

24 January 2025

Dear Chief Executive,

You are receiving this letter because we are setting out our new strategy for supervising wholesale brokers, which is how we define your firm. As in previous years, the FCA continues to take a strategic approach to our supervision of firms operating similar business models. As part of this approach, we take a view on what we see as the key harms that brokerages operating in wholesale financial markets pose to their clients and to markets.

We expect you to discuss the contents of this letter with your Board, understand how the risks apply to your business and take action to manage those risks effectively.

Sector overview

Wholesale brokers play a vital role in financial markets, by sourcing liquidity for their clients, providing market access for clients who are unable to access them otherwise, and by connecting buyers and sellers to negotiate, match and execute trades. The skill and insight of brokers when arranging transactions means that, when operating at their best, they improve client outcomes and contribute significantly towards upholding market standards.

We are pleased that there continues to be a vibrant wholesale broking market in the UK, despite persistent headwinds. Globally, financial markets continue to be challenging and regularly experience increased levels of uncertainty and periods of heightened volatility. This is caused by a diverse set of factors including wars and geopolitical tensions, supply-demand imbalances due to frictions in global trade and evolving central banking policies in response to inflationary pressures. Despite these circumstances, wholesale brokers continue to perform strongly as a sector, albeit we observe a growing trend of the largest players being able to benefit more from current market conditions. Consequently, we have observed a gradual change in the sector with larger firms acquiring smaller ones, which either complement their existing operations or provide entry into new markets, while some weaker mid-sized and smaller firms are exiting the market altogether. However, a strong core of specialist firms continues to exist and thrive, resulting in an overall healthy and competitive sector for wholesale intermediaries.

Previous cycle

Over the last two years, we have engaged with firms on a wide range of issues including liquidity risk management, financial crime, culture, and non-financial misconduct. Our general observation is that firms in the portfolio are improving in these areas, but this improvement is not evenly distributed, meaning more work is needed, particularly with firms who are lagging behind the rest.

Prudential risk management

The strategic focus of our work on prudential risk in the last two years was on clearing brokers, given the critical role they play in wholesale commodities markets. In our 2023 '[Dear CEO' letter](#)¹, we noted that for a subset of these firms, both liquidity risk management and stress testing were not fit for purpose. These weaknesses gave rise to risks such as clients experiencing losses and sudden, disorderly firm failure, both of which could affect the stability of certain markets.

Since then, we have been encouraged by the results obtained from our work with firms on their liquidity risk management frameworks (LRMFs), and by the work that some firms had already undertaken to improve their financial resilience. Although we imposed capital and liquidity guidance on individual firms, required CEO attestations to confirm successful remediation, and provided robust feedback to the portfolio overall, firms were eager to engage in a constructive dialogue with us throughout the review. To make sure this positive momentum is maintained, we will be publishing an observation paper shortly, which will summarise good and poor practices observed during our review. Once published, we expect all firms in the portfolio to analyse that paper closely and consider how they might further strengthen their own LRMFs.

Although clearing brokers are generally becoming stronger prudentially, further work is needed to ensure that all firms manage their risks adequately. There were still instances in the last two years where liquidity risk crystallised due to firms' risk management being deficient. Our strategic focus on prudential risk management will continue and we will undertake additional proactive work in this space.

Financial crime

There is an inherent risk that wholesale brokers may be used to execute trades which facilitate financial crime. Consequently, we maintain our focus on scenarios where wholesale brokers with weak controls may be used to launder money through capital markets. Due to these ongoing concerns, we undertook a multi-firm assessment of [Money Laundering Through the Markets](#) (MLTM) in our last strategy cycle, which built on the issues previously identified in our thematic review, [TR19/4](#)².

Our findings from the MLTM review were mixed. We observed improvements in certain risk assessment processes, better formalisation of governance and oversight frameworks for financial crime, and we also noted an improved collaboration between trade surveillance and trade monitoring teams. However, we are concerned that, too often, firms underestimate the money laundering risks to which they are exposed. As a result, some firms' business-wide risk assessments are incomplete and other firms do not have one at all, some firms fail to develop adequate methodologies for risk-rating their clients and activities appropriately, and some tend to rely on other parties within the transaction chain for due diligence where this is not appropriate.

¹ <https://www.fca.org.uk/publication/correspondence/wholesale-brokers-portfolio-letter-2023.pdf>

² <https://www.fca.org.uk/publication/thematic-reviews/tr19-004.pdf>

We expect firms to read our publication in full³, incorporate good practices and stop poor practices where relevant. For firms included in the multi-firm assessment, we will check whether our feedback and recommended actions were implemented appropriately.

Importantly, we find that weaknesses in anti-money laundering controls often go hand in hand with those for market abuse. For further guidance on the latter, firms should consider [Market Watch 62](#)⁴ where we shared our concerns about Personal Account Dealing (PAD) and [Market Watch 69](#)⁵ where we discuss firms' arrangements for market abuse surveillance, drawing on our observations from engaging with small and medium-sized firms.

Remuneration and broker misconduct

Appropriate and SM&CR-compliant remuneration arrangements at wholesale brokers are important and can affect the overall culture of a firm. When implemented well, they provide strong incentives for good conduct by front office staff as well as an effective deterrence against misconduct; when implemented poorly, they become one of the key drivers of harm for the portfolio. These harms can crystallise if, for example, the firm retains remuneration structures that were established prior to the introduction of the Remuneration Code, placing more emphasis on revenue generation and not enough on remuneration being used as a tool to address poor behaviour.

Unfortunately, we continue to observe an inconsistent application of the Remuneration Code across firms. At the most extreme end, some firms in scope of the rules have not yet implemented an appropriate remuneration policy; in other cases, firms skirt the rules on deferrals and non-cash variable remuneration, and their fixed and variable components of remuneration do not appear appropriately balanced.

As a result, we have asked firms identified as not having an appropriate remuneration policy in place to take immediate action to remediate this failing. We are also engaging directly with firms where it appears, from regulatory reporting, that they may not be adhering to the Remuneration Code requirements around the use of deferrals and the non-cash element of variable remuneration. Following this engagement, if firms identified still fail to take the necessary steps to remediate, we will use our regulatory tools, including imposing additional capital requirements to reflect the increased risk arising from poor remuneration practices. We remind Boards that we expect firms to adhere to the Remuneration Code at all times.

In addition to the rules themselves, we will also test whether remuneration is used as an effective disciplinary tool by firms to address broker misconduct, including non-financial misconduct (NFM). Regarding the latter, we were encouraged to see strong engagement with our recent NFM survey⁶ and we are planning further proactive work with firms on this topic.

Our strategy for the next two years

Given the uneven nature of progress made in areas which are of strategic importance to us, we will be focused particularly on ensuring that regulatory compliance and good standards of conduct are adhered to by all firms. To maintain a vibrant market for intermediaries, our aim is

³ <https://www.fca.org.uk/publications/corporate-documents/money-laundering-through-markets>

⁴ <https://www.fca.org.uk/publication/newsletters/market-watch-62.pdf>

⁵ <https://www.fca.org.uk/publications/newsletters/market-watch-69>

⁶ <https://www.fca.org.uk/news/press-releases/fca-publishes-results-non-financial-misconduct-survey>

to ensure that firms with a healthy and compliant culture are not put at a disadvantage to firms with a poor culture. Therefore, where firms have continuously failed to bring themselves up to the standards required, we will intervene using the regulatory tools at our disposal including, where relevant, Board effectiveness reviews, increased capital requirements, and business restrictions. This is to ensure that 'outlier' firms do not cause ongoing harm to the UK market and that healthy competition is maintained.

For the next two years, we have identified four strategic areas which will be the focus of our programme of proactive work. We will use a combination of regulatory reporting data analysis, proactive outreach, and incisive testing to assess and mitigate risks of harm. In addition to our usual proactive engagement with wholesale brokers, we will engage with other wholesale firms who deal with firms in the portfolio on a regular basis; this is to gain a better understanding of the value wholesale brokers bring to markets and how they are viewed by the users of their services.

Broker conduct

Brokers are the main revenue earners for their firms and are also the main points of contact for clients. These two factors mean that they hold significant bargaining power over their employer. Furthermore, brokers have access to sensitive and valuable information such as the overall supply-demand dynamics of the market, as well as the trading intentions of their clients. If not properly managed, these drivers of risk can lead to two types of harm. First, there is an inherent conflict of interest where a broker's personal interest might go against that of their client, preventing the latter from achieving best outcomes. Second, firms could be incentivised to actively ignore instances of misconduct if the broker engaging in misconduct (whether financial or non-financial) is also a significant revenue producer. Consequently, if there is inadequate oversight of front office activity, the sorts of risks that can crystallise include:

- Insider trading – for example, when brokers use non-public, material information to trade ahead of clients for personal gain.
- Market abuse, resulting from creating a false impression of market liquidity or price by unaccountable brokers. We have signalled our concern about 'flying and printing' on multiple occasions, most recently in [Market Watch 76](#)⁶ and previously in [Market Watch 57](#)⁷.
- Overcharging clients for order execution, particularly in more niche markets or markets where participants are less sophisticated.
- Abuse of gifts and entertainment so that trade flow is directed towards specific brokers/desks, in contravention of best execution requirements.
- Non-financial misconduct, where firms tolerate or turn a blind eye to discrimination, harassment and bullying by employees, particularly if they are 'star' brokers/performers.

Given this, we will be conducting targeted work to assess how firms manage their brokers. We expect firms to have suitable controls in place to detect misconduct and to take appropriate action against those found to be committing misconduct. If we identify material weaknesses in the frameworks governing broker conduct, we will take actions which may include restrictions placed on individual firms or enforcement action against firms or individuals.

⁶ <https://www.fca.org.uk/publications/newsletters/market-watch-76>

⁷ <https://www.fca.org.uk/publication/newsletters/market-watch-57.pdf>

Culture

Good conduct stems from good culture, and this starts with a strong tone from the top. From our supervisory experience, firms governed by diverse boards with a suitable mix of skills and experience, provide more effective challenge to management. This leads to better decision making and drives the success of firms, both commercially and culturally. Further, having executives with varied but relevant skillsets allows for different viewpoints and effective challenge and enables well considered decisions to be made. Conversely, more homogenous Boards and Management teams could succumb to “groupthink” and fail to understand adequately the nature of the firm’s business, leaving themselves open to significant risks, including from poor individual broker conduct.

Healthy workplace cultures are essential across all markets we regulate, which is why we launched the NFM survey in 2024 to understand better how firms identify, report, and investigate instances of NFM. We will use the survey results for further proactive engagement with the portfolio, with a strong focus on the ‘outlier’ firms from the survey data. In particular, with respect to those outlier firms, we will scrutinise (i) policies and procedures in place for reporting NFM concerns, including evidence of firms encouraging a good ‘speak up’ culture and giving staff confidence that they will be treated appropriately if they raise concerns, (ii) management of NFM cases by firms once they are reported by staff and (iii) processes for ensuring that fair outcomes are reached.

Business oversight

Whilst good culture is an important driver of good conduct, it needs to be complemented by a robust control environment. Firms need to have effective and comprehensive risk and control oversight frameworks to detect and prevent harm from occurring and penalise undesirable behaviour. We intend to test firms’ frameworks comprehensively through our proactive work on broker conduct. Apart from the usual detective and monitoring controls (e.g., trade and communications surveillance, client onboarding, monitoring of unsettled and/or failed trades and escalation processes), we will be particularly interested in the firms’ use of remuneration tools such as deferrals, clawback or malus in cases of proven misconduct. This is because we consider remuneration as a critical component of firms’ toolkit when dealing with brokers’ non-compliance, and we want to test whether firms are using these measures consistently across the portfolio.

Financial resilience

As mentioned earlier, although progress has been made by firms, prudential risks nevertheless remain. It is vital that wholesale brokers maintain adequate levels of capital and liquidity so that they are less likely to enter a disorderly wind-down and cause market disruption should they fail. We will therefore focus on ensuring that firms which were subject to our liquidity review have acted on our feedback and implemented good practices. More broadly, we will test wholesale brokers’ contingency funding plans and frameworks to assess whether firms’ plans are adequate for potential liquidity challenges caused by stress events. Overall, we expect firms to review their levels of liquidity continuously to ensure that they comply with the Investment Firm Prudential Regime (IFPR) at all times. Where we identify material weaknesses, we are likely to impose additional capital and liquidity requirements.

Next steps

As CEO, the Senior Managers and Certification Regime makes you responsible for ensuring that relevant staff at your firm understand our rules and principles for businesses and for ensuring that your firm complies with them. If you are not meeting those rules and standards, you must notify the FCA immediately, setting out what you are doing to remedy any breaches.

By the end of March 2025, we expect all CEOs to have discussed this letter with their fellow directors and/or Board and to have agreed actions and/or next steps.

If you have any questions about this letter, please contact your named supervisor, if your firm has one. If you do not have a named supervisor, please contact us on 0300 500 8082 which is the primary contact for your firm's day-to-day interactions with the FCA. Further details of how we can be reached are available on our website. We recognise there may be occasions when your firm faces urgent issues of strategic importance. Therefore, if those circumstances do arise, please contact either your named supervisor or the Manager of the Wholesale Brokers Flexible Supervision Team, Maciej Wroblewski at Maciej.Wroblewski@fca.org.uk.

We look forward to working with the sector to continue improving standards and market outcomes for you and your customers.

Yours faithfully,

Mark Francis – Interim Director, Wholesale Sell-Side