards and specific rules is also a priority.

Supervisors take a forward-looking approach, seeking to mitigate conduct risks before they become significant sources of customer detriment or market impact. The FCA is also the largest prudential regulator in Europe by numbers, employing a risk-based approach to assessing and supervising firms' financial soundness.

Supervision engagement with firms and key individuals within them takes the following four principal forms:

First, proactive supervision of firms to assess and provide feedback to firms on their mitigation of specific risks and a broad range of foundational factors. These include the suitability of their leadership teams, business models, governance, systems and controls, remuneration, incentives, tone from the top, risk management capabilities and quantitative analyses of their financial resources.

Second, investigation of crystallised risks to ensure firms take action to prevent recurrence and to provide the FCA with information to enable us to make decisions about enforcement action and consumer redress schemes as necessary.

Third, work to sample and assess industry practices and compliance and provide broad-based feedback to the sector in areas of high risk.

Fourth, formal determination of regulatory transactions, for example the authorisation of firms offering regulated activities.

We supervise approximately 56,000 firms on a broad array of topics. Our supervision strategy is designed to identify potential conduct or prudential issues before they become significant and to prioritise our engagement with specific firms based on analysis of the risks that they present to consumers, competition and market integrity. It draws on:

- the strategic Sector Views of risk trends
- intelligence gathered from a variety of sources including consumer and firm interactions with the contact centre, other parts of the FCA, the Financial Ombudsman Service, other regulators, and industry sources
- analysis of industry and firm data.

Supervision uses a consistent supervision model tailored to the risks presented by each firm:

- For each fixed-portfolio firm, we deploy a dedicated team of supervisors. The leader of the supervision team is accountable for all the relevant risks of the firm and is responsible for commissioning relevant specialists in sectors and functions as needed.
- For flexible-portfolio firms, we adapt our deployment of resources in response to the risks presented by the firms. Teams of supervisors are accountable for all the relevant risks of portfolios of similar firms. The teams use business model analysis and intelligence to identify emerging risks and high-risk outliers to prioritise proactive, reactive and sector-wide work.

Our supervision work

There are three aspects to our supervision:

- **Pillar 1** – Ongoing proactive supervision of the firms that present most risk to our objectives.
- **Pillar 2** – Event-driven, reactive supervision of actual or emerging risks.
- **Pillar 3** – Thematic work that focuses on risks and issues affecting a number of firms across the market.

Where necessary, we look closely at firms' business models to assess whether they are sound and robust. We focus on the most significant issues and seek to ensure that firms identify and tackle the root causes of problems.

We focus attention on the most significant drivers of behaviours, including senior management accountability and remuneration, and on firms improving their standards of conduct at all levels.



Where we believe firms' behaviour may pose a significant risk to consumers or the market, we work with them to raise their standards.



Helping smaller firms comply

Our 'Live & Local' programme continues in 2017/18, spending time in each of the UK's 12 regions, running roundtables, surgeries and sessions on culture and governance. The programme takes our expertise directly to firms, helping them comply with their obligations, discuss ways to improve governance and troubleshoot. We work in partnership with local firms and advisers, basing the programme on the key risks we have identified in these firms' sectors. We see around 500 delegates in each region, providing information and feeding back 'on the ground' issues to different parts of the FCA. In 2017/18 our senior management and senior industry figures will continue to attend and support the programme, giving smaller firms the opportunity to have discussions with them.

We produce the monthly 'Regulation round-up' e-bulletin to keep all firms up to date with the latest FCA policy and regulatory developments.



We set the standards by which financial services firms operate. However, it is for firms' boards to ensure they meet them; we cannot be a substitute for firms' governance. The SM&CR supports firms' development of a culture of responsibility to identify the harm developing from their behaviour and take steps to address the risk. We need to be confident that, if problems do occur, firms will do the right thing for their customers and markets.

When we find poor practice we use our supervisory and enforcement tools to mitigate risks, deter others and get redress for consumers where necessary.

Our supervisory and enforcement framework includes finding ways to reduce the volume of financial crime and money laundering, while ensuring that regulation is proportionate and effective.

We also place great emphasis on preventing and tackling scams and on ensuring that firms' systems are resilient against cyber-attacks.

We also undertake ongoing systematic supervision of firms for prudential, CASS (Client Assets) and financial crime purposes. Some flexible-portfolio firms will be part of these systematic programmes.

We have also launched a programme to deliver improvements to our supervision model and make us more efficient and effective. The programme will enable us to improve risk identification and delivery of risk management plans for firms and sectors, and more efficiently deploy our resources.

Our prudential responsibilities

The PRA is the prudential regulator of the most systemically important financial firms – around 1,700 deposit takers, insurers and

investment firms. We are responsible for the prudential regulation of all authorised firms not prudentially regulated by the PRA; around 18,000 firms⁴⁴ that include asset managers, investment firms, platforms and infrastructure providers.

As with our supervision of conduct, our prudential supervision goes beyond a quantitative analysis of firms' financial resources. We consider firms' systems and controls, governance arrangements and risk management capabilities and how these link to the firm's conduct.

The aim of our prudential approach is to minimise harm to consumers, wholesale market participants and market stability when firms experience financial stress or fail. Our starting principle is that firms of all sizes should be allowed to fail, but in an orderly way.

⁴⁴ The PRA is the prudential regulator of banks, building societies, credit unions, insurers and designated investment firms, and is part of the Bank of England. We have a defined prudential regime for c. 18,000 firms. This figure does not include the larger population of consumer credit firms that are subject to high-level prudential resource requirements, EEA Service Companies that we only regulate for conduct issues, and Small Payment Institutes, which are not subject to capital requirements.

For the, usually smaller, firms that pose less risk to our objectives, we take a more reactive approach.

These prudential responsibilities help ensure we meet our statutory objective to protect and enhance the integrity of the UK's financial system. Given the direct links between conduct and prudential risk, our prudential approach also helps ensure relevant protection for consumers.

Enforcement

Our Enforcement division supports our objectives by making it clear there are real and meaningful consequences for firms and individuals who don't follow the rules.

Our approach to using our powers focuses on deterrence. Both specific deterrence (deterring the person from offending again) and general deterrence (deterring others from offending) are important aims of enforcement. However, we also have other necessary aims. FCA investigations help engender public confidence in the financial system and markets that wrongdoing is properly identified and dealt with, and our public sanctions underline the value and legitimacy of the rule, requirement or standard our investigation is upholding. In this way, investigations draw clear bright lines that the rest of the market can follow, helping everyone comply, and ensuring our markets work well.

Our Enforcement division works closely with our Authorisation, Supervision, and Strategy and Competition divisions, as well as other regulators and law enforcement, both domestically and internationally. This means we can identify and act early when enforcement action is necessary.

We use a wide range of enforcement powers – criminal, civil and regulatory – to protect consumers and markets and to take action against firms and individuals that do not meet our standards.

We can take action such as:

- withdrawing a firm's authorisation
- prohibiting individuals from operating in financial services or from undertaking specific activities
- suspending firms and individuals from undertaking activities
- censuring firms and individuals through public statements
- issuing fines against firms and individuals who breach our rules or commit market abuse, and against firms breaching competition laws
- applying to the courts for injunctions and restitution orders
- bringing criminal prosecutions to tackle crimes such as insider dealing and firms undertaking regulated activities without authorisation

Developing policy

We use our policy-making powers to promote and deliver robust, practical rules and frameworks that support our objectives. This applies both to policy that we initiate and to our work with external policy developments and legislation. When developing policy, we clearly set out what we expect from regulated individuals and other market participants with the aim of changing behaviour in financial markets. We consult widely and publicly with the industry, consumers and other relevant groups on our rules and guidance before we finalise them. We use evidence and analysis to assess the costs and benefits of both our, and others', proposals to ensure they support our statutory objectives, general duties and regulatory principles. We also consider the impact and implications of rule changes on the wide range of different organisations and activities we regulate. As part of the broader rollout of the Enterprise Act, we conduct impact assessments to understand the cost and impact on industry on a wide range of our interventions.

We play a key role in influencing and then implementing domestic and European legislation and international policy. Many of the rules and standards that we apply continue to come from European and international work, and we are planning for the impact of the UK's future exit from the European Union. Through active engagement with a wide range of European and global bodies, we help to shape policy debates, share our regulatory experience and perspective, review how agreed standards are implemented and help identify and mitigate new and emerging issues.



Promoting competition in both the wholesale and retail markets in the interests of consumers is a statutory objective and a vital part of our overarching objective to make markets function well.





While our work directly protects millions of UK consumers, consumers also need to know how they can help and protect themselves.



Our policy principles

Our policy work is guided by the following principles:

- prioritising and targeting our policy activities where they can make the most difference
- only making or supporting new rules and guidance if we believe this will be an effective and proportionate solution to the relevant problem
- reviewing rules, and encouraging others to do the same, where we believe they no longer achieve the right aims
- aligning our initiatives and strategy with the European and international agendas and timetables

Our general approach to implementing EU legislation is usually to intelligently adopt word for word transposition⁴⁵ of agreed requirements into our Handbook, and only to go beyond what is required if we consider this is proportionate. When we do this, it is usually to maintain exist in standards of consumer protection or to minimise possible competitive distortions, and we always undertake public consultation and cost-benefit analyses. Our policy work will be affected by the UK's departure from the EU. We have a dedicated team planning for that impact and to ensure that we modify our approach to EU legislation once the broader approach to EU legislation within the UK is clearer.

In the Mission we have committed to being clearer with firms about the decisions that we take and the expectations that they have of us. We have said we will review our Handbook to ensure it remains fit for purpose and that our rules are clear. The first step of this review will be to ensure that any changes needed for the UK leaving the European Union are made.

After this, we will seek further input on areas of the Handbook that would benefit from clarification.

Understanding consumers

Our understanding of consumers' needs, experiences and behaviour when dealing with financial services is a major help when we decide how to identify risks, prioritise our actions and design our interventions.

To help build our insight into consumers we use a variety of tools, including:

- A segmentation model called Consumer Spotlight: It recognises that not all consumers are exposed to all our identified risks. Nor are all consumers equally affected by any particular risk. Consumer Spotlight gives us better understanding of which consumers are most at risk from specific products, services or practices.
- Financial Lives (formerly Consumer Insight) Annual Survey: We run extensive consumer surveys every year with all types of consumers and across retail financial markets to give us insight into changes and trends in the way that firms and consumers interact.
- Market research: As well as the Annual Survey programme, we also carry out one-off qualitative and quantitative market research to support our frontline work, particularly in policy, supervision and competition. We use insights from behavioural economics, together with more traditional analysis of competition and market failures, to help us better assess problems in financial markets, choose more appropriate remedies and deliver more effective regulation.

45 Also referred to as 'copy-out'

- **Consumer Network:** We operate a wide network with organisations, including charities that represent the needs of particular consumer groups. This network provides a rich source of information about the needs, experiences and behaviours of consumers across the markets.
- **Experimental and analytical research:** Where appropriate, we test consumer-focused interventions experimentally. We also analyse consumer behaviour using rigorous statistical methods. This helps us develop sound evidence on what works and what doesn't to support our policymaking.
- **Publications:** We publish papers on consumer issues, such as our Occasional Paper on Vulnerability. These papers show thought leadership and many also provide practical help and resources for firms and others. The Vulnerability paper, for instance, gave examples of good practice and suggestions on how firms can develop and implement a vulnerability strategy.

Raising consumer awareness

While our work directly protects millions of UK consumers, consumers also need to know how they can help and protect themselves. They need the information to ensure they do not fall victim to scams, check if a company is legitimate, understand their rights, know how to complain and who to complain to.

We have an ongoing programme of work with firms to support greater transparency and better disclosure of information to consumers across many different sectors. We also work closely with consumer groups to raise consumer awareness. We give consumers this information via our website, contact centre and communications campaigns. Since 2014, we have run our ScamSmart campaign, partly funded by funds recovered from the proceeds of crime to proactively give consumers the information they need to spot

and avoid a scam. So far, over 450,000 consumers have visited our ScamSmart webpages and more than 45,000 checked an investment on our Warning List.

Financial stability – working with the Financial Policy Committee

The Financial Policy Committee (FPC) is the UK's main body for analysing financial stability and is the main lens through which we view systemic risk. As part of our role to protect and enhance the integrity of the UK financial system, we closely monitor financial stability risks, including the soundness, stability, and resilience of financial markets. Our Chief Executive is a member of the FPC and we work closely with the Bank of England on areas of interest to the FPC such as market liquidity and housing issues.

Shaping thinking on financial services

We are a significant and influential voice among international regulatory bodies, working to ensure effective cross-border cooperation and consistency. Many countries see our initiatives as industry-leading, both in terms of developing new approaches to financial regulation such as Project Innovate, and our Consumer Spotlight work, and in the way we work with our stakeholders to shape policy and implement regulation. We have already signed cooperation agreements to foster collaboration in promoting financial innovation with a number of other authorities, including the Australian Securities and Investments Commission, the Financial Services Commission of the Republic of Korea, the Monetary Authority of Singapore, The People's Bank of China, the Hong Kong Monetary Authority and the Ontario Securities Commission. We will build and expand our relationships with regulators in other jurisdictions in 2017/18.

We work closely with firms and other stakeholders on changes to policy, amending rules and implementing new legislation. We use Consultation, Discussion and Occasional papers to get stakeholders' views and find out more about their experiences to help us deliver change in the most efficient and effective way possible.

450,000
consumers have
visited our
ScamSmart
webpages.



How we operate

This section provides details on our operational activities, including our finances.

Our budget

Our annual budget reflects the cost of the resources we need to carry out our work in 2017/18.

The key elements of our budget are:

- The cost of our core operating activities (our Ongoing Regulatory Activity or ORA), the largest element of which is our people.
- The total amount we charge the industry to fund our plans (our Annual Funding Requirement).
- Capital expenditure for developing of our information systems and new regulatory and operational requirements.

Table 2: Operating costs

Operating costs (ORA)	2016/17 £m	2017/18 £m
Staff costs	316.8	324.2
IS costs	93.4	86.5
Depreciation	39.3	39.5
Accommodation and office services	31.5	32.2
Enforcement case costs	8.3	8.6
Professional fees	16.2	40.6
Training, recruitment, travel	12.7	14.0
Printing and publications and other	9.8	10.1
Sundry income	(25.2)	(47.7)
Total ORA	502.9	508.0

Note: 2016/17 restated to reallocate project contingencies from IS costs to printing, publications and other consistency in prior year comparators.

Table 3: Annual Funding Requirement (AFR)

Annual Funding Requirement (AFR)	2016/17 £m	2017/18 £m	Movement	
			£m	%
ORA budget	502.9	508.0	5.1	1.0%
Recovery of scope change activities	16.4	16.4	0.0	-
EU withdrawal	0.0	2.5	2.5	
Total AFR	519.3	526.9	7.6	1.5%
Financial penalty rebate	(48.7)	(51.6)	(2.9)	6.0%
Fees payable	470.6	475.3	4.7	1.0%

Annual Funding Requirement (AFR)

Our AFR for 2017/18 is £526.9m, an increase of 1.5% driven by the £5.1m (1.0%) increase in our ORA budget and £2.5m for EU withdrawal. Our AFR includes our ORA budget costs, the costs we need to recover for changes in scope to the FCA's regulated activities (including new responsibilities) and EU withdrawal.

In 2017/18 we will recover scope change costs for the Senior Managers and Certification Regime, MiFID II and Consumer Credit. Consumer Credit firms were not billed for the full costs of regulation during the setup and transition period, and the outstanding deficit will continue to be recovered over ten years at £6.2m per annum.

We will also recover incremental costs in 2017/18 for EU withdrawal outside of our ORA budget comprising our EU planning & coordination hub and general counsel activity. As we gain more certainty over the process we will review the need to recover these incremental costs in future years.

Capital expenditure

Our capital expenditure budget reflects the ongoing delivery of IT systems and infrastructure development and refresh as well as implementing the necessary IT change driven by legislation such as the Markets in Financial Instruments Directive II (MiFID II).

In 2018/19 our leases for our Canary Wharf properties come to an end and the FCA has signed an Agreement for Lease for 20 years to move to Stratford. We will incur fit-out costs to get the building ready for occupation. The current intention is that they will be funded by external financing, the costs of which will be recovered against the rent free period.

Table 4: Capital expenditure

Capital expenditure	2016/17 £m	2017/18 £m
IT systems development & infrastructure	39.4	41.6
Property, plant and equipment	1.0	1.0
Total capital excluding TIQ	40.4	42.6
Stratford property	25.0	60.0
Total capital	65.4	102.6

Applying financial penalties

We must pay to the Treasury all financial penalties that we receive, less certain enforcement costs.

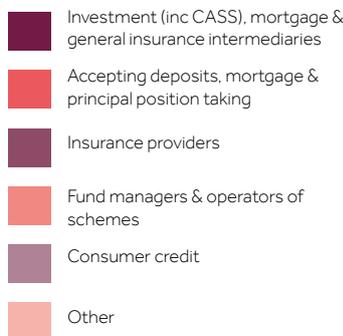
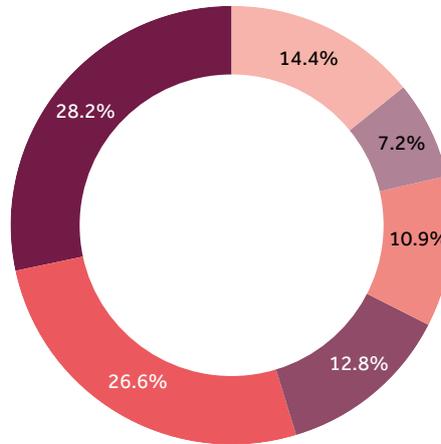
These retained penalties are used to reduce our fees for firms, apart from the fees of the penalty payer themselves. We estimate the financial penalty rebate to be £51.6m in 2017/18.

Impact on our fee payers

Every year we consult with our fee payers on the fee rates to recover our Annual Funding Requirement (AFR) for the forthcoming financial year. We do this via our fees rates consultation paper published in April 2017.

Our consultation paper explains how the movement in our AFR has been allocated across fee blocks, as well as any changes being made to the fee blocks. Among other things, it also explains any proposed change to the minimum fees and provides details of the financial penalty scheme and our estimated financial penalty rebates for 2017/18. The chart on this page reflects how we will be funded by industry sector as represented by groupings of fee blocks, as proposed in our April 2017 consultation paper.

Fees allocation percentage by industry sector



Transition to Stratford

We are moving our offices to the Queen Elizabeth Olympic Park in Stratford in 2018. We plan to take possession of our new building on 1 April 2018 and move from our Canary Wharf Offices between May and August 2018. Our new office will accommodate all FCA London employees.

The FCA will incur c. £90m of Capital Expenditure, primarily for FCA specific construction, fit-out and furniture costs. This will predominantly be funded through the rent free period negotiated as part of the new lease agreement. The current intention is that costs for the move and dual running expenses over the move period will be funded through ORA reserves.

The new building will incur a significantly lower rent than we could get if we remained in Canary Wharf, given the end of the current 20-year lease. It will also provide efficiencies, particularly in energy use and maintenance.

We will have a strong focus on preparatory work in 2017/18 to ensure that the move has little or no impact on our regulatory work.

We have a strategy to support our staff and stakeholders during this transition, to ensure that we continue to attract and retain talented employees, and that all our stakeholders find it as easy to contact and meet us as before.

In the long term, we have forecast that we will make significant cost-savings due to lower running costs.

Payment Systems regulator

The Payment Systems Regulator (PSR) is a separate legal entity based at the FCA, with its own board and statutory objectives. Details of its funding can be found in the PSR's Annual Plan.

Value for money

Our overarching Value for Money (VFM) strategy is to maximise the impact of delivering our statutory objectives and desired outcomes, while minimising costs. Our drive to deliver year-on-year improvements in effectiveness, efficiency and economy is an ongoing project.

VFM criteria are being embedded in our decision-making process at all levels. This, together with reviews of our internal processes, benchmarking, and ensuring flexibility in our workforce, will drive further efficiencies.

We strengthened our focus on embedding VFM into our culture through a number of measures, including a training and communications programme, and we work closely with other regulators to share expertise, best practice and resources where possible.

We will continue to develop a constructive relationship with the National Audit Office (NAO) to address recommendations coming from its reviews of the FCA. As the NAO observes, our strategic approach is evolving and we will be using the NAO's recommendations to build on our current VFM strategy.

Our people

Our work and decisions affect the lives of millions of people who rely on UK markets every day. It is vital that our people reflect the society we serve so that we can bring diverse attitudes and opinions to our judgments and decision making. We are building a diverse and inclusive place to work because it is right, because we want our people to be confident they can be themselves at work and because this diversity makes us a more effective regulator.

We know we still have more work to do to achieve this. To firmly demonstrate our commitment to diversity and inclusion, we have set a target for 45% of our senior leadership team to identify as female by 2020, and 50% by 2025. We have also set a target for 8% of our senior leadership to identify as Black or Minority Ethnic (BAME) by 2020, and 13% by 2025.

As well as building a diverse workforce with a broad range of skills, we also want to develop our people to their fullest potential and keep our best talent.

In addition to a rolling programme of events to keep staff informed of economic and market

developments, we will start the fourth cohort of our MSc in Financial Regulation with Henley Business School. We will continue with our successful secondment programme with a wider range of regulated firms and consumer organisations. We will also strengthen our management framework through the Future and Advanced Management Programmes, investing in our future leadership and helping balance our people's technical expertise with the best people and operational management skills.

Reporting on our achievements

The main way in which we report on our performance is through our Annual Report. To make our work more transparent throughout the year we also publish a quarterly data bulletin, which provides information about what we do and the markets we regulate.

In the Annual Report we report on a range of performance factors prescribed by FSMA, and self-imposed ones, such as the delivery of our Business Plan commitments, outcome measurement, operational effectiveness and efficiency, value for money and the key work we have delivered. For 2016/17 we will be reporting on indicative success measures on our priority themes for the first time. Our intention is to build on this framework over 2017/18 and ensure that we have credible ways to measure our influence and the impact of our intervention on the various sectors in financial services.

We include several measures that analyse the efficiency and effectiveness of our work. Measures for our authorisations function include, for example, how we determine applications within the statutory service standards, the average time it takes us to make a decision on different types of cases, feedback from stakeholders on our process and quality assurance results. Examples from other areas

include the redress we obtain for consumers, how we use our enforcement powers, the outcomes of our enforcement activity, the number of financial penalties we have levied, the number of fines and prohibitions and the impact of specific interventions.

We also use an outcomes-based performance framework, which examines the external markets we regulate and assesses the impact of our work on our statutory objectives in different financial sectors.

Achieving our outcomes is an ongoing task. We will continue to monitor them to assess whether progress is being made, and where we need to take further action.

Analysing our performance against our statutory objectives

We set out our framework for analysing our performance against our statutory objectives. We have a pragmatic approach to measuring how we perform against our statutory objectives and take into account the way we use our resources. This means we use all available research and analysis, rather than solely relying on designing large research programmes ourselves.

Measuring outcomes is challenging and regulatory success is hard to judge, especially as our success is often achieved by preventing problems from happening or worsening, which may not be as visible. Some of the difficulties we encounter include establishing cause/effect relationships, time lags between our actions and their impact and our limited control over issues that are heavily affected by external factors and the actions of others. These include market conditions, the general economic state, the work of other regulators and the political agenda.



Our overall framework, its outcomes, indicators and performance measures will evolve over time as we develop our performance framework further and identify better measures.

Working in partnership

We are an integral part of the UK's wider financial regulation framework. This involves a number of public bodies, each with their own duties and objectives. They include the Bank of England, the Payment Systems Regulator (PSR), the CMA, the Money Advice Service, the Pensions Regulator, the Financial Ombudsman Service, the Financial Services Compensation Scheme and the Treasury. We work closely with these public bodies and others to advance our objectives.

We have a statutory Memorandum of Understanding with the PRA that sets out the responsibilities for each regulator. We regularly

monitor performance against this, and coordinate and cooperate with the PRA across all relevant activities, which we actively and jointly oversee.

As a member of both the UK Regulators Network and the UK Competition Network we engage with broader regulatory issues and priorities.

During 2017/18 we will continue to work with the Money Advice Service, the Treasury and the Department for Work and Pensions to ensure that there is a smooth transition to the new Single Financial Guidance Body. The SFGB will bring together pensions, money guidance and debt advice in one place, delivering and commissioning specific services to ensure that as many consumers as possible receive high-quality, impartial financial guidance. We also work with the Serious Fraud Office, the National Crime Agency, the City of London Police and other enforcement agencies to take action against firms and individuals who may have committed financial crime.

We also work closely with the PSR, the independent economic regulator for the £75 trillion payment systems industry. The PSR is a subsidiary of the FCA, which was incorporated in April 2014 and became fully operational in April 2015.

Many new rules we make come from the need to implement European policy. The European Supervisory Authorities (ESAs) have significant powers to propose draft rules and make decisions that have major implications for national supervisors and firms.

45%

women,
8% black or
minority ethnic.

Our aim for our
leadership team
by **2020.**

Over 2017/18, we anticipate that the shape of this work will change as the detail of the UK departure from the EU becomes clearer. We have a dedicated team planning for that impact but our day-to-day activities are currently largely unchanged.

We work closely with other European regulators and the ESAs, in particular the European Securities and Markets Authority (ESMA), and are influential in ensuring that we:

- assist in and influence policy making
- are properly informed about relevant risk
- avoid duplication of regulatory activities

FCA statutory panels

We are required to consult on the impact of our work with four statutory panels. These panels represent the interests of consumers, practitioners, smaller regulated firms and markets. We also consult with the Listing Authority Advisory Panel.

These panels play an important role in both advising and challenging us, and bring a depth of experience, support and expertise in identifying risks to the market and consumers. We consider their views when developing our policies and when deciding and implementing other regulatory interventions. Each panel publishes its own annual report. The Panels are:

The Consumer Panel

This represents the interests of consumers, monitors how far we are fulfilling our statutory objectives to consumers when developing rules or policy and provides us with advice and challenge.

The Practitioner Panel

The panel represents the interests of practitioners. It provides us with external input from the industry as a whole.

The Smaller Business Practitioner Panel

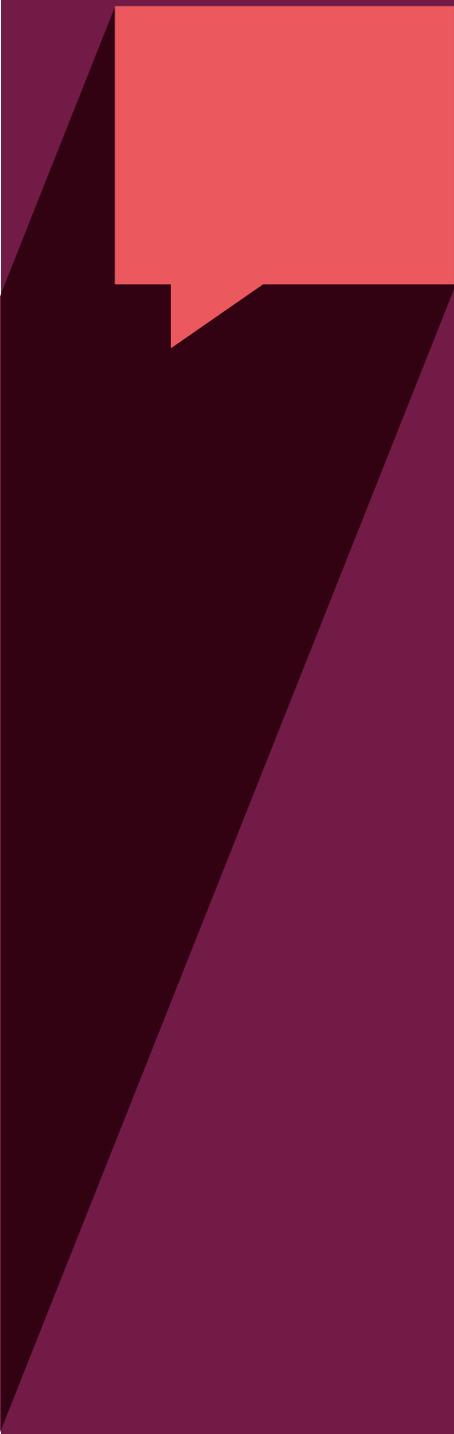
This represents smaller regulated firms, who may otherwise not have a strong voice in policy making.

The Markets Practitioner Panel

This panel reflects the interests of practitioners who are likely to be affected by our functions involving markets.

The Listing Authority Advisory Panel

This non-statutory panel advises the FCA on policy issues that affect issuers of securities, and on policy regulation proposals from the FCA listings function.



As well as building a diverse workforce with a broad range of skills, we also want to develop our people to their fullest potential and keep our best talent.

Annex 1

Update on ongoing market-based activity

The table below lists a number of thematic reviews, market studies and other reviews, with indicative timings for delivery. Some of the work has not been completely scoped and therefore the delivery date is not known.

The list is not exhaustive and we will undertake additional market-based work throughout the year in line with the priorities identified in our Business Plan and as necessary to address emerging issues that arise in the year.

Pensions and retirement income	Project type	Timing (complete by)
The Joint Review of Industry Progress Against the Independent Project Board (IPB) recommendations	Thematic Review	Q3 2017/18
Retirement outcomes review	Review	Q1 2018/19
Fair treatment of with-profits customers	Thematic Review	Q3 2018/19
Non-advised drawdown sales	Thematic Review	Q4 2017/18
Non-workplace pensions market	Review	2018/19

Retail banking	Project type	Timing (complete by)
Retail Banking Strategic Review	Review	2018/19
PCBS – Customer Understanding of Transactions	Thematic Review	Q2 2017/18

Financial crime	Project type	Timing (complete by)
Financial Crime review of e-money	Thematic Review	Q1 2018/19

General insurance and protection	Project type	Timing (complete by)
Pricing Practices	Review	Q1 2018/19
Wholesale insurance market study	Market study	2018/19
Value in the distribution chain	Review	Q1 2018/19

Retail investments	Project type	Timing (complete by)
Assessing suitability of advice follow-up	Review	Q2 2018/19
Investment platforms market study	Market study	2018/19
Follow-up work on Contracts for Difference	Review	Q1 2017/18
Unsuitable advice on complex products	Review	Q4 2017/18
Outcomes testing on auto-advice	Review	Q2 2018/19
Wealth management suitability – follow-up	Review	Q3 2017/18

Investment management	Project type	Timing (complete by)
Asset Management market study	Market study	Q2 17/18

Mortgages and mutuals	Project type	Timing (complete by)
Maturing interest-only mortgages	Thematic Review	Q4 2017/18
Forbearance for long-term mortgages arrears	Thematic Review	Q4 2018/19
Mortgages market study	Market study	Q4 17/18

Consumer credit	Project type	Timing (complete by)
High-cost credit Call for Input	Call for inputs	Q4 2017/2018
Debt management sector review	Thematic Review	Q4 2018/19
Motor finance	Review	2018/19
Point of Sale	Thematic Review	Q4 2018/19

Annex 2

EU initiatives

Anti-Money Laundering Directive IV (4MLD)

Audit Regulation and Directive

Securities Financing Transactions Regulation

EU Benchmarks Regulation

Markets in Financial Instruments Directive II and Regulation (MiFID II/MiFIR)

Payment Services Directive II (PSD II)

Insurance Distribution Directive (IDD)

Revised Data Protection Regulation

Regulation on Money Market Funds (MMF)

Securitisation Regulation (CMU package)

Packaged Retail Investment and Insurance Products Regulation (PRIIPS)

Revised Shareholders' Rights Directive

Prospectus Regulation (CMU package)

European Market Infrastructure Regulation (EMIR) Review

Recovery and Resolution of Central Counterparties

Pan-European Venture Capital Funds Proposal (CMU package)

Consumer Credit Directive Review (tbc)

Common Consolidated Corporate Tax Base Proposal (CMU package)

Capital Requirements Directive IV/Regulation (CRD IV/CRR) Review

Business Restructuring and Second Chance (Insolvency Proposals – CMU package)

Bank Structural Reform Regulation

Retail Financial Services Action Plan (CMU package)

Pan-European Personal Pensions (PEPP) framework

Pan-European Framework for Covered Bonds (CMU Package) (tbc)

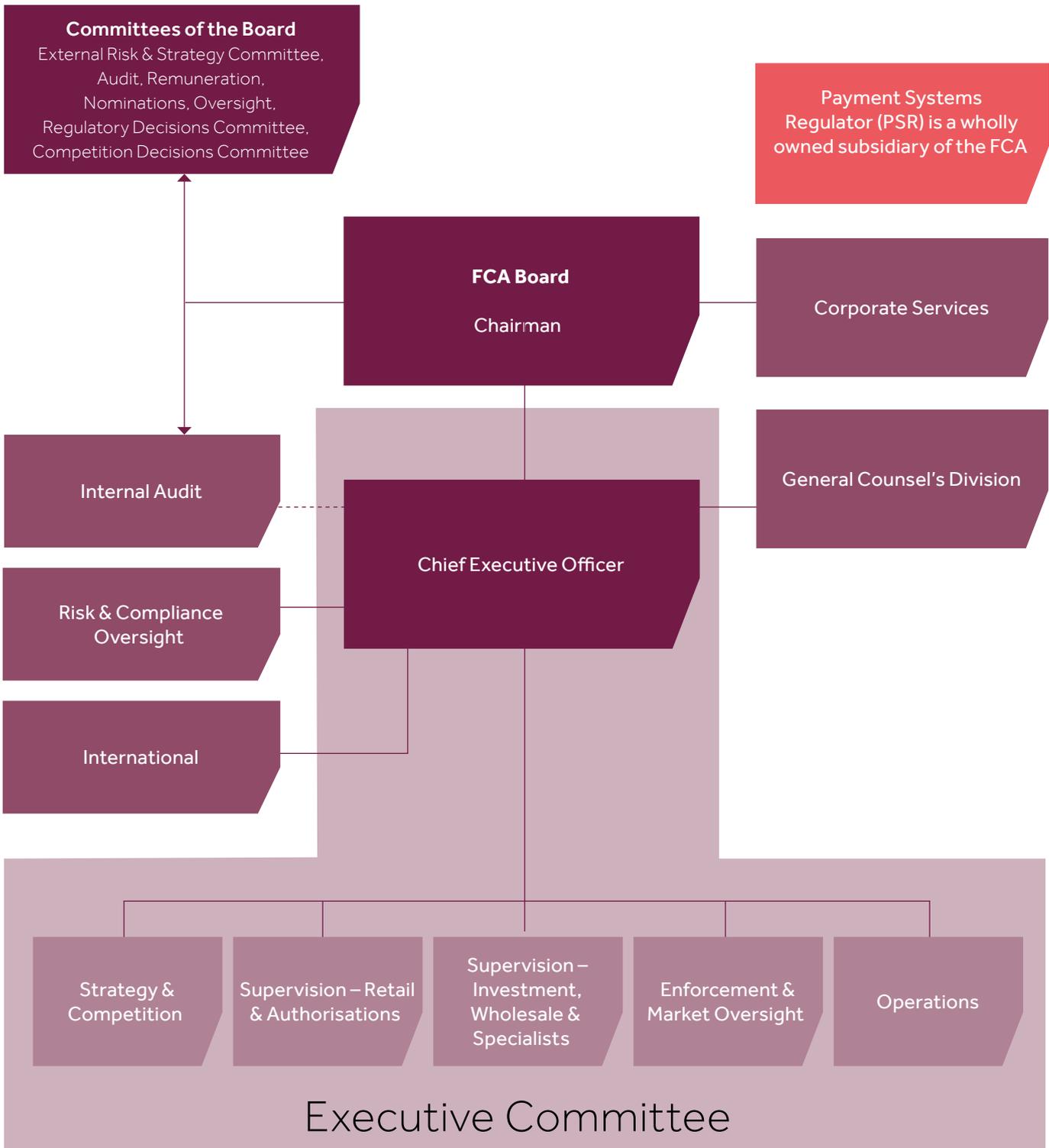
Capital Markets Union Package (CMU)

 Consultation/drafting  Negotiation  Transposition



Annex 3

FCA organisational chart





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