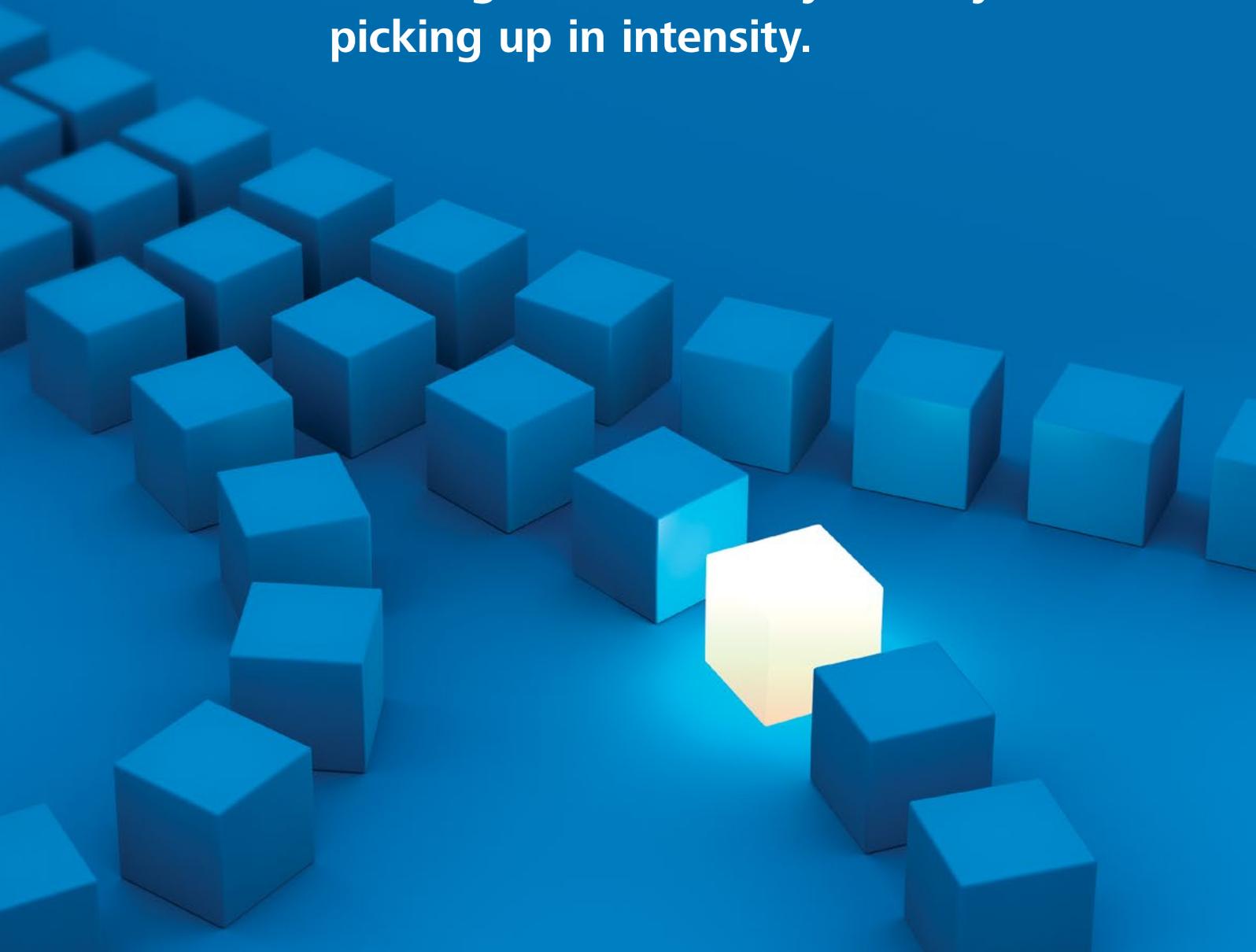




Trends in Regulatory Enforcement in UK Financial Markets 2016/17 Mid-Year Report

By **Robert Patton** and **Erin McHugh**

FCA fine activity in the first half of the 2016/17 financial year was low as compared to recent levels. This may be a transitory lull as the FCA redirects its resources from large-scale investigations that have recently concluded. Indeed, based upon fine activity in October, fines against firms may already be picking up in intensity.



Trends in Regulatory Enforcement in UK Financial Markets 2016/17 Mid-Year Report

Robert Patton and Erin McHugh¹

December 2016

NERA Economic Consulting maintains a proprietary database of fines and other enforcement activity by the Financial Conduct Authority (FCA) and, previously, the Financial Services Authority (FSA). This includes data on fines from 1 April 2002.² We undertake a detailed analysis of recent enforcement activity and how it conforms to stated priorities, revealing underlying trends that may not be apparent from a review of individual cases.

Introduction

Both the number and monetary value of FCA fines slowed to a trickle in the first half of the 2016/17 financial year (ended 30 September 2016), with the regulator imposing less than £7 million in fines—a small fraction of the more than £1 billion imposed as recently as the second half of 2014/15. This lower level of fines might be seen as consistent with earlier suggestions that the Authority would now take a “softer approach” than it has over the past several years.³ On the other hand, the first half of 2016/17 may simply reflect a transient lull in fines as the FCA redirects resources and attention from several large-scale investigations that have recently concluded.

A decline in FCA fine activity was already apparent in the second half of the 2015/16 financial year, as we described in our last report.⁴ In that period, the total amount of fines imposed fell to less than £100 million, from £794.3 million in the first half of 2015/16. Moreover, the number of fines imposed both on firms and on individuals in 2015/16 was lower than in any of the prior four financial years (see Table 1 on the next page).

This steep decline continued during the first half of 2016/17, with the FCA imposing only 12 fines totalling £6.3 million. The number and amount of FCA fines over any semi-annual period has not been this low since the second half of the 2007/08 financial year.⁵

Table 1. **Annual FCA Fines**
2011/12–2015/16, and First Half 2016/17

	2011/12	2012/13	2013/14	2014/15	2015/16	H1 2016/17 ²
Number of Fines¹						
Individuals	40	20	22	24	15	9
Firms	23	26	27	27	17	3
Totals	63	46	49	51	32	12
Aggregate Fines (£ millions)¹						
Individuals	19.9	5.1	3.9	7.1	16.2	0.7
Firms	58.9	422.2	416.9	1,403.1	874.0	5.5
Totals	78.8	427.3	420.8	1,410.3	890.2	6.3

Notes and Sources:

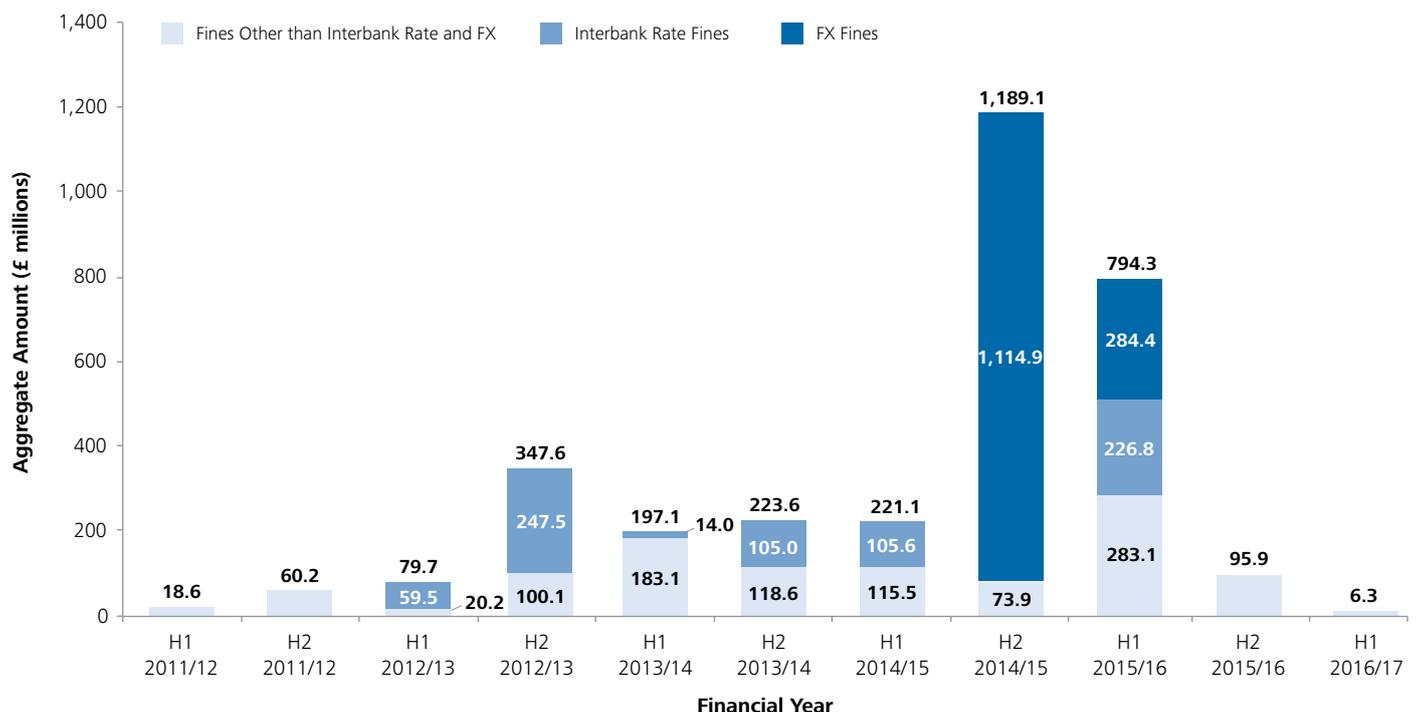
Numbers may not sum precisely to totals due to rounding.

¹ The annual number and aggregate amount of fines shown here may differ from statistics reported by the FCA in its annual reports (for example, the FCA's reported 2014/15 totals for number of fines and aggregate fine amount were 43 and £1,409.8 million, respectively). This is for three reasons. First, beginning with its 2009/10 Annual Report, the FCA assigns each fine to a financial year based on the publication date of the press release announcing the fine, whereas NERA uses the date of the final notice. Second, the FCA does not include in its count of fines those reduced to zero owing to financial hardship, whereas NERA does. Finally, NERA treats fines on sole proprietorships (ie businesses consisting of a single individual) as having been imposed on individuals, whereas the FCA classifies these as fines on firms.

² Figures cover the first half of the 2016/17 financial year, from 1 April 2016 to 30 September 2016.

Even excluding the arguably extraordinary fines in relation to manipulation of interbank rates (eg LIBOR⁶) and foreign exchange (FX) markets over the last four financial years, aggregate fines in the first half of 2016/17 were exceptionally low compared to those in prior semi-annual periods (see Figure 1).

Figure 1. **Semi-Annual Aggregate FCA Fine Amounts against Both Firms and Individuals**

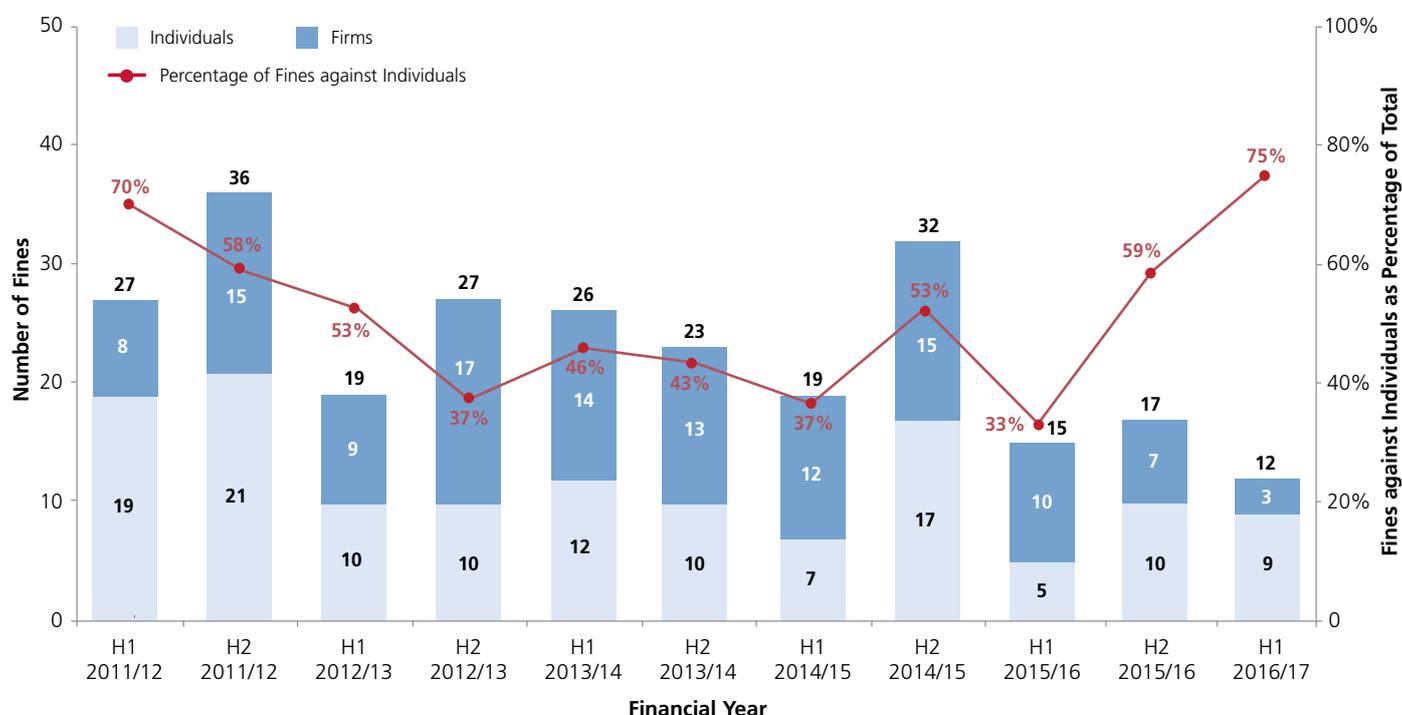


Notes and Sources:

Numbers may not sum precisely to totals due to rounding.

Of the 12 fines imposed in the first half of the 2016/17 financial year, three-quarters (9 of 12) were against individuals, a higher proportion than in any semi-annual period during the prior five financial years (though, as discussed below, this is in part due to the low number of fines imposed on firms) (see Figure 2).

Figure 2. **Semi-Annual Number and Percentage of Fines against Individuals**



Notes and Sources:
 NERA classifies fines on sole proprietorships as fines on individuals.
 NERA includes in its tallies fines that were reduced to zero owing to financial hardship.

In the sections that follow, we discuss recent trends in enforcement against firms and individuals separately, considering non-pecuniary sanctions as well as fine activity.

Enforcement against Firms

The era of large FCA fines against firms for manipulation of interbank rates and FX markets now appears to be in the past. The last such fines imposed by the Authority were in April 2015 and May 2015, relating to manipulation of interbank rates and FX markets, respectively.⁷

During the first half of 2016/17, the FCA issued fines against just three firms, totalling £5.5 million. This is the lowest level of total fines against firms in any semi-annual period since the second half of 2007/08, well before the FCA was established on 1 April 2013. On an annualised basis, this level of fines (£11.0 million per year) is lower than the annual average of aggregate fines during the financial years 2002/03 to 2007/08—ie the so-called “light touch” era.⁸ However, as detailed below, fines in October 2016 alone exceeded the total for the first half of the 2016/17 financial year (ie the six months ending 30 September 2016).

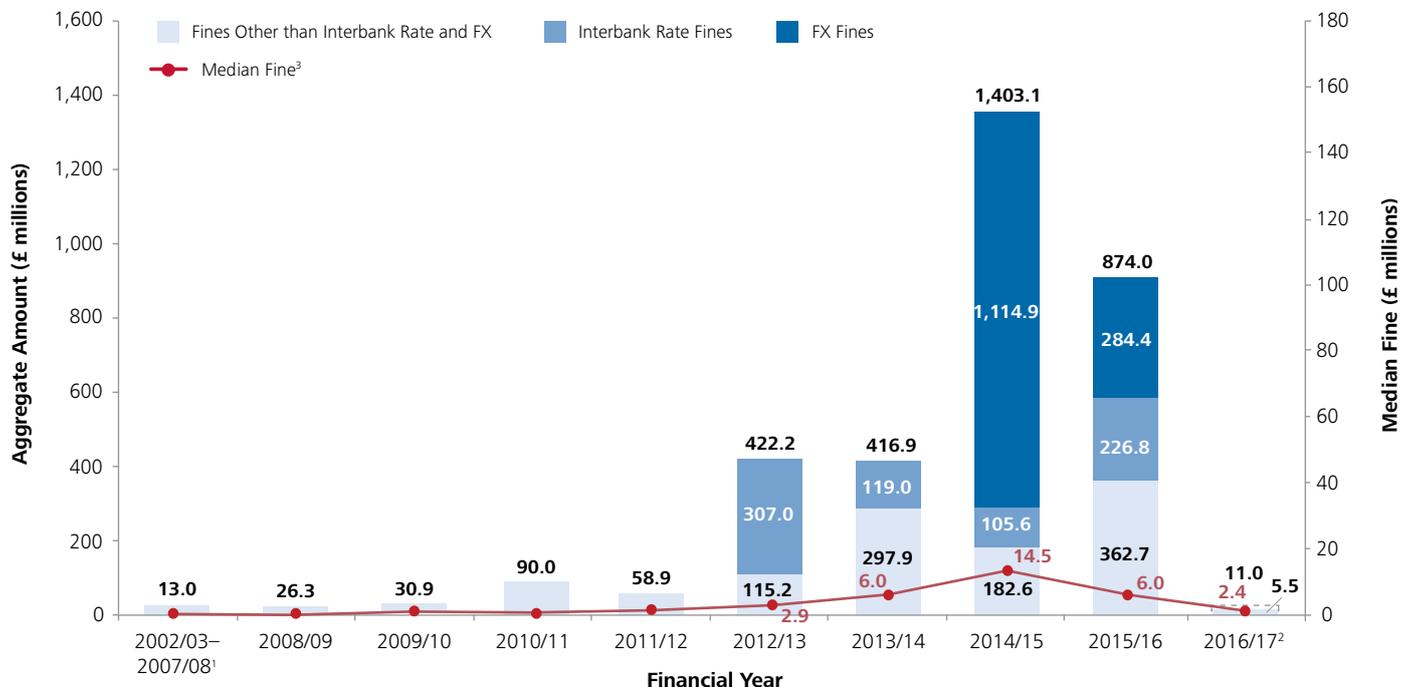
The three fines imposed on firms in the first half of 2016/17 comprise:

- a £2.6 million fine on Towergate Underwriting Group Limited for alleged mishandling of client assets. This fine is noteworthy in that Towergate’s chairman John Tiner once headed the FSA.

- a £2.4 million fine assessed against CT Capital Limited for alleged mishandling of customer complaints related to Payment Protection Insurance (PPI), a subject of frequent FCA and FSA enforcement.⁹
- a £0.5 million fine levied on small-cap broker Cenkos Securities Plc for alleged inadequate security and safeguards with respect to provision of sponsor services.¹⁰ The fine was in relation to Cenkos’s sponsorship of an insurance company formerly known as Quindell, and, in particular, related to Cenkos’s work in late 2013 and early 2014 advising Quindell on its effort to become listed on the London Stock Exchange main market. According to the FCA, Cenkos advised the Authority that Quindell was eligible for a listing without adequate basis. In particular, the FCA concluded that Cenkos had not taken “reasonable steps sufficient to ensure that the information provided to the Authority was accurate and complete in all material respects.”¹¹ Quindell itself was the subject of an FCA investigation in relation to public statements regarding the company’s 2013 and 2014 financial accounts. In August 2015, following an external review of the company’s accounting policies, Quindell restated its 2013 financial results from a pre-tax profit to a loss and reported a large pre-tax loss for 2014.¹² The FCA dropped its investigation of Quindell in August 2015 in light of a parallel (ongoing) Serious Fraud Office (SFO) criminal probe into the company’s business and accounting practices.¹³

During the first half of 2016/17, the median of the fines imposed on firms—which can be interpreted as reflecting the “typical” fine—was £2.4 million. Consistent with the historically low aggregate fine amount, this median fine is less than half of the median fine in each of the financial years 2013/14 to 2015/16 (see Figure 3).

Figure 3. **Aggregate and Median Annual FCA Fine Amounts against Firms**



Notes and Sources:

Numbers may not sum precisely to totals due to rounding.

NERA classifies fines on sole proprietorships as fines on individuals.

¹ Annual average.

² Figures cover the first half of the 2016/17 financial year, from 1 April 2016 to 30 September 2016. The scaled up amount represents the annual total that would be obtained if aggregate fines in the second half of the 2016/17 financial year equal fines in the first half.

³ The calculation of the median fine excludes fines reduced to zero because of financial hardship.

Outlook for Fines on Firms

While the recent low level of FCA fines against firms has attracted some media attention,¹⁴ this trend may not persist. Rather, it may, at least in part, reflect a pause as the regulator redirects resources previously devoted to interbank rate and FX manipulation and the Operation Tabernula insider dealing investigation.

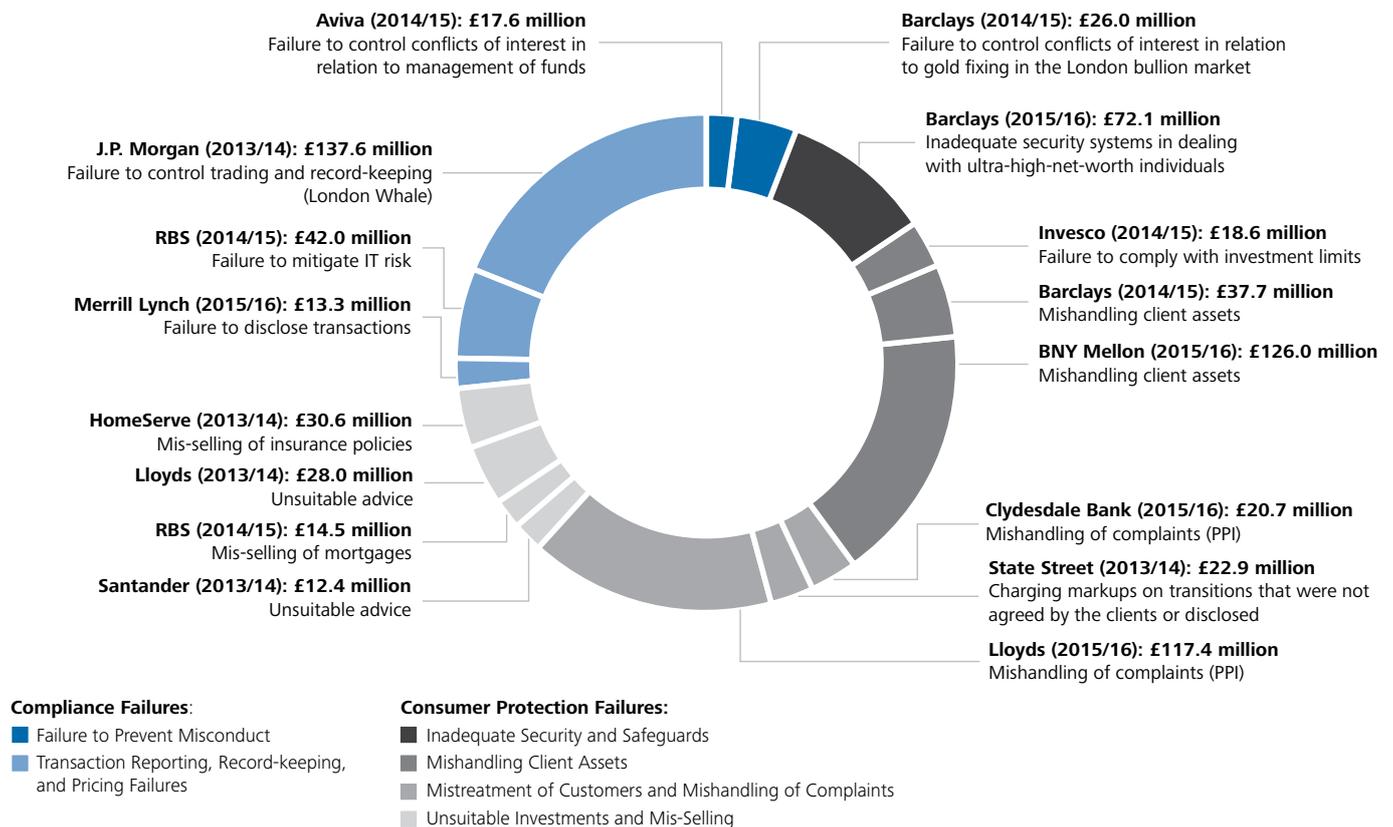
However, even if the low level of fines observed in the first half of 2016/17 does not persist, it is unclear exactly how fines on firms will evolve. One potentially relevant observation is that, even setting aside fines relating to interbank rates and FX markets, the FCA has imposed fines of substantial size, relating to a variety of conduct issues, with greater frequency than the FSA did previously.

As Figure 4 depicts, even excluding interbank rate and FX fines, the FCA has imposed 16 fines of £10 million or more in three and one-half years, a rate of four to five such fines per year. The FSA imposed half as many such fines (ie half as many fines of £10 million or more, other than those relating to interbank or FX manipulation) in its more than 11-year history.¹⁵

Figure 4 classifies these FCA fines by the type of alleged misconduct (see the Appendix for a description of our classification scheme). It shows that recent larger fines are not dominated by any one conduct issue. They include financial penalties relating to firms' consumer protection failures, such as mishandling of client assets and mis-selling, as well as firms' compliance failures, such as those relating to transaction reporting and failure to prevent misconduct.

This recent fine activity might, therefore, be taken as broadly indicative of the range of conduct issues attracting the FCA's attention and the severity of fines that the Authority is willing to impose.

Figure 4. **FCA Fines against Firms in Excess of £10 Million, Excluding Interbank Rate and FX Fines**
1 April 2013 to 30 September 2016



However, that is subject to at least two caveats. First, the FCA's enforcement philosophy may change, such that these larger fines are not necessarily indicative of the severity of future fines. Second, the level of fines imposed will ultimately also depend on which conduct issues arise in future and the seriousness of those issues.

The first several weeks of the second half of the current financial year (which began on 1 October 2016) provided an indication that the very low levels of fines observed during the first half of the financial year may have been a transitory phenomenon. On 5 October 2016, the FCA imposed an £8.2 million fine against two units of the insurer Aviva for client money failings. A week later, on 12 October 2016, the FCA fined Sonali Bank (UK) Limited £3.25 million for failures in Anti-Money Laundering (AML) controls. These two fines, for a total of more than £11 million, already exceed the total imposed in the first half of the current financial year, ie in the six months ended 30 September 2016.

Non-Pecuniary Measures

While the level of fines against firms was low in the first half of the 2016/17 financial year, the FCA's use of non-pecuniary enforcement measures (ie measures other than fines) against firms actually exceeded the levels observed in recent years (for descriptions of the various enforcement measures available to the FCA, see the Appendix to our 2015/16 year-end report¹⁶). During the first half of the current financial year, the FCA resolved 29 cases involving variations, cancellations, or refusals of permission to operate within the UK financial industry. At the current pace, the total number of non-monetary enforcement sanctions against firms for 2016/17 is on track to exceed the levels observed in eight of the last nine financial years¹⁷ (see Figure 5 on the next page).

Enforcement against Individuals

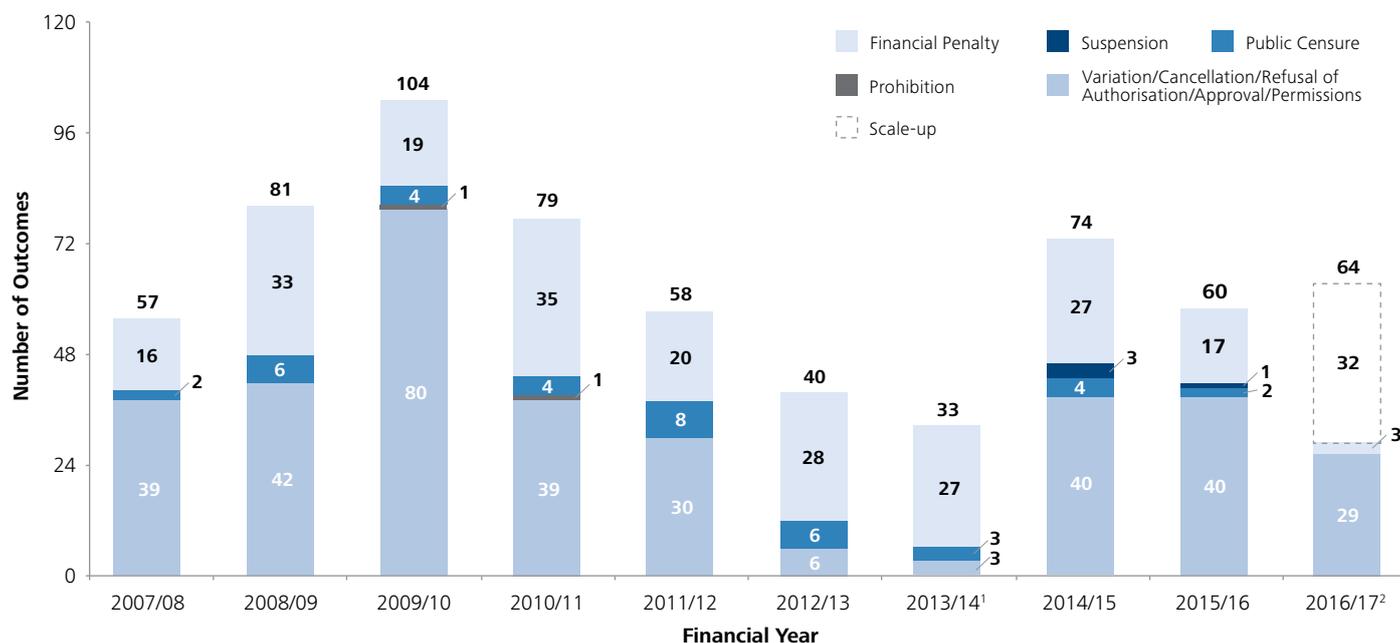
While the FCA imposed only nine fines on individuals in the first half of the 2016/17 financial year, these represented 75% of the total number of fines imposed during that period. The last financial year in which the FCA imposed a greater number of fines against individuals than it imposed on firms was in 2011/12.

Of the nine fines, three were reduced to zero due to financial hardship; the remaining six collectively totalled £0.7 million, a modest aggregate amount in comparison to recent years (see Figure 6 on page 8). If fines on individuals were to continue at the same pace in the second half of 2016/17 as in the first half, the resulting aggregate fine amount (approximately £1.5 million) would be lower than in any of the prior seven financial years, even if those prior totals are calculated excluding the top 10 largest fines ever issued by the FCA against individuals.¹⁸

The largest fine against an individual in the first half of 2016/17 was for £450,000, less than half of the fine amount that would be required to qualify for inclusion in the top 10. This fine was imposed in a final notice dated 8 April 2016 and was in relation to approved person regulatory failures. Timothy Alan Roberts, former chief executive at Catalyst Investment Group, was fined and issued a prohibition order based on the regulator's finding that Mr Roberts had "acted without integrity (in breach of Statement of Principle 1) and failed to exercise due skill, care and diligence (in breach of Statement of Principle 6)"¹⁹ when raising funds for investment in asset-backed securities issued by Asset Backed Securities SA (ARM).

The FCA found that Catalyst had sold asset-backed securities issued by ARM, a Luxembourg-based firm run by Mr Roberts, even though ARM had not received a licence to issue the securities. The FCA further found that Mr Roberts did not reveal this fact to independent financial advisors to whom Catalyst promoted the ARM securities.

Figure 5. **FCA Enforcement Activity against Firms by Type of Sanction**
2007/08–2015/16, and First Half 2016/17



Notes and Sources:

For financial years 2007/08–2013/14, data are taken directly from the “Enforcement Activity” appendices to FCA annual reports. For 2014/15 and thereafter, data were compiled by NERA from final notices.

Therefore, for financial years prior to 2014/15, the annual numbers of financial penalties shown here may differ from statistics reported by NERA in Table 1. Moreover, the numbers presented in Figure 5 for financial years prior to 2014/15 (taken from the FCA annual reports) are on a slightly different basis to the numbers for 2014/15 and after (compiled by NERA). This is for several reasons. First, beginning with its 2009/10 Annual Report, the FCA assigns each fine to a financial year based on the publication date of the press release announcing the fine, whereas NERA uses the date of the final notice in Table 1 and in the figures presented in Figure 5 for 2014/15 and later. Moreover, the FCA does not include in its tallies fines that were reduced to zero owing to financial hardship, whereas Table 1 includes such fines. Finally, NERA classifies fines on sole proprietorships as fines on individuals, whereas the FCA classifies these as fines on firms. The outcomes represent single enforcement actions against firms. For example, three enforcement actions within the same case (ie fine, public censure, and prohibition against a firm) are counted as three distinct outcomes.

¹ Does not include Threshold Condition outcomes where the FCA only cancels a firm’s Part 4A permission or its registration (“Threshold Conditions are effectively the minimum standards for being, and remaining, authorised by the FCA. Maintaining these is an ongoing requirement, and the FCA can vary or cancel a firm’s permission if it believes that that firm is failing, or likely to fail, to meet them.” See Threshold Conditions, *Global Insurance Management*, 24 June 2013, available at: <http://www.globalim.co.uk/latestnews/insurance-intermediaries/fsa%20news/2013/jun/24/threshold-conditions>).

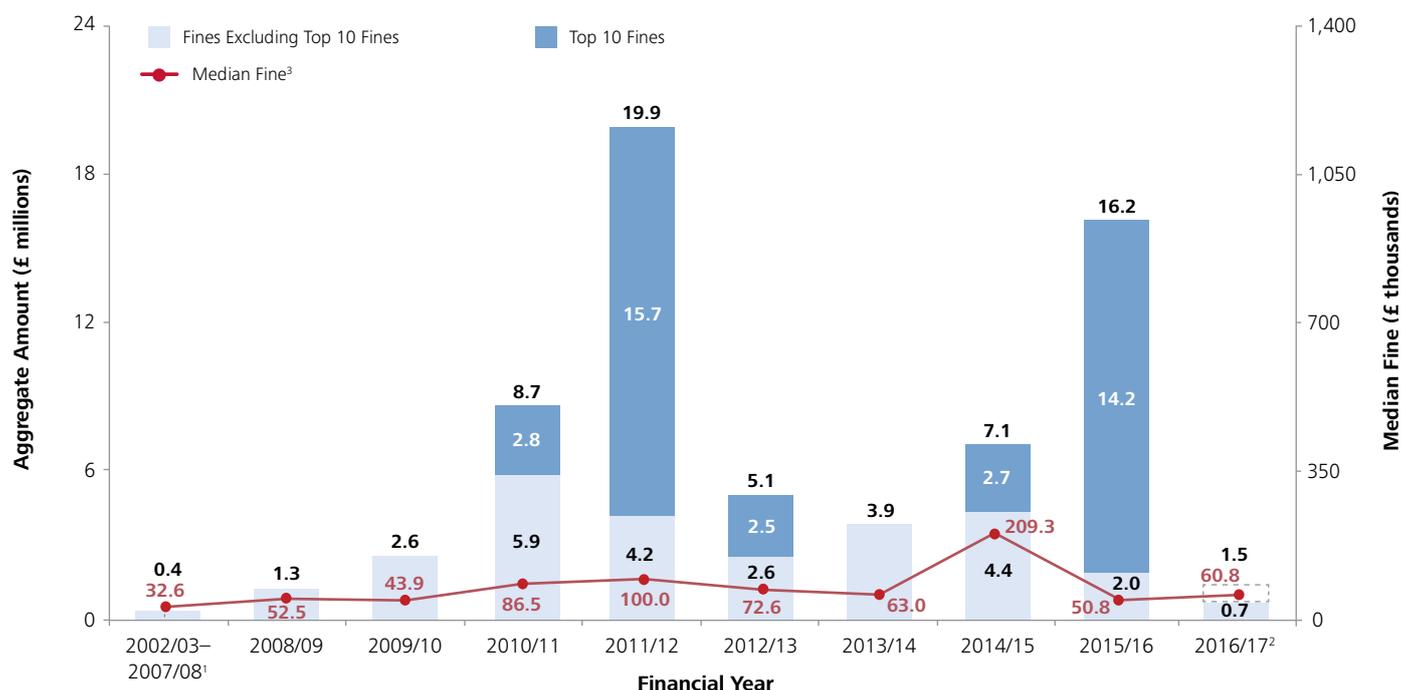
² Figures cover the first half of the 2016/17 financial year, from 1 April 2016 to 30 September 2016. The scaled up figure represents the annual total number of outcomes that would be taken if the number of outcomes in the second half of the 2016/17 financial year equals the number in the first half.

The fine on Mr Roberts followed a victory for the FCA at the Upper Tribunal in August 2015. Both Mr Roberts and Andrew Peter Wilkins, a former co-director at Catalyst, had gone to the Tribunal to challenge 2013 FCA decision notices relating to ARM, in which the Authority sought to impose a £450,000 fine on Mr Roberts and a £100,000 fine on Mr Wilkins. As discussed in a prior edition of this report,²⁰ the Upper Tribunal upheld the fine on Mr Roberts and upheld the FCA’s findings that he had acted without integrity and failed to exercise due skill, care, and diligence.

With respect to Mr Wilkins, however, the FCA only partially upheld the FCA’s findings and reduced his fine to £50,000 (this was imposed in a final notice dated 22 October 2015 and is thus included in our fine totals for 2015/16).

Other enforcement actions against individuals during this period included a fine of £109,400, accompanied by a prohibition order, against Elizabeth Anne Parry in relation to forgery of Statements of Professional Standing and attempts to mislead the FCA. Also, a £59,557 fine and a public censure were imposed on Gavin Duncan Paul Breeze for insider dealing. The enforcement action against Mr Breeze was noteworthy amongst insider dealing cases in that, in addition to the monetary fine, the

Figure 6. **Aggregate and Median Annual FCA Fine Amounts against Individuals**



Notes and Sources:

Numbers may not sum precisely to totals due to rounding.

NERA classifies fines on sole proprietorships as individual fines.

¹ Annual average.

² Figures cover the first half of the 2016/17 financial year, from 1 April 2016 to 30 September 2016. The scaled up amount represents the annual total that would be obtained if aggregate fines in the second half of the 2016/17 financial year equal fines in the first half.

³ The calculation of the median fine excludes fines reduced to zero because of financial hardship.

Authority required Mr Breeze to pay restitution to counterparties to his trades.

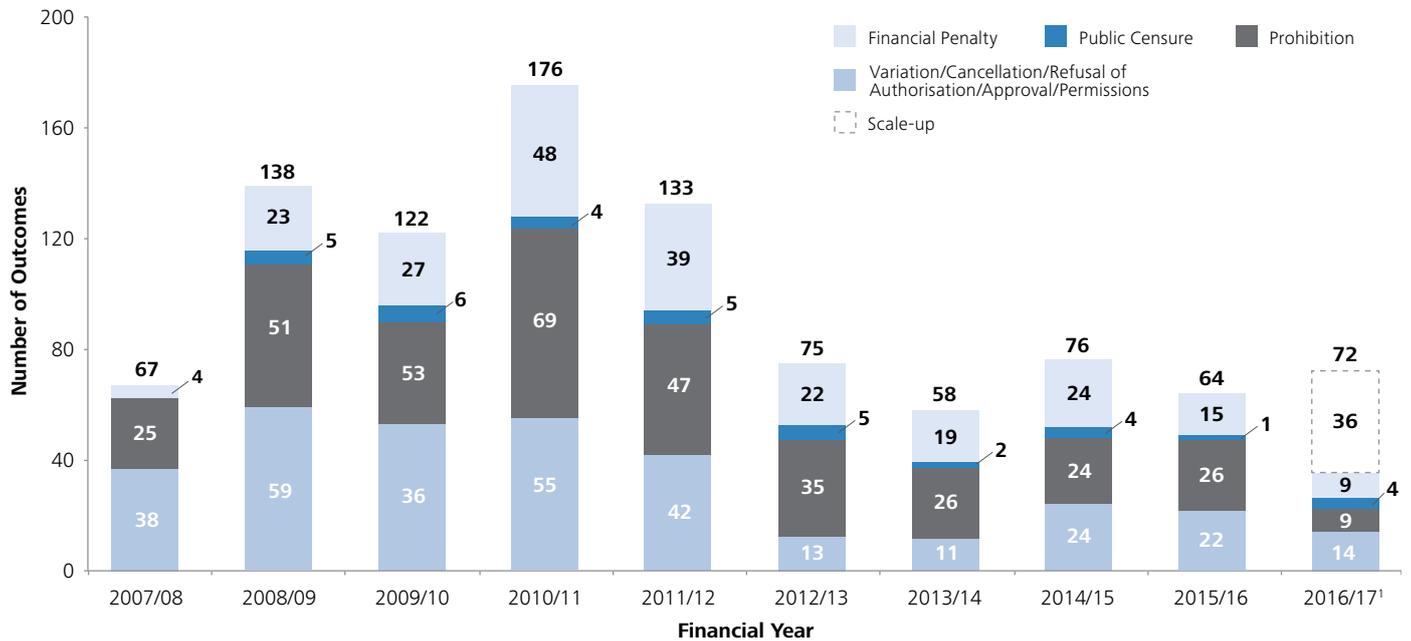
The median fine against individuals in the first half of the current financial year (£60,833, calculated excluding fines reduced to zero due to economic hardship) was somewhat higher than in 2015/16, though much lower than the median fine of £209,300 in 2014/15.

Non-Pecuniary Measures

Despite the relatively low number and amount of financial penalties imposed by the FCA on individuals in the first half of 2016/17, the use of non-pecuniary enforcement sanctions appears to be in line with the levels observed over the prior four financial years (see Figure 7 on the next page). Prohibitions remain the most commonly used of these non-monetary deterrence measures; in fact, eight of the nine financial penalties imposed in the first half of 2016/17 were accompanied by a prohibition order.

The FCA has continued to pursue enforcement actions against individuals in relation to the manipulation of interbank benchmarks, complementing the SFO’s ongoing criminal investigations. In the first six months of the 2016/17 financial year, the Authority publicly censured Paul White, a former LIBOR rate submitter at the Royal Bank of Scotland, and banned him from performing any function in relation to any regulated activity within the UK financial services industry. The proposed fine of £250,000 was reduced to zero due to financial hardship.

Figure 7. **FCA Enforcement Activity against Individuals by Type of Sanction**
2007/08–2015/16, and First Half 2016/17



Notes and Sources:

For financial years 2007/08–2013/14, data are taken directly from the “Enforcement Activity” appendices to FCA annual reports. For 2014/15 and thereafter, data were compiled by NERA from final notices.

Therefore, for financial years prior to 2014/15, the annual numbers of financial penalties shown here may differ from statistics reported by NERA in Table 1. Moreover, the numbers presented in Figure 7 for financial years prior to 2014/15 (taken from the FCA annual reports) are on a slightly different basis to the numbers for 2014/15 and after (compiled by NERA). This is for several reasons. First, beginning with its 2009/10 Annual Report, the FCA assigns each fine to a financial year based on the publication date of the press release announcing the fine, whereas NERA uses the date of the final notice in Table 1 and in the figures presented in Figure 5 for 2014/15 and later. Moreover, the FCA does not include in its tallies fines that were reduced to zero owing to financial hardship, whereas Table 1 includes such fines. Finally, NERA classifies fines on sole proprietorships as fines on individuals, whereas the FCA classifies these as fines on firms. The outcomes represent single enforcement actions against individuals. For example, three enforcement actions within the same case (ie fine, public censure, and prohibition against an individual) are counted as three distinct outcomes.

¹ Figures cover the first half of the 2016/17 financial year, from 1 April 2016 to 30 September 2016. The scaled up figure represents the annual total number of outcomes that would be taken if the number of outcomes in the second half of the 2016/17 financial year equals the number in the first half.

Another ongoing high-profile case involves Andrew Tinney, former Global Chief Operating Officer of Barclays Wealth and Investment Management. The FCA alleges that during his tenure, Mr Tinney suppressed an internal report commissioned from a third-party consultancy whose contents appeared to be highly critical of the corporate culture at Barclays. The report expressed an opinion that Barclays’ US wealth unit had “pursued a course of revenue at all costs” and recommended a senior management reshuffle.²¹ The FCA also alleges that Mr Tinney made misleading statements and omissions to colleagues as to the report’s nature and/or existence. The Authority is seeking to publicly censure Mr Tinney and ban him from carrying out any senior management or significant influence functions in the UK financial services industry. The case currently awaits a hearing at the Upper Tribunal.²²

The FCA announced a prohibition for Andrew Barry Hart, the director and owner of Wage Payment and Payday Loans Limited (WPPL), from carrying out activities as an approved person. The FCA also announced a cancellation of permission for WPPL. In July, the FCA had issued a decision notice²³ relating to the intended actions; at that time, Mr Hart and WPPL planned to appeal to the Upper Tribunal, but the appeal was subsequently withdrawn. The FCA found that Mr Hart contributed to and failed to stop unfair business practices that had a direct negative impact on customers, including causing them financial losses. This enforcement action represents an exercise by the FCA of its powers to regulate consumer credit, which it took over from the Office of Fair Trading (OFT) in April 2014.

Trends in FCA Criminal Prosecution

During the first half of the 2016/17 financial year alone, the Authority criminally indicted more individuals than in either of the previous two financial years. In June 2016, the FCA charged five individuals with alleged investment fraud in relation to “a purported commercial development in Madeira in which, in total, 175 investors may have lost approximately £2.75 million.”²⁴ The FCA also charged a former investment portfolio manager at Blackrock Investment Management (UK) Ltd., Mark Alexander Lyttleton, with insider dealing. Mr Lyttleton pleaded guilty to two counts of insider dealing on 2 November 2016 and will be sentenced on 21 December 2016.

If the pace of indictments over the first six months of 2016/17 continues over the remainder of the financial year, the FCA will match the number of indictments in the 2013/14 financial year, the maximum during the FCA’s existence (see Table 2).

Table 2. **FCA Criminal Indictments**
2002/03–2015/16, and First Half 2016/17

	Indictment Year ¹								Total
	Prior to 2010/11	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	H1 2016/17 ²	
Indictment of Individuals									
Insider Dealing	12	14	4	8	1	3	3	1	46
Land Banking	0	0	0	0	8	0	0	0	8
Other Indictments ³	20	1	0	3	3	1	0	5	33
Total	32	15	4	11	12	4	3	6	87

Notes and Sources:

Data are from FCA press releases, supplemented by a review of news articles. The table includes only named defendants.

¹ If the indictment date is not reported in the FCA’s press releases, the arrest date is used.

² Figures cover the first half of the 2016/17 financial year, from 1 April 2016 to 30 September 2016.

³ Includes cases of mis-selling, stealing, fraud, illegal deposit taking, and failure to cooperate with the FCA.

Indeed, there is some indication that the pace of indictments may accelerate in the second half of the current financial year. In the first three months of the current financial year, the FCA opened 14 new criminal investigations into insider dealing, bringing the total number of open cases to 54.²⁵ With the large-scale Operation Tabernula investigation largely concluded,²⁶ the FCA may now be in a position to focus more resources on other investigations, including ones related to insider dealing. The release of the FCA’s most recent market cleanliness statistics in July 2016²⁷ may be a further indication that the Authority will focus its attention on this area. They showed that share prices moved abnormally ahead of almost one out of every five UK public takeover announcements in 2015 (the highest level since 2011).

Five verdicts were reached in criminal prosecutions by the FCA against individuals during the first half of the 2016/17 financial year. Each of these was in connection with Operation Tabernula. Two of the five individuals were convicted, while the remaining three were acquitted (see Table 3 on the next page).

Table 3. **FCA Criminal Verdicts**
2002/03–2015/16, and First Half 2016/17

	Verdict Year ¹								Total
	Prior to 2010/11	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	HI 2016/17 ²	
Outcomes									
Insider Dealing Convictions	5	5	1	12	1	3	1	2	30
Land Banking Convictions	0	0	0	0	0	0	8	0	8
Other Convictions ³	9	0	4	1	2	3	0	0	19
Acquittals	1	3	0	5	4	0	0	3	16
Total	15	8	5	18	7	6	9	5	73

Notes and Sources:

Data are from FCA press releases, supplemented by a review of news articles. The table includes only named defendants.

¹ If the verdict date is not reported in the press release, the sentencing date is used instead.

² Figures cover the first half of the 2016/17 financial year, from 1 April 2016 to 30 September 2016.

³ Includes cases of mis-selling, stealing, fraud, illegal deposit taking, and failure to cooperate with the FCA.

Conclusion

FCA fine activity in the first half of the 2016/17 financial year was low as compared to recent levels. This may be a temporary lull as the FCA redirects its resources from large-scale investigations such as those into interbank rate and FX manipulation and Operation Tabernula. Based upon fine activity in the first few weeks of the second half of the 2016/17 financial year, fines against firms may already be picking up in intensity.

While the FCA has continued to emphasise the importance of holding senior managers at financial institutions to account, the number and amount of financial penalties imposed by the FCA on individuals in the first half of 2016/17 remained low. However, this trend may be reversed with the introduction of the Senior Manager’s Regime (SMR) and the European Union’s Market Abuse Regulation (MAR). The pending case against Andrew Tinney reflects an intended enforcement action against a senior executive at a major bank. Moreover, criminal prosecution of individuals is on the rise, with the FCA indicting more individuals in the first six months of this financial year than in either of the prior two financial years.

The FCA recently published a document with its proposals as to its future mission (the Mission).²⁸ The Authority is soliciting feedback from market participants as to the best way for the Authority to apply its statutory objectives in future. In the Mission, the FCA highlights the importance of protecting vulnerable consumers, making clear that the Authority will intervene in unregulated activities (ie activities outside of the FCA’s direct remit) if these activities threaten the FCA’s objectives—for example, if they pose a threat to the UK financial system.²⁹ This suggests some potential for a widening of the scope of activities that may be subject to FCA enforcement. The Mission also indicates that the FCA will be reviewing its use of “private warnings”—ie non-public warnings made to firms that they came close to being subject to a formal (public) action. If the FCA were to foreclose the option of providing firms with private warnings, this could potentially lead to increased publicly announced enforcement actions against firms.³⁰

NERA will continue to monitor and analyse these developments as they unfold.

Appendix: Classification of Fines by Type of Alleged Misconduct

Market Integrity Violations

Our classification scheme makes a basic distinction between cases alleging violations of market integrity—behaviour that distorts or otherwise negatively affects financial markets—and other types of cases. We classify four types of conduct as relating to market integrity:

- *Insider Dealing*: Unlawful trading based on non-public (inside) information and/or improper dissemination of such information.³¹
- *Market Manipulation*: Transactions made, orders placed, or other similar actions intended to manipulate the price of a financial instrument or otherwise create a false impression about the market for a financial instrument.³²
- *Misleading Disclosures*: Dissemination of misleading information about an investment or issuer, or other actions taken to give a false impression about, and thus distort the market for, an investment.³³
- *Failures to Disclose*: Delay or omissions by a publicly traded company in providing the market with information that is required to be disclosed, leading to a distortion in the market for the company's securities.³⁴

Customer Protection Failures

Fines related to customer protection failures involve the following types of misconduct:

- *Unsuitable Investments and Mis-Selling*: This category includes cases that allege investment advice given to, or investments made on behalf of, a client or clients, which are not suitable to client risk preferences or circumstances (or both). Often these cases involve a failure to obtain “know your customer” information necessary to assess the suitability of investment recommendations or decisions.³⁵ This category also includes improper marketing cases including failure to provide sufficient and non-misleading information in promoting or selling a security,³⁶ and some small capitalisation stock brokerage, or “boiler room”, cases.³⁷
- *Mistreatment of Customers & Mishandling of Complaints*: This includes cases where clients were not catered to in a manner deemed fit by the FCA. Common examples include overcharging of customer fees, using high-pressure sales tactics,³⁸ poor treatment of customers facing mortgage arrears, or disadvantaging certain customers in any way.³⁹ Failures to respond appropriately to client complaints are also included in this category.⁴⁰
- *Mishandling of Client Assets*: This includes failure to segregate client assets from firm assets and other failures to safeguard, or misuse of, money managed on behalf of clients.⁴¹
- *Inadequate Security and Safeguards*: These include control failures relating to financial crime prevention—such as failing to screen customers against the government's “sanctions list”, failing to report or appropriately monitor suspicious behaviour (such as potential bribery), or allowing third parties inappropriate access to client funds, as well as cases where identity fraud risks were posed due to the granting of access to client funds or confidential information without the adequate verification of the identity of the party seeking such access or information.⁴²

Compliance Failures

Fines related to failures in regulatory compliance involve the following types of misconduct:

- *Transaction Reporting, Record-Keeping, and Pricing Failures:* These are cases alleging inadequacies in maintaining accurate records and/or reporting such records in a timely and accurate manner. They often relate to failures to provide accurate and timely transaction reports or to mis-marking of securities.⁴³
- *Approved Person Regulation Failures:* These relate to breaches of the FCA's Approved Persons regulations, for example allowing an individual to hold a "significant influence function" (SIF) such as director or officer, without obtaining the FCA's approval, or a failure to notify the FCA of a regulatory investigation in respect of an approved person in the UK.⁴⁴
- *Failure to Prevent Misconduct:* These relate to cases in which the FCA sanctions managers (eg SIF holders) not directly involved in underlying misconduct but in a position to have prevented misconduct committed by others.⁴⁵
- *Other Compliance Failings by Firms:* To date, these cases include fines for lying to the FCA, failing to adequately respond to FCA requests, operating without required FCA authorisation, and tampering with documents sent to the FCA.⁴⁶

Fraud or Other Deliberate Misconduct

These cases have included fraud related to mortgage applications, insurance issuance, and misleading clients or potential clients regarding status as an approved person.⁴⁷ This category also includes theft from clients and misappropriation of client assets.

Notes

- 1 Mr Patton and Ms McHugh are Associate Directors at NERA Economic Consulting. The authors were assisted by Marcin Pruski, a former Economic Analyst at NERA. The authors would like to thank Bradley Heys for valuable feedback on earlier drafts, and George Moschopoulos and Davide Oneglia for research assistance.
- 2 On 1 April 2013, the Financial Services Act 2012 came into force, and the FCA superseded the FSA as financial enforcement regulator. In this paper, unless indicated otherwise, we use “FCA”, “the Authority”, or “the regulator” to refer to the FSA and the FCA collectively. Unless otherwise indicated, information presented in this paper relating to fines is taken from NERA’s database of final notices obtained from the FCA and FSA websites.
- 3 Laura Noonan, “New Bank Regulator Andrew Bailey Signals Softer Approach”, *Financial Times*, 27 January 2016.
- 4 Robert Patton, Erin McHugh, Giulio Renzi-Ricci, and Marcin Pruski, *Trends in Regulatory Enforcement in UK Financial Markets: 2015/16 Year-End Report*, 8 July 2016, available at: <http://www.nera.com/publications/archive/2016/trends-in-regulatory-enforcement-in-uk-financial-markets-2015-16.html>.
- 5 From 1 October 2007 to 31 March 2008, the FSA imposed 11 fines totalling £3.4 million.
- 6 LIBOR is the London Interbank Offered Rate and is a series of benchmark rates that banks charge one another for short-term unsecured loans of various maturities. It serves as a reference rate for many financial products and contracts. It is set on a daily basis based on estimated borrowing rates submitted by major banks.
- 7 A fine of £226.8 million was imposed on Deutsche Bank on 23 April 2015 in relation to alleged interbank rate manipulation. A fine of £284.4 million was issued against Barclays on 20 May 2015 in relation to alleged FX manipulation.
- 8 Evan Weinberger, “New UK Finance Regulator Won’t Bring Back ‘Light Touch’ Era”, *Law360*, 22 October 2012.
- 9 PPI policies are designed to cover repayment of debts (eg loans, mortgages, and credit card debt) in certain adverse circumstances—for example, if the borrower suffers an accident or illness. The FCA has found that PPI policies were mis-sold to many consumers. See, for example, *Payment Protection Insurance (PPI) Explained*, Financial Conduct Authority, 14 March 2016, available at: <https://www.the-fca.org.uk/consumers/payment-protection-insurance-ppi-explained>.
- 10 Companies approved as sponsors under the FCA’s Sponsor Regime help maintain integrity of the premium listed London equity market. Their responsibilities consist of assisting current and prospective companies throughout the premium listing process, as well as providing key regulatory assurances to the FCA.
- 11 Final Notice 2016: *Cenkos Securities Plc*, Financial Conduct Authority, 8 August 2016, p. 18, available at: <https://www.fca.org.uk/sites/default/files/cenkos-securities.pdf>.
- 12 “Quindell PLC 2014 Results Announcement”, *Regulatory News Service*, 5 August 2015.
- 13 “FCA Discontinues Investigation into Quindell”, *Financial Times*, 18 August 2015. “Cenkos Investigated by City Watchdog over Quindell”, *Financial Times*, 27 July 2016.
- 14 See, for example, “Nothing to Fine Here: Bank Penalties Drop 99.7%”, *Financial News*, 10 October 2016.
- 15 The FSA was created in 1997 and began to exercise its statutory powers under the Financial Services and Markets Act 2000 in December 2001. The FSA imposed eight fines in excess of £10 million, as follows (ranked by size of fine): 1) JP Morgan, 2010, failure to protect client assets: £33.3 million; 2) Prudential, 2013, failure to inform the regulator of an intended acquisition: £30.0 million; 3) UBS, 2012, failure to prevent misconduct (unauthorised trading): £29.7 million; 4) Goldman Sachs, 2010, weaknesses in controls/failure to report authorised person: £17.5 million; 5) Royal Dutch Shell, 2004, disclosure violations: £17.0 million; 6) Citigroup, 2005, systems and controls violations relating to trading conduct: £14.0 million; 7) Card Protection Plan, 2012, insurance mis-selling: £10.5 million; 8) HSBC, 2011, failures relating to suitability of investment advice provided by NHFA Limited: £10.5 million. Even if only the final three years of the FSA’s existence are considered, during which period it imposed large fines with greater frequency than previously, the six fines of £10 million or more from 1 April 2010 through to 31 March 2013 equate to a rate of two such fines per year.
- 16 Robert Patton and Marcin Pruski, *Trends in Regulatory Enforcement in UK Financial Markets: 2015/16 Mid-Year Report*, 15 October 2015, p. 25, available at: <http://www.nera.com/publications/archive/2015/trends-in-regulatory-enforcement-in-uk-financial-markets.html>.
- 17 The 29 non-monetary enforcement sanctions against firms during the first half of 2016/17 equate to 58 non-monetary sanctions on an annualised basis (=29 * 2).
- 18 See Table 4 of our 2015/16 full-year report for the complete list. Robert Patton, Erin McHugh, Giulio Renzi-Ricci, and Marcin Pruski, *Trends in Regulatory Enforcement in UK Financial Markets: 2015/16 Year-End Report*, 8 July 2016, available at: <http://www.nera.com/publications/archive/2016/trends-in-regulatory-enforcement-in-uk-financial-markets-2015-16.html>.
- 19 Final Notice 2016: *Timothy Alan Roberts*, Financial Conduct Authority, 8 April 2016, p. 1, available at: <https://www.fca.org.uk/publication/final-notices/timothy-alan-roberts.pdf>.
- 20 Robert Patton and Marcin Pruski, *Trends in Regulatory Enforcement in UK Financial Markets 2015/16 Mid-Year Report*, 15 October 2015, p. 22, available at: <http://www.nera.com/publications/archive/2015/trends-in-regulatory-enforcement-in-uk-financial-markets.html>.
- 21 *Decision Notice 2016: Andrew James Tinney*, Financial Conduct Authority, 8 July 2016, p. 2, available at: <https://www.fca.org.uk/sites/default/files/andrew-tinney.pdf>.
- 22 *The FCA Publishes Decision Notice for Andrew Tinney, Former Barclays Wealth Senior Director*, Financial Conduct Authority, 14 September 2016, available at: <https://www.fca.org.uk/news/press-releases/fca-publishes-decision-notice-andrew-tinney-former-barclays-wealth-senior>. *Decision Notice 2016: Andrew James Tinney*, Financial Conduct Authority, 8 July 2016, available at: <https://www.fca.org.uk/sites/default/files/andrew-tinney.pdf>.
- 23 *Decision Notice 2015: Andrew Barry Hart*, Financial Conduct Authority, 31 July 2015, available at: <https://www.fca.org.uk/publication/decision-notices/andrew-barry-hart.pdf>.

- 24 FCA Charge Five in Alleged Investment Fraud, Financial Conduct Authority, 16 June 2016, available at: <https://www.fca.org.uk/news/press-releases/fca-charge-five-alleged-investment-fraud>.
- 25 Katie Marriner, "FCA Criminal Probes into Insider Dealing Soar", Money Marketing, 23 September 2016.
- 26 The one remaining defendant, Richard Baldwin, was deemed too ill to face trial earlier this year. A decision has not yet been made about how to proceed with the charges against him.
- 27 Annual Report and Accounts 2015/16, Financial Conduct Authority, 12 July 2016, p. 16.
- 28 Our Future Mission, Financial Conduct Authority, October 2016, available at: <https://www.fca.org.uk/publication/corporate/our-future-mission.pdf>.
- 29 Our Future Mission, Financial Conduct Authority, October 2016, p. 4-5, 18-19, available at: <https://www.fca.org.uk/publication/corporate/our-future-mission.pdf>.
- 30 Mark Taylor, "Lawyers Wary as FCA Shifts to US-Style Enforcement", Law360, 1 November 2016.
- 31 These cases typically are described by the FCA as breaching sections 1.3 ("Insider Dealing"), 1.4 ("Improper Disclosure"), and/or 1.5 ("Misuse of Information") of its Code of Market Conduct (MAR). These cases typically also include references to Section 118 ("Market Abuse") of the Financial Services and Markets Act 2000.
- 32 Market manipulation cases typically allege breaches of sections 1.6 ("Manipulating Transactions"), 1.7 ("Manipulating Devices"), and/or 1.9 ("Misleading Behaviour & Distortion") of the FCA's Code of Market Conduct (MAR). These cases may also include references to Section 118 ("Market Abuse") of the Financial Services and Markets Act 2000.
- 33 Misleading disclosure cases typically correspond to breaches of section 1.8 ("Dissemination") of the FCA's Code of Market Conduct (MAR) and often cite breaches of the FSA's Listing Rules (LR). These cases may also include references to Section 118 ("Market Abuse") of the Financial Services and Markets Act 2000.
- 34 These are typically described as breaching the FCA's "Listing Rules" (LR) but not its Code of Market Conduct (MAR).
- 35 These typically allege a breach of Principle 9 ("Customers: Relationships of Trust") of the FCA's Principles for Businesses (PRIN).
- 36 These typically allege a breach of Principle 7 ("Communications with Clients") of the FCA's Principles for Businesses (PRIN).
- 37 In some other cases "boiler room" activities may amount to market abuse.
- 38 This category includes the 2008 fine against Square Mile for both using high-pressure sales tactics and providing misleading information to investors.
- 39 These cases typically allege breaches of Principles 6 ("Customers' Interests") or 8 ("Conflicts of Interest") of the FCA's Principles for Businesses (PRIN).
- 40 These typically allege breaches of Principles 6 ("Customers' interests") of the FCA's Principles for Businesses (PRIN).
- 41 These cases typically allege breaches of the FCA's Client Money Rules or Principle 10 ("Clients' Assets") of the FCA's Principles for Business (PRIN).
- 42 Cases involving control failures relating to financial crime often cite breaches of Principles 2 ("Skill, Care and Diligence") and 3 ("Management and Control") of the FCA's Principles for Businesses (PRIN). Cases involving identity fraud risks typically allege breach of the "Money Laundering Rules" (ML), as the potential identity fraud could have been used in money laundering schemes.
- 43 These cases typically cite breaches of Principle 2 ("Skill, Care and Diligence"), Principle 3 ("Management and Control") of the FCA's Principles for Businesses (PRIN), and may also cite breaches of the FCA's "Statement of Principles for Approved Persons" (APER).
- 44 Most recently, these cases cite breaches of Principle 1 ("Integrity") and Principle 11 ("Relations with Regulators") of the FCA's "Principles for Businesses" (PRIN), and breaches of Principle 6 ("Skill, Care, and Diligence") of the FCA's "Statements of Principles for Approved Persons" (APER).
- 45 These cases often cite breaches of Principles 2 ("Skill, Care and Diligence") and 3 ("Management and Control") of the FCA's Principles for Businesses (PRIN) and often additionally cite breaches of the FCA's "Statement of Principles for Approved Persons" (APER). These cases include failures to prevent market abuse.
- 46 These cases have included breaches of the Listing Rules and the FCA's "Principles for Businesses" (PRIN), including Principle 2 ("Skill, Care and Diligence"), Principle 3 ("Management and Control"), Principle 8 ("Conflicts of Interest"), and Principle 11 ("Relations with Regulators").
- 47 These cases typically include breaches of the FCA's Principles for Businesses and often additionally cite breaches of the FCA's "Statement of Principles for Approved Persons" (APER).

About NERA

NERA Economic Consulting (www.nera.com) is a global firm of experts dedicated to applying economic, finance, and quantitative principles to complex business and legal challenges. For over half a century, NERA's economists have been creating strategies, studies, reports, expert testimony, and policy recommendations for government authorities and the world's leading law firms and corporations. We bring academic rigor, objectivity, and real world industry experience to bear on issues arising from competition, regulation, public policy, strategy, finance, and litigation.

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