



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY



Consultation Paper | FCA CP16/10
| PRA CP14/16

Proposed Implementation of the Enforcement Review and the Green Report

This Consultation Paper (CP) includes proposed changes to the FCA's Decision Procedure and Penalties Manual and Enforcement Guide.

Chapters 3 and 4 of this CP, which consult in respect of regulator cooperation (FCA and PRA) and subjects' understanding and representations in the context of Enforcement Investigations, are the subject of a joint consultation by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA).

*** April 2016

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We are asking for comments on this Consultation Paper by 14 July 2016.

You can send them to us using the form on our website at: www.the-fca.org.uk/cp16-10-response-form.

Or in writing to:

Law and Policy Team
Enforcement and Market Oversight Division
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Telephone: 020 7066 0220

Email: cp16-10@fca.org.uk

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This Consultation Paper does not propose any changes to the PRA Rulebook.

Please address responses, comments or enquiries by 14 July 2016 to:

Ref: CP14/16
Regulatory Action Division,
Prudential Regulation Authority
20 Moorgate
London EC2R 6DA

Email: CP14_16@bankofengland.co.uk

Abbreviations in this document

CMA	Competition and Markets Authority
CP	Consultation Paper
DEPP	Decision Procedure and Penalties Manual
EG	Enforcement Guide
EMO	Enforcement and Markets Oversight
FCA	Financial Conduct Authority
FEMR	Fair and Effective Markets Review
FSA	Financial Services Authority
HMT	Her Majesty's Treasury
PIR	Preliminary investigation report
PRA	Prudential Regulation Authority
RAD	Regulatory Action Division
RDC	Regulatory Decisions Committee
UKLA	UK Listing Authority

1. Overview

Introduction

- 1.1** On 18 December 2014, HM Treasury (HMT) published its 'Review of enforcement decision-making at the financial services regulators' (hereinafter referred to as 'the HMT Review' or 'the Review').¹ The focus of the Review was on the transparency, fairness, effectiveness and speed of the FCA's and the PRA's enforcement decision-making processes.
- 1.2** The HMT Review acknowledged that both regulators had delivered strong enforcement action. It made a number of recommendations to the FCA and the PRA with the aim of improving current decision-making processes and arrangements.
- 1.3** The FCA and the PRA intend to implement these recommendations. As the recommendations have been made across the full lifecycle of an enforcement case, and vary in nature, the regulators will use a variety of tools to implement them. This paper sets out the regulators' response to some of the recommendations and proposals for implementation.
- 1.4** On 19 November 2015, the PRA and the FCA published two reports: (1) A joint report into the failure of HBOS plc; and (2) Andrew Green QC's Report into the FSA's enforcement actions following the failure of HBOS ('the Green Report').²
- 1.5** The Green Report made four recommendations, three of which are relevant to the HMT Review recommendations. They cover: (1) pre-referral decision-making, (2) ongoing dialogue between enforcement and supervision during an investigation, and (3) informing the subject of an investigation about the matters under investigation.
- 1.6** This CP incorporates the PRA and FCA's proposals for implementing recommendations (2) and (3) in Chapters 3 and 4. Chapter 2 explains the PRA and FCA's implementation at an operational level of recommendation (1).
- 1.7** The final recommendation of the Green Report (recommendation (4)) in relation to internal meeting minutes has already been adopted and implemented by the PRA and the FCA at an operational level.³
- 1.8** This CP follows the same order as the HMT Review:
 - Chapter 2 deals with referral decision-making recommendations in the HMT Review (FCA) and Green Report (PRA and FCA).

1 Available online at: www.gov.uk/government/uploads/system/uploads/attachment_data/file/389063/enforcement_review_response_final.pdf.

2 See online at: www.bankofengland.co.uk/publications/Pages/news/2015/086.aspx and www.fca.org.uk/news/publication-of-hbos-failure-review.

3 See Recommendation 4: Accuracy of ExCo minutes at p.92 (Appendix E: Recommendations).

- Chapter 3 deals with cooperation between the regulators in enforcement investigations, addressing both HMT Review and Green Report recommendations (PRA and FCA).
- Chapter 4 deals with subjects' understanding and representations in joint enforcement investigations, addressing both HMT Review and Green Report recommendations (PRA and FCA).
- Chapter 5 deals with settlement (FCA).
- Chapter 6 deals with contested decision-making (FCA).
- Annex 1 lists the questions in this CP (PRA and FCA).
- Annex 2 sets out our compatibility statement in relation to the proposed changes (PRA and FCA).
- Appendix 1 sets out our proposed amendments to the text of Decision Procedure and Penalties Manual (DEPP) and Enforcement Guide (EG) (FCA).

PRA and FCA consultation

- 1.9** Chapters 3 and 4 of this CP consult on cooperation between the FCA and PRA in enforcement investigations and subjects' understanding and representations in relation to such investigations. These matters are the subject of a joint consultation by the FCA and PRA, as the regulators consider that it is appropriate to consult together in respect of regulator cooperation and investigations.

FCA-only consultation

- 1.10** As indicated above, Chapters 2, 5 and 6 are FCA-only proposals. When the FCA published the revised DEPP and EG in July 2007, it confirmed that it would consult on any material changes it proposed to make to EG (even though EG, unlike DEPP, is not part of the FCA's Handbook and is not therefore subject to statutory consultation requirements).
- 1.11** The recommendations fall generally into three categories based on the appropriate method of implementation:
- Those that do not need changes to EG or DEPP and can be implemented within 'business as usual' processes (e.g. implementation through information published in the Annual Report or on the website, or by embedding in existing oversight arrangements).
 - Those that need only clarification or minor amendments to EG and DEPP. These do not require consultation but we have included them in this paper for completeness.
 - Those that require material changes to DEPP and EG and therefore need formal consultation.
- 1.12** The HMT Review focused on regulatory enforcement cases, and in particular on disciplinary cases. It noted that, while certain recommendations will also apply to regulatory market abuse investigations, they will be less relevant to criminal investigations and civil litigation conducted

by regulators, such as unauthorised business and criminal insider dealing cases. For that reason, there will be some enforcement cases where it would not be efficient or appropriate to adopt the processes developed in response to the Review.

Additional PRA consultation

- 1.13** The PRA will be consulting separately on the settlement and contested decision-making recommendations (Chapters 5 and 6 of the HMT Review) later this year, once the Bank of England and Financial Services Bill has passed through Parliament.⁴ The reforms proposed by the new Bill will effect certain changes to the Bank's corporate governance structure, including the change from the PRA being a subsidiary of the Bank of England to the creation of a new committee at the Bank of England, to be known as the Prudential Regulation Committee (PRC).
- 1.14** The PRA is also planning to publish its enforcement referral framework (Chapter 2 of the HMT Review). It plans to do so alongside its implementation of the other HMT Review recommendations.

Who does this consultation affect?

- 1.15** This consultation will be of interest to all firms and individuals involved in providing financial services. It will be of particular interest to all firms and individuals (and their professional advisers) that are, or expect to be, subject to FCA and/or PRA enforcement action. It may also be of general interest as it builds on our existing statements about our use of enforcement powers.

Is this of interest to consumers?

- 1.16** This consultation does not directly affect consumers. However, as these proposals concern the transparency of the FCA's approach to enforcement decision-making and its enforcement process, they may be of general interest to consumers and the organisations which represent them.

Equality and diversity considerations

- 1.17** We have assessed the likely equality and diversity impacts of the proposals and do not think they give rise to any concerns, but we would welcome your comments.

Next steps

- 1.18** Please provide your comments by 14 July 2016. We will publish feedback on responses and issue a Policy Statement once we have reviewed your comments.

⁴ See online at: <http://services.parliament.uk/bills/2015-16/bankofenglandandfinancialservices.html>.

2. Referral decision-making

- 2.1** This chapter consults on the FCA's proposed implementation of the HMT Review and Green Report recommendations relating to referral decision-making. As explained above at paragraph 1.14, the PRA will be publishing its enforcement referral framework alongside its implementation of the other HMT Review recommendations. This chapter also includes an account of the PRA's proposed adoption of recommendation (1) in the Green Report.

The Green Report recommendation

- 2.2** The Green Report recommended that before making a referral in connection with a particular set of events, the regulators should identify each firm or individual in respect of whom the statutory threshold test for conducting an investigation is met in respect of those events. It also recommended that the regulators should create a record of the potential subjects of investigation so identified.⁵
- 2.3** The Report stated that the regulators should then decide, by considering the referral criteria, which if any of the potential subjects should, in fact, become the subject of an investigation, and that the regulators should record the reasons why each potential subject was being referred, or not being referred, for investigation. The Report recommended that an identified individual, at an appropriate level of seniority, should be made responsible for the pre-referral decision-making process (i.e. from the point in time at which a referral is being considered), and in particular, for determining the subject(s) for referral and the scope of that referral ('the referral decision-maker').

PRA

- 2.4** As indicated above, the PRA will be publishing its enforcement referral framework later this year. In the interim, the PRA proposes to adopt recommendation (1) in the Green Report in respect of its current internal referral processes from supervision to the Regulatory Action Division (RAD).
- 2.5** RAD will continue to advise supervision by setting out the background to the alleged misconduct, and providing a view as to whether there are grounds to make a referral, but the referral analysis should be structured so as to (1) identify up front in respect of which firms and individuals the threshold for launching an investigation appears to be met, and then (2) apply the referral criteria to each potential subject.

⁵ See Recommendation 1: Pre-referral decision-making at p.91 (Appendix E: Recommendations).

- 2.6** The PRA's normal approach is that the decision to make a referral from supervision to RAD is a joint decision of the Head of RAD and the Head of Division or Director of the supervisory area concerned, who together constitute the referral decision-maker. This ensures that decisions to open investigations are taken at a suitable level of seniority within the PRA.

FCA

- 2.7** The FCA has built on the referral decision-making process that is described in Box 2.C in the HMT Review, and has amended the Enforcement Referral Document to include a table that sets out all potential subjects, a summary of the circumstances and reasons why a firm or individual is or is not being referred. The FCA ensures that the appropriate seniority of decision-making is maintained by having a Head of Department sign the Enforcement Referral Document.

The HMT Review recommendations

- 2.8** The aim of the HMT Review's referral recommendations was to ensure consideration of the full range of regulatory options at a senior level, with a focus on identifying and implementing the right regulatory response and consistency of decision-making. The HMT Review noted that at the time it was published the FCA had recently revised its decision-making framework and was reviewing the referral criteria. This chapter sets out the FCA's proposals for the remaining referral recommendations.

The purposes of enforcement

- 2.9** The HMT Review recommended that the FCA publish referral criteria which:
- explicitly consider whether an enforcement investigation, rather than an alternative regulatory response, is the right course in all of the circumstances and
 - reflect the various objectives of their enforcement action, including its strategic purpose in publicly reinforcing the regulatory requirements in priority areas.
- 2.10** In July 2015, in response to the HMT Review, the FCA published revised referral criteria. These criteria set out a range of factors we consider when deciding whether to appoint enforcement investigators. When we open an investigation, we have not decided that there have been breaches, nor what type of enforcement action, if any, should be taken if it turns out that there have been. In deciding whether an enforcement investigation is likely to further the FCA's aims and objectives, the FCA considers factors including the following:
- the strength of the evidence and the proportionality and impact of opening an investigation
 - the purpose or goal that would be served if the FCA were to end up taking enforcement action in the case and
 - relevant factors to assess whether the purposes of enforcement action are likely to be met, e.g. changing behaviour and raising standards in the industry

The FCA will amend EG to reflect the new referral criteria and case selection approach.

- 2.11** The FCA does not propose to amend the paragraphs in EG that explain its approach to referring to enforcement cases about breaches of the Threshold Conditions or unauthorised business cases. This is because the FCA's starting point in those cases is different from other regulatory discipline cases. If the problem cannot be fixed swiftly, the FCA cannot disregard cases where it appears that the Threshold Conditions have been breached as these are fundamental requirements for authorisation. As such, the same issues of prioritisation and (occasionally) appointment of investigators do not arise, and the FCA will generally take action in all such cases that come to its attention and which cannot be resolved using supervisory tools. In assessing which unauthorised business cases to take on, the FCA's primary focus is to seek to ensure that consumers are protected from unregulated business. It is the risk of or actual consumer harm which drives decisions as to whether the FCA should take enforcement action (rather than other prosecuting and investigating agencies).
- 2.12** In relation to the FCA's UK Listing Authority (UKLA) and non-criminal market abuse investigations, the FCA proposes to amend EG to clarify that, although the revised referral criteria do not directly apply to such cases, it will bear them in mind when deciding whether to open such an investigation.
- 2.13** However, given the often limited alternatives to enforcement action available to address market abuse (with many of the subjects typically unauthorised), the FCA will give greater emphasis to the seriousness and deterrence value of a particular case when making such decisions.
- 2.14** Similarly, many, if not all, of the tools other than enforcement are not available in the context of listing regime breaches:
- Other than in certain niche areas (sponsors, primary information providers), when the FCA is acting as the UKLA it has a very different regulatory relationship with those against whom it may wish to take enforcement action. While breaches will generally involve actions by listed companies (or their directors), the fact that they are listed does not mean that there is an ongoing supervisory relationship with them; as such, the possibility for use of early intervention-type tools is not available.
 - While the listing regime provides for the FCA to pre-approve eligibility for official listing, it is not an authorisation regime and so as such it cannot restrict permissions (other than to a very limited extent within the sponsor regime). Thus, the possibility of preventing or restricting certain activities is limited.
 - The scope of the skilled person regime is also limited, covering only regulated firms rather than listed companies. The FCA has used it in the context of listing breaches, but only in considering the actions of sponsor firms that are regulated entities.
 - While the listing regime does provide the ability to enforce against directors that are knowingly concerned in breaches, the regime is not one that approves individuals and so does not include, for example, a fit and proper test.
- 2.15** As the HMT Review notes, the FCA already provides examples of cases where the firm's or individual's cooperation and subsequent remedial action have been a significant factor in the decision that formal enforcement action is not the right regulatory response.
- 2.16** The HMT Review recommended that the FCA should provide further examples of cases in which a firm's response to a breach of the regulatory requirements has been a factor in deciding not to take enforcement action.

- 2.17** The FCA will try to identify additional useful examples to publish on its website. However, some cases do not get referred because supervisory tools are a better choice in a particular case for a number of reasons (which may include cooperation, but may be equally driven by other factors). Additionally, some cases are so serious that it would be inappropriate not to seek some form of disciplinary outcome, and such cases would be referred. Given that the FCA expects cooperation from regulated firms and approved individuals, there should be a degree of cooperation in all cases. The focus will therefore be on identifying those cases where the significant extent of cooperation was a large factor in deciding not to refer a case to enforcement.

Identifying the right regulatory response

- 2.18** HMT Review's recommendations centred on the existence of a referral decision-making framework that promotes:
- consideration of appropriate alternative regulatory responses
 - referral to enforcement only where that is considered to be the appropriate regulatory response and
 - consistency of approach to referral decision-making.
- 2.19** The Review concluded that the present FCA framework should improve governance, promote good supervision and enforcement coordination and assist in evaluating and identifying the appropriate regulatory response. The Review recommended that the FCA should regularly review the performance of its Steering Groups and their composition, and ensure appropriate expertise and seniority of representation.
- 2.20** The Review also recommended that, along with publishing referral criteria, the FCA should publicly articulate its approach to taking these decisions, whilst noting that it should retain the flexibility to make operational adjustments as appropriate.
- 2.21** As noted above, in July 2015, the FCA also published a summary of the referral process and framework in response to the Review, which explained how Enforcement and Markets Oversight (EMO) and Supervision work together in the enforcement referral process to identify the right regulatory response. The overarching question asked in that process is 'is an enforcement investigation likely to further the FCA's aims and objectives'. That framework will continue to be kept under review.

Transparency of enforcement activities

- 2.22** The HMT Review recommended that the FCA continue to publish information about its enforcement activities to enhance transparency, and explore how better information might be provided. It recommended that:
- information should also extend to early intervention work, where enforcement and supervision staff work together to persuade firms to take action to address risk

- the FCA's Annual Report should clearly state the enforcement action that it has taken in priority areas, whether in opening investigations or through formal outcomes and
- the FCA should also publish information following thematic reviews, to explain – generally, and without identifying firms – why certain cases were referred for investigation but others were not.

2.23 The Fair and Effective Markets Review (FEMR) also called for increased publicity about the successful use of early intervention work, especially where this would help ensure firm- or scenario-specific lessons are learnt.

2.24 The Enforcement Annual Performance Account will continue to publish information about disciplinary outcomes, including cases where no further action was taken, and the number of cases opened during that year and their related issues such as client assets, integrity, mis-selling etc.

2.25 The FCA will endeavour to publish more information about early intervention work, either at the end of a specific case or from thematic reviews, where it is legally able to do so. However, FEMR has identified a difficulty in doing this. This is that publication needs to be done in ways which ensure that appropriate firm confidentiality is maintained, so as not to impact on the willingness of firms to cooperate with regulators in such scenarios. The FCA will need to balance providing enough detail so that firms can learn meaningful lessons from these examples with the need to maintain confidentiality, and in particular with thematic reviews, to ensure that the effect of any publicity does not identify those under investigation through details of which firms are not under investigation.

2.26 The recommendation for the FCA to explain why certain cases were referred for investigation specifically notes that such explanation should not identify firms. There is no change to the policy of not normally making public whether or not a particular matter is under investigation unless there are exceptional circumstances (see Chapter 6 of EG for further details). In addition, the Regulatory Decisions Committee (RDC) process is confidential, to help operate a fair process and ensure compliance with the statutory restrictions on publishing information relating to statutory notices.

2.27 The FCA welcomes views on different vehicles for publication and suggestions about the level of detail that firms and others interested in the approach to early intervention would find useful, while avoiding the pitfalls described above.

Q1: *Do you agree with this approach to referral decision-making?*

Q2: *Do you have any comments on the proposed implementation of the Green Report?*

3.

Cooperation between the regulators in enforcement investigations

- 3.1** This chapter sets out our proposals for implementing the Review's recommendations on the way the FCA and the PRA work together on joint- or dual-regulated firm investigations and related investigations concerning individuals.
- 3.2** The high-level framework for cooperation between the FCA and the PRA is set out in the 'Memorandum of Understanding (MoU) between the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA)', which the regulators are required to prepare and maintain under section 3E of FSMA.⁶ The MoU acknowledges that the two authorities have separate and independent mandates which are set out in statute, and states that while it is important that this is respected, it is also essential that the regulators coordinate in some areas and cooperate in others.⁷
- 3.3** It notes that under FSMA, the FCA's responsibility is broadly:
- regulating standards of conduct in retail and wholesale markets
 - supervising trading infrastructures that support those markets
 - the prudential supervision of firms that are not PRA-regulated and
 - the functions of the UKLA.
- 3.4** The FCA has a single strategic objective to ensure that the markets for financial services function well. Three operational objectives support this: securing an appropriate degree of protection for consumers (including wholesale consumers); protecting and enhancing the integrity of the UK financial system; and promoting effective competition in the interests of consumers in the markets for financial services.⁸
- 3.5** The PRA is responsible under FSMA for the authorisation (in conjunction with the FCA) and prudential supervision of individual deposit-takers (including banks, building societies and credit unions), insurers (including friendly societies), and certain designated investment firms. Its general objective is to promote the safety and soundness of PRA-authorised persons. It is required to advance this objective, primarily by:
- seeking to ensure that the business of PRA-authorised persons is carried on in a way which avoids any adverse effect on the stability of the UK financial system

⁶ See online at www.fca.org.uk/your-fca/documents/mou/mou-between-the-fca-and-the-pracoordination and in the PRA section of the Bank of England website at: www.bankofengland.co.uk/pr/Pages/regulatorydata/workingwithfca.aspx.

⁷ Para.2 of the MoU.

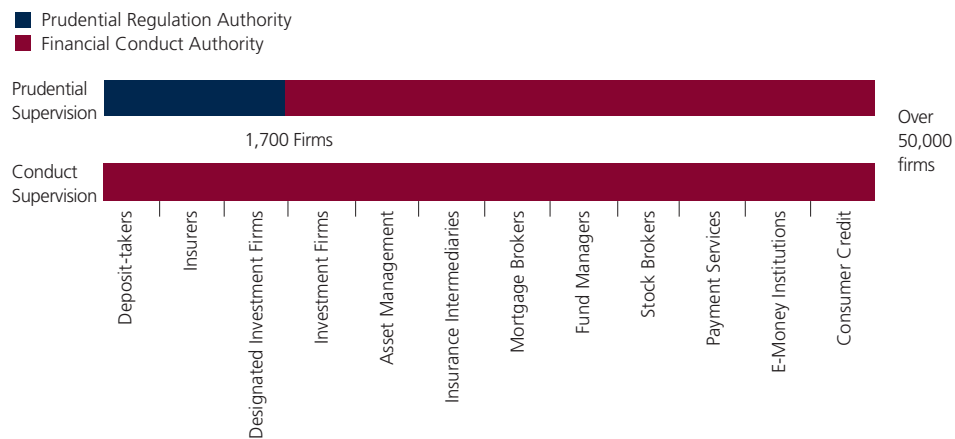
⁸ Paras.3–4 of the MoU.

- seeking to minimise the adverse effect that the failure of a PRA-authorized person could be expected to have on stability and
- discharging its general functions in relation to ring-fencing in a way that seeks to ensure that the business of ring-fenced bodies:
 - is carried on in a way that avoids any adverse effect on continuity of provision of core services (which may, in particular, result from the disruption of the continuity of financial services) and
 - is protected from risks that could adversely affect this continuity

It is also required to seek to minimise the risk that the failure of a ring-fenced body (or a member of a ring-fenced body's group) could affect the continuity of the provision in the UK of core services.⁹ In the case of insurers, the PRA has the additional objective of contributing, through its prudential supervision of insurers, to securing an appropriate degree of protection for policyholders.¹⁰

3.6 When discharging its general functions in a way that advances its objectives, the PRA must also, so far as is reasonably possible, act in a way that facilitates effective competition in the markets for services provided by PRA-authorized persons in carrying on regulated activities.¹¹

3.7 The following diagram, which was originally contained in the PRA's Annual Report and Accounts 2015, illustrates the split of regulatory responsibilities between the PRA and the FCA. It highlights the sector of the regulated population where joint enforcement investigations can potentially occur:¹²



Note: This is not to scale of number of firms

3.8 The section of the MoU entitled 'Formal regulatory processes and enforcement' (paragraphs 41–52) covers consultation between the regulators in relation to enforcement cases and other regulatory actions. It also covers more general information-sharing in the context of any significant public communications about either of the regulators' general approach to enforcement or related policy that may materially affect the other's objectives.

⁹ Section 2B of FSMA ('The PRA's general objective').

¹⁰ Para.5 of the MoU.

¹¹ Section 2H of FSMA ('Secondary competition objective and duty to have regard to regulatory principles').

¹² See Figure 7: 'Stylised illustration of the split of regulatory responsibilities between the PRA and FCA', p.19, online at: www.bankofengland.co.uk/publications/Documents/annualreport/2015/prareport.pdf

- 3.9** The detail of coordination of formal regulatory processes and of enforcement and legal intervention is set out in Annex 1 to the MoU. The section of that Annex titled 'Enforcement and legal intervention' ('(vi)') applies to firms that are either dual-regulated, or a member of a group that includes a PRA-authorized firm.¹³ It provides that, when contemplating the appointment of enforcement investigators in respect of such a firm, the FCA and the PRA will notify one another to allow each to analyse the impact of the proposed action on its statutory objectives.¹⁴ If the issue affects advancement of both PRA and FCA objectives, the regulators will determine whether an enforcement investigation against the firm and/or relevant individuals should be carried out by the FCA, the PRA or both jointly, and how to coordinate any investigation and subsequent proceedings. Where the PRA or the FCA proceeds with the investigation on its own, they must keep the other regulator regularly updated on 'material aspects of the progress of the investigation'.¹⁵
- 3.10** The MoU also requires the FCA and the PRA to consult one another when they have reached a view in principle about an action which might lead to a warning notice or decision notice, but before they have taken a formal decision to issue this notice.¹⁶ The FCA and the PRA also notify one another in cases involving proposed civil or criminal proceedings when they have reached a view in principle and before they have taken a formal decision to issue proceedings.¹⁷ Each regulator also notifies the other before issuing a press release involving enforcement action or legal proceedings against a firm that is dual-regulated or a member of a group that includes a PRA-authorized firm.¹⁸
- 3.11** In addition to the main MoU between the PRA and the FCA, there is also a specific MoU that sets out the roles of the regulators in regulating and supervising with-profits policies.¹⁹ Again, this MoU provides that each regulator will notify the other in advance of any proposed legal or regulatory action or supervisory intervention that appears likely to be materially relevant to the other regulator's objective(s).²⁰
- 3.12** In respect of completed enforcement cases, as at the date of the publication of this CP, the FCA and PRA had published 'joint' disciplinary outcomes in respect of three cases. Two case studies are set out below:
- 1) Case study 1:** The action taken against **Royal Bank of Scotland Plc, National Westminster Bank Plc, and Ulster Bank Ltd** in November 2014 for IT failures that resulted in those banks' customers being unable to access banking services in June and July 2012,²¹ due to an outage of a number of customer-facing IT systems.²² The banks are regulated by the PRA for prudential purposes and by the FCA for conduct matters.

In April 2013, the PRA and the FCA agreed to undertake a joint investigation into the IT outage. This was the first time that the regulators decided to take joint enforcement action. The FCA and the PRA considered a joint investigation necessary because the failings

¹³ See paras.19–27 of Annex 1 to the MoU ('Regulatory processes, enforcement and legal intervention').

¹⁴ See para.23 of Annex 1.

¹⁵ See para.24 of Annex 1.

¹⁶ See para.25 of Annex 1.

¹⁷ See para.26 of Annex 1.

¹⁸ See para.27 of Annex 1.

¹⁹ See 'With-Profits, Memorandum of Understanding' online at: www.bankofengland.co.uk/about/Documents/mous/prastatutory/mouwithprofits.pdf.

²⁰ At para.35 of the above.

²¹ Disruption to the majority of RBS and NatWest systems lasted until 26 June 2012, and Ulster Bank systems until 10 July 2012. Disruptions to other systems continued into July 2012.

²² See PRA Press release online at: www.bankofengland.co.uk/publications/Pages/news/2014/152.aspx and FCA Press release online at: www.fca.org.uk/news/fca-fines-rbs-natwest-and-ulster-bank-ltd-42m-for-it-failures.

included both conduct and prudential issues, and so had implications for both regulators' statutory objectives. In particular, the issues engaged:

- the PRA's general objective of promoting the safety and soundness of PRA-authorized persons
- the FCA's overarching strategic objective of ensuring that the relevant markets function well and the advancement of the FCA's operational objectives of: (i) securing an appropriate degree of protection for consumers; and (ii) protecting and enhancing the integrity of the UK financial system

The conduct of the PRA's investigation (including gathering and analysing evidence and interviews) was outsourced to the FCA.²³ During the course of the investigation, the FCA and the PRA held regular meetings²⁴ to ensure that both regulators were always kept up to date about the progress of the investigation.

The FCA imposed a financial penalty on the banks of £42 million and the PRA imposed a financial penalty of £14 million. These penalties were for the banks' failure to have adequate systems and controls to identify and manage their exposure to IT risks between 1 August 2010 and 10 July 2012, in breach of Principle 3 of the Principles for Businesses (Principle 3 states that a firm must take reasonable care to organise its affairs responsibly and effectively, with adequate risk management systems). The banks agreed to settle at an early stage of the joint investigation and therefore qualified for a 30% (Stage 1) discount under the regulators' executive settlement procedures. Were it not for this discount, the FCA would have imposed a financial penalty of £60 million and the PRA a financial penalty of £20 million.²⁵

- 2) Case study 2:** The action taken against **The Co-operative Bank Plc** ('Co-op Bank' or 'the Firm') in August 2015 resulted in a public censure being issued by both the PRA and the FCA for failing to deal with the regulators in an open and cooperative manner (PRA/FCA), serious risk management failings (PRA), and a breach of the Listing Rules (FCA).²⁶ As with the first case above, Co-op Bank is regulated by the PRA for prudential purposes and by the FCA for conduct matters.

In January 2014, the FCA and the PRA agreed to undertake a joint investigation into potential breaches of Principle 11 of the Principles for Businesses, which provides that a firm must deal with its regulators in an open and cooperative way. The regulators considered a joint investigation necessary because the potential breaches included both conduct and prudential issues and so had implications for both regulators' statutory objectives. As in the first case above, the potential breaches were considered relevant to:

- the PRA's general objective under section 2B(3)(a) of FSMA
- the FCA's overarching strategic objective of ensuring that the relevant markets function well and the advancement of the FCA's operational objectives of: (i) securing an

²³ See further section entitled 'Outsourcing enforcement investigations' on the PRA's website: www.bankofengland.co.uk/pr/Pages/supervision/regulatoryaction/enforcement.aspx.

²⁴ Including by teleconference.

²⁵ See PRA Final Notice online at: www.bankofengland.co.uk/pr/Documents/supervision/enforcementnotices/en201114.pdf. See FCA Final Notice online at: www.fca.org.uk/your-fca/documents/final-notices/2014/rbs-natwest-ulster

²⁶ See PRA Press release online at: www.bankofengland.co.uk/publications/Pages/news/2015/066.aspx and FCA Press release online at: www.fca.org.uk/news/fca-censures-the-co-operative-bank-for-listing-rules-breaches.

appropriate degree of protection for consumers; and (ii) protecting and enhancing the integrity of the UK financial system

The enforcement investigation followed a similar course to the first case, with regular meetings between the regulators and regular (approximately monthly) meetings between the Head of the PRA's Regulatory Action Division and the responsible FCA Head of Department to set the strategy for the investigation and monitor progress.

Following the joint investigation, the regulators found that the Firm had fallen short of its responsibility to be open and cooperative with its regulators, as required by Principle 11, by failing to notify the regulators of intended changes to two senior positions, and the reasons for those changes.

Separately, and in addition to the joint investigation, the PRA found that Co-op Bank had failed to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management controls during the period 22 July 2009 to 31 December 2013, in breach of Principle 3 of the Principles for Businesses. The FCA also found that for the period 21 March to 17 June 2013, Co-op Bank had breached the FCA's Listing Rule 1.3.3R, which prohibits publishing misleading information.

The regulators considered the above breaches to be sufficiently serious to warrant a substantial penalty and would otherwise have imposed a financial penalty.²⁷ However, the regulators concluded that in the exceptional circumstances of the case a censure should be issued.²⁸

- 3.13** The PRA proposes to include a high-level description of the process in joint PRA/FCA investigations in the enforcement section of the PRA website ('Supervision, Regulatory Action').²⁹

Involvement of supervisors during the investigation phase

HMT Review Recommendations:

- Rec. 9** Given the importance of consultation and coordination between the regulators, updates between the FCA and PRA on enforcement investigations should generally involve representatives from the enforcement and supervisory teams of both regulators, to promote symmetry of information.
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- Rec. 10** It is also important that the information does not just flow in one way, and that supervisors are similarly encouraged to bring information to the attention of investigators, where that information might potentially be relevant, for example, to the scope of the investigation. Potentially material information should be communicated promptly, and shared on an ad hoc basis, outside of formal updates, when appropriate.
-

²⁷ The PRA's Final Notice made clear that the PRA would have imposed a financial penalty of approximately £121m on Co-op Bank. This would have been reduced to £85.3 million through the application of the 30% discount because the PRA reached settlement with the firm at Stage 1.

²⁸ See PRA Final Notice online at: <http://www.bankofengland.co.uk/pr/Documents/supervision/enforcementnotices/en110815.pdf> and FCA Final Notice at: <http://www.fca.org.uk/your-fca/documents/final-notices/2015/the-co-operative-bank-plc>

²⁹ See online at: <http://www.bankofengland.co.uk/pr/Pages/supervision/regulatoryaction/default.aspx>.

- 3.14** The HMT Review recommended that updates between the FCA and the PRA on enforcement investigations should generally involve representatives from the enforcement and supervisory teams of both regulators, to promote symmetry of information, and that supervisors should be encouraged to promptly bring potentially relevant information to the attention of investigators.

Green Report Recommendation:

- 3.15** The Green Report recommended that following a referral to enforcement, the referral decision-maker should meet regularly with supervision and a representative of the Enforcement Investigation case team. It indicated that the appropriateness of the scope of the ongoing investigation should be discussed during that meeting, and that in particular, consideration should be given to: (1) any matters that have arisen that might require the scope of the investigation to be reconsidered; and (2) whether there are other subjects in respect of whom the statutory threshold test for conducting an investigation are met and, if so, which potential subjects should be investigated by reference to the referral criteria.³⁰
- 3.16** The report recommended that such meetings should take place at least quarterly and should be recorded. It stated that a record should be made of the reasons why any new potential subject is either being referred, or is not being referred, for investigation.

Proposed implementation of both the HMT Review and Green Report Recommendations

- 3.17** Under the main MoU between the FCA and the PRA, both regulators have agreed that if one regulator considers that information it has gathered would be of material interest to the other, it will actively offer such information to the other.³¹ This is not limited to enforcement matters and enforcement teams, but also includes supervision.³² At the working level, the PRA and the FCA investigation teams have the primary responsibility to keep each other and their respective supervisory teams regularly informed about the investigation's progress. They will aim to update each relevant supervisor at least every two weeks in line with the regular updates between the two regulators about the progress of the investigation, as well as any necessary ad hoc updates.
- 3.18** The FCA and the PRA monitor the effectiveness of their coordination by measuring their performance in a number of areas through detailed quarterly reports to senior management. Regular and more frequent updates take place at senior management level, including the quarterly meetings of senior officials from the FCA and the PRA responsible for enforcement and legal intervention or other regulatory action (see para.47 of the MoU), and at a working level, for example, between PRA/FCA enforcement liaison teams.
- 3.19** In the specific enforcement context, both regulators consider that cooperation and coordination on enforcement issues is working well. However, they will continue to keep the MoU and the day-to-day effectiveness of these arrangements under review.
- 3.20** The Financial Service Authority's 'Enforcement Process Review: Report and Recommendations' ('the Strachan Review'),³³ published in July 2005, had previously examined supervisors involvement during the investigation phase, and concluded that this was an area in which it would be counterproductive to attempt to be too prescriptive.³⁴

³⁰ See Recommendation 2: ongoing dialogue between enforcement and supervision during an investigation at p.91 (Appendix E: Recommendations).

³¹ Para.7 of the MoU.

³² See 'Information sharing: general' section of the MoU at paras.6–12.

³³ See online at: www.fsa.gov.uk/pubs/other/enf_process_review_report.pdf.

³⁴ At p.30 of the Strachan Review, para.5.15.

- 3.21** The Strachan Review noted that throughout the investigation, the channel of communication for matters relating to the investigation will be from the case team to the firm or individual concerned. It noted it was nonetheless important that the supervisor was kept informed of the investigation's progress, and consulted in advance if there were significant developments or changes – unless there were very good reasons not to do this. The Review explained that this was both to ensure that any relevant history was made available to the case team and also that any implications for the continuing supervision of the firm were taken into account.³⁵
- 3.22** This approach has been adopted by the PRA and the FCA, and continues to be the interaction used between enforcement and supervision. The PRA Annual Report and Accounts 2015 noted that: 'Coordination between supervisory and specialist teams [which includes the Regulatory Action Division] in both the FCA and PRA has seen continual improvement over the reporting period and no substantive breaches of the MoU have been reported'.³⁶
- 3.23** In terms of future changes to RAD's processes, the PRA proposes the following:
- the PRA investigation team will, at the outset of an investigation, diarise a quarterly meeting, which will be attended by the member of RAD management who made the decision to refer the case to enforcement, the Head of the referring supervisory area and a representative of the PRA investigation team
 - the meeting will have a standing agenda to discuss: (i) progress in the case, (ii) a review of the appropriateness of the proposed scope of, or continuing with, the investigation and (iii) a review of any potential new subjects arising for investigation
 - minutes of the meeting will be taken by the PRA investigation team, and, in particular, will record any discussion of further potential subjects for investigation (if any), and reasons for concluding that the investigation should, or should not, be extended to them.
- 3.24** The FCA's supervision and enforcement already liaise to a significant degree:
- the FCA proposes to put those meetings on a more formal basis by arranging for enforcement Heads of Department to meet at least quarterly with a member of the investigation team and representatives of supervision
 - the FCA is arranging for the issue of the appropriateness of scope (including whether to continue with the investigation, or increase or narrow the scope of the investigation in relation to the subject already under investigation), and a review of whether any new subjects should be referred for investigation, to be a standing item on the meeting's agenda
 - minutes of that meeting will be recorded, which will record the discussion and decisions made at that meeting.

Q3: *Do you agree with the approach outlined above? Are there any particular adjustments that you consider should be made in relation to the process of involving supervisors in the investigation phase?*

³⁵ At p.31 of the Strachan Review, para.5.16.

³⁶ At p.34 of the PRA's Annual Report and Accounts 2015.

Joint investigations

Rec. 11 Because they may prove especially onerous for subjects, the FCA and PRA should provide more guidance about the conduct of joint investigations. However, the regulators may wish to develop their experience of, and approach to, these types of investigation before setting out detailed guidance.

Rec. 13 The regulators should provide guidance as to how they will approach decision-making in contested cases, following joint investigations, to ensure effective coordination.

3.25 The HMT Review recommended that the FCA and the PRA should provide more guidance about the conduct of joint investigations and how they will approach decision-making in contested cases following joint investigations. It is important to note that the RDC does not have any involvement in the investigation itself – nor will the PRA’s Enforcement Decision-making Committee, once established. The Review also noted that both the PRA and the FCA may wish to develop their experience of, and approach to, these types of investigations before setting out detailed guidance.

3.26 Under Annex 1 to the MoU, if an issue affects the advancement of both the FCA’s and PRA’s objectives, the regulators will determine whether any investigation against a firm or officer/employee should be carried out by the FCA, by the PRA, or jointly, and how to coordinate any investigation and subsequent proceedings.³⁷

3.27 At this stage, given the comparatively small number of joint investigations completed to date, the FCA and the PRA are approaching each investigation on a case-by-case basis in line with the MoU. Both regulators believe it is too early to come to a settled approach in joint investigations that would enable us to set out detailed guidance about how we will approach these cases more generally.

3.28 Similarly, in relation to decision-making in contested cases following joint investigations, FSMA and the MoU ensure effective coordination by stating that each regulator will consult the other when they have reached a view in principle regarding the action they plan to take, and before a formal decision to issue a warning notice or decision notice has been taken.³⁸

3.29 The regulators propose to implement the recommendation that the FCA and the PRA provide more detailed guidance as to the conduct of joint investigations, and also how the regulators will approach decision-making in contested enforcement cases following a joint investigation. They will do so once the PRA has consulted on, and set out its plans for, a functionally independent Enforcement Decision-making Committee and once we have had more experience of joint investigations. The PRA will publish new procedural documentation in due course once its Enforcement Decision-making Committee has been established.

Rec. 12 It will often be appropriate and expedient for the regulators to issue joint information requests. However, as a matter of course, the regulators should indicate to which investigation(s) the information sought is relevant, so that subjects can be satisfied that that information is within scope.

³⁷ At para.24 of Annex 1 to the MoU.

³⁸ At para.25 of Annex 1 to the MoU.

- 3.30** The HMT Review also recommended that in the context of joint information requests, the PRA and the FCA should indicate to which investigation(s) the information sought is relevant, so that subjects can be satisfied that the information is within scope. At present, information requests may be grouped by theme, rather than by regulator, but the split between the scope of the two investigations as set out in the respective Memoranda of Investigation allows the subject to identify whether the information required is relevant to the FCA's or the PRA's investigation.
- 3.31** The FCA proposes to amend EG to reflect that an information request should make it clear which parts of the request relate to which investigation. The PRA proposes to adopt the same approach in its enforcement investigations.

Q4: *Do you agree that the PRA and the FCA should identify the information requested by each regulator within the same information request?*

FCA/PRA cooperation

Rec. 14 The FCA already publishes information about its cooperation with overseas regulators, and should publish high-level information about its cooperation with the PRA.

- 3.32** The HMT Review also recommended that the FCA publish high-level information about its cooperation with the PRA.
- 3.33** The FCA reports information about its coordination with the PRA in the FCA's Annual Report and will continue to do so. The FCA Annual Report for 2014/15 contained a section entitled 'Coordinating with the Prudential Regulation Authority (PRA)'.³⁹
- 3.34** The PRA similarly reports information about its coordination with the FCA in its Annual Report and will continue to do so. The PRA Annual Report 2015 contained a section entitled 'Financial Conduct Authority: effective regular co-ordination'.⁴⁰ The PRA also proposes to include a description of its enforcement cooperation with the FCA in a webpage on the PRA website.

Enforcement policy and process

Rec. 15 The government recommends that the PRA develop guidance on its enforcement policy and process, particularly in respect of the conduct of investigations and the exercise of statutory powers.

- 3.35** The HMT Review recommended that the PRA develop guidance on its enforcement policy and process, particularly in respect of the conduct of investigations and the exercise of statutory powers. This recommendation will be the subject of a separate PRA-only consultation later this year alongside the proposed establishment of the Enforcement Decision-making Committee. The Bank of England, of which the PRA is currently a subsidiary, proposes to establish the

³⁹ At p.70 of the Report, online at: www.fca.org.uk/your-fca/documents/corporate/annual-report-14-15.

⁴⁰ At p.34 of the Report, online at: www.bankofengland.co.uk/publications/Documents/annualreport/2015/prareport.pdf.

Enforcement Decision-making Committee covering the different types of contested enforcement cases across the full range of its supervisory functions, once the Bank of England and Financial Services Bill has completed its parliamentary stages. The Bank will publicly consult on this proposal later this year.⁴¹ This “One Bank” approach is in keeping with the Bank’s Strategic Plan (“One Bank, One Mission”)⁴².

⁴¹ The progress of the Bill can be followed online at: services.parliament.uk/bills/2015-16/bankofenglandandfinancialservices.html.

⁴² See online at: <http://www.bankofengland.co.uk/about/pages/strategicplan/default.aspx>

4.

Subjects' understanding and representations in enforcement investigations

- 4.1** The HMT Review made a number of recommendations about communication between the PRA/FCA and firms and individuals under investigation during the investigative phase. The Review also included a recommendation concerning the provision of more information on the factors that the regulators take into account when considering applications to extend the period for responding to a Preliminary Investigation Report (PIR) or warning notice. This chapter sets out the regulators' proposals for implementation of these recommendations.

Initial notice of investigation

HMT Review Recommendation:

- Rec. 16** The Government recommends that the regulators provide more information within Memoranda of Appointments (MoAs) or in accompanying documents, as to the basis for a subject's referral to enforcement. In particular, explanations for referral should link expressly to the published referral criteria, to enhance transparency.
-

- 4.2** The HMT Review recommended that the FCA and the PRA provide more information (within the MoA of Investigators or in accompanying documents) as to the basis for a subject's referral to enforcement. In particular, it recommended that explanations for referral should link expressly to the published referral criteria.

Green Report Recommendation:

- 4.3** The Green Report recommended that unless the referral decision maker considered that there were compelling reasons not to do so (such reasons being properly recorded), the regulators should include within the MoA, or alternatively in a separate document which is also sent to the subject of an investigation, succinct accounts of the following:
- i. A summary of the potential breaches.
 - ii. An explanation of the matters that are said to give rise to those breaches.⁴³
- 4.4** The Report recognised that this recommendation was consistent with recommendation no.16 in the HMT Review.

⁴³ Recommendation 3: Informing the subject of an investigation about the matters under investigation at pp.91–92 (Appendix E: Recommendations).

Proposed implementation of both the HMT Review and Green Report Recommendations

- 4.5** The FCA proposes to amend EG to reflect that if a decision to refer to enforcement is made, the FCA will set out in writing (and give to the subject at the same time the MoA is issued) a succinct summary of the potential breaches, a succinct explanation of the matters that are said to give rise to those breaches, and an explanation of the criteria they have applied in coming to the decision to refer.
- 4.6** The PRA proposes to include more information within the investigation MoA, or accompanying documents, about the basis for a subject's referral to enforcement, including more of the context in which the alleged breaches occurred. This information will link to the PRA's referral framework, once published. As indicated above at page 7, the PRA will be publishing more about its referral framework later this year.

Q5: *Do you agree with the above approach in respect of the initial notice of investigation?*

Scoping meetings

Rec. 17 Scoping meetings should usually take place once investigators are in a position to share their indicative plans on the direction of the investigation and timetabling of key milestones, based on the particular circumstances of the case.

- 4.7** The HMT Review recommended that scoping meetings should usually take place once investigators are in a position to share their indicative plans on the direction of the investigation and timetabling of key milestones, based on the particular circumstances of the case. The Review also recommended that subjects are expressly invited, at scoping meetings or otherwise at an early stage, to provide an indication as to whether they accept the suspected misconduct, or specific aspects of it.
- 4.8** The regulators propose to adopt the recommendation that scoping meetings should usually take place once investigators are in a position to share their indicative plans on the direction of the investigation and timetabling of key milestones, based on the particular circumstances of the case. However, the FCA and the PRA will need to retain flexibility about the timing of scoping meetings. Some individuals and firms prefer a meeting as soon as possible after the appointment of investigators in order to meet the investigators and have the enforcement process explained. However, it may be difficult to give much information in relation to the direction of the investigation if the meeting is held so early in the process. In such circumstances, it may be more appropriate to deal with the timetabling of the next steps in the investigation, and explore the scope and extent to which the firm or individual accepts any part of the suspected misconduct at a later meeting.
- 4.9** The aim of these proposals is not to make the process more cumbersome, but to ensure that subjects get more information about how an investigation is intended to develop, as part of an overall effort by the regulators to increase the transparency of the investigation process to the subject of the investigation. As such, while the meeting may cover extra areas, and take place slightly later in the timetable than currently, the regulators' aim is to give the subject of the investigation, and their advisers, more information about the next steps, to engender a dialogue about the investigation itself at the early stages of the investigation which does not currently routinely happen.

Rec. 18 The Government recommends that subjects are expressly invited, at scoping meetings or otherwise at an early stage, to provide an indication as to whether they accept the suspected misconduct, or specific aspects of it. The regulators should consider (potentially in the course of the FCA's forthcoming review of its penalty policy) whether it may be appropriate to expressly incentivise admissions at this stage, within their penalty setting frameworks.

4.10 The FCA proposes to explore this recommendation, as suggested in the Review, as part of its forthcoming review of its penalty policy. Similarly, the PRA intends to consider this recommendation as part of a forthcoming review of its settlement policy. However, it should be noted that both regulators currently incentivise early admissions as part of their respective approaches to settlement.

4.11 Both the FCA and the PRA recognise the benefits of, and public interest in, timely and comprehensive settlement on appropriate terms, particularly the early settlement of enforcement action. In recognition of this, the PRA's settlement policy provides that the amount of the penalty that would otherwise have been payable may be reduced, depending on the stage at which a binding settlement agreement is reached.⁴⁴ Under both regulators' current policies, they may begin settlement discussions at any stage of an enforcement action. The FCA's settlement policy provides that, once the FCA has a sufficient understanding of the nature and seriousness of the misconduct to make a reasonable assessment of the appropriate outcome, it may begin settlement discussions. Depending on the nature of any admissions at the scoping stage, this may result in an agreed settlement within the Stage 1 period and would be eligible for a 30% settlement discount. The FCA's present settlement policy also provides for a reduction in the amount of penalty that would otherwise be payable, depending on the stage at which a resolution of the investigation is reached.⁴⁵

4.12 However, any further incentivisation of early settlement will need to balance the desirability of the matter concluding quickly with the need to ensure that the full extent of the misconduct is understood.

Q6: *Do you agree with the regulators' proposals around the scoping meetings?*

Q7: *Pending consideration of whether it may be appropriate expressly to incentivise admissions at scoping meetings (in the context of the FCA's forthcoming review of its penalty policy and the PRA's forthcoming review of its settlement policy), do the regulators' current approaches to discounts for early settlement provide sufficient incentive for early admissions at scoping meetings?*

⁴⁴ See 'The Prudential Regulation Authority's approach to enforcement: statutory statements of policy and procedure' (January 2016) at p.28, online at: www.bankofengland.co.uk/pradocuments/publications/sop/2016/approachenforcementupdate.pdf.

⁴⁵ The FCA policy on discount for early settlement is set out in the FCA Handbook in DEPP 6.7. For the PRA policy, see footnote immediately above.

The involvement of supervisors

Rec. 19 In most investigations referred from supervision, it will be beneficial for supervisors to share information with investigators on the firm's business and relevant market practice issues. However, the appropriateness of the involvement, depending on the particular circumstances of the case, should be calculated at the outset and kept under review by senior staff.

Rec. 20 Where appropriate, supervisors of relationship-managed firms should attend scoping and progress meetings with a firm under investigation.

Rec. 21 Investigators and supervisors should ensure that they maintain an open dialogue throughout investigations to promote a broad symmetry of information.

4.13 The HMT Review recommended that the regulators consider how best to utilise the referring area's knowledge of the firm's financial sector and that, where appropriate, supervisors of relationship-managed firms should ordinarily attend scoping and progress meetings with the firm under investigation. It also recommended that investigators and supervisors should ensure that they maintain an open dialogue throughout investigations.

4.14 It is important to note that the majority of firms that the FCA regulates do not have specific supervisors in relation to their firm (see diagram at paragraph 3.7 regarding the types of firms regulated by the FCA). However, where a firm is a relationship-managed firm, the FCA proposes to amend and clarify the involvement of supervisors during the investigation phase in EG.

4.15 All large PRA deposit-taking, insurance and investment firms are relationship-managed and in such cases, where appropriate, supervisors attend scoping and progress meetings. Investigators and supervisors have maintained an open dialogue in PRA investigations and, in particular, at certain key stages of those investigations. For example, at the scoping stage, supervisors may provide key basic information regarding the firm (e.g. organisation charts, annual reports) to avoid unnecessary information requests being sent to the firm. The extent of information already held by supervisors will be checked, and investigators can usefully draw on supervisors' expert knowledge throughout the course of the investigation.

4.16 Recommendations 19–21 are related and similar to recommendations 9–10 above. The PRA proposes to maintain the approach recommended by the Strachan Review, set out above at paragraphs 3.20-3.21, and implement certain changes to RAD processes set out at paragraph 3.23 above.

Q8: *Do you agree with the above approach to supervisory involvement in enforcement investigations?*

Periodic updates and constructive dialogue

Rec. 22 The Government recommended that investigators provide periodic updates to subjects about the progress of investigations in appropriate cases. Updates should focus on the practical steps that have been taken in the investigation to date, and that are intended to be taken in the coming months. Investigators should also reference and update the indicative timeline set out at the scoping meeting. The circumstances of the case may influence how regularly updates should take place, but they should occur on at least a quarterly basis, and subjects should be able to request a face-to-face meeting.

- 4.17** The Strachan Review had previously examined the issue of keeping the subject of the investigation (firm or individual) informed during the investigation.⁴⁶ It noted that some responses to the Issues Paper had suggested that the case team should communicate better with the subject as the case progressed, thereby avoiding the impression that the 'shutters have come down'. However, it noted that there was recognition of the limits as to how forthcoming the FSA could be on matters it was still considering or the issue of further investigation.
- 4.18** The PRA and the FCA consider they can do more, beyond the approach originally recommended in the Strachan Review, to improve communication with the subjects of an investigation.
- 4.19** The 2014 HMT Review's Call for Evidence paper noted that, although the FCA EG states that the FCA will have an 'ongoing dialogue' with the subject through the enforcement process, unlike the Competition and Markets Authority (CMA), the FCA does 'not have a policy of formally offering investigation subjects regular opportunities to meet representatives of the case team'.⁴⁷
- 4.20** The Review recommended that investigators should provide periodic updates to subjects about the progress of investigations in appropriate cases that would focus on the practical steps that have been taken in the investigation to date, and that are intended to be taken in the coming months, giving updated indicative timelines. The Review also recommended that these should occur on at least a quarterly basis, and subjects should be able to request a face-to-face meeting.
- 4.21** The PRA and the FCA have had helpful discussions with the CMA about its policy and practice on case updates and state-of-play meetings. The regulators note that the CMA generally provides case updates to the subjects of investigation either by telephone or in writing, as the most efficient and effective way of sharing information on case progress for the CMA and the subjects of investigation.⁴⁸ The PRA and the FCA have begun using this approach in current investigations.
- 4.22** The CMA also offers each party under investigation separate opportunities to meet with representatives of the case team to ensure that they are aware of the stage the investigation has reached. These state-of-play discussions are sometimes held by conference call.⁴⁹

⁴⁶ See online at: www.fsa.gov.uk/pubs/other/enf_process_review_report.pdf, p.31, para.5.17.

⁴⁷ HM Treasury, 'Review of enforcement decision-making at the financial services regulators: call for evidence', online at: www.gov.uk/government/consultations/review-of-enforcement-decision-making-at-the-financial-services-regulators-call-for-evidence/review-of-enforcement-decision-making-at-the-financial-services-regulators-call-for-evidence.

⁴⁸ See CMA, 'Competition Act 1998: Guidance on the CMA's investigation procedures in Competition Act 1998 cases' (CMA8, March 2014), at p.50, para.9.14, available online at: www.gov.uk/government/uploads/system/uploads/attachment_data/file/288636/CMA8_CA98_Guidance_on_the_CMA_investigation_procedures.pdf.

⁴⁹ As above at para.9.15.

- 4.23** In the CMA, the state-of-play meetings take place at the scoping stage and shortly before taking the decision on whether or not to issue a Statement of Objections.⁵⁰ They are closest in similarity to scoping meetings and what will be pre-Stage 1 and Stage 1 discussions at the FCA and the PRA. The CMA also offers a further state-of-play meeting post-Statement of Objections.⁵¹
- 4.24** The FCA proposes to amend EG to reflect its aim to give periodic updates on at least a quarterly basis. These will cover the steps taken in the investigation to date, as well as the next steps and indicative guidelines.
- 4.25** The FCA also proposes to amend EG to reflect the practice that, in joint investigations with the PRA, discussions with the firm or individual under investigation will normally occur with representatives of both regulators present and that, where possible, the regulators will seek to ensure that the respective enforcement processes are coordinated.
- 4.26** The PRA proposes to adopt a similar approach to that set out above in its investigations, for both joint PRA/FCA and PRA-only investigations.

Q9: *Do you agree with the above approach to periodic updates in the context of enforcement investigations?*

Rec. 23 The Government recommends that the regulators consider how best to promote early, constructive engagement between investigators and subjects, and that they consider, for example, the provision of specific training to investigators, increased involvement of senior staff – from the regulators, and from firms under investigation – and encouraging greater cooperation from subjects.

- 4.27** The HMT Review recommended that the regulators should consider how to promote early, constructive engagement between investigators and subjects. The Review suggested that consideration be given to the provision of specific training, increased involvement of senior staff from both the regulators and firms under investigation, and encouragement of greater cooperation from subjects.
- 4.28** In respect of the FCA, the FCA's senior staff will be involved throughout an investigation and will be informed of the investigation's progress. This may be at project sponsor and head of department level, involve directors within EMO or be escalated to senior decision-making committees. The FCA acknowledges that this may not always be apparent to those under investigation. While increased or more apparent involvement by senior staff may be appropriate in some cases, the FCA considers that a key factor in promoting constructive engagement is ensuring that an investigation team has the right level of experience. It is also important that the subject of an investigation recognises that if and when the investigation team is able to share its emerging thinking, that communication does not commit the team to any particular position, as their thinking may well change.
- 4.29** For the PRA, the Head of RAD has overall responsibility for a PRA investigation. Each investigation has an investigation team, headed by a senior member of RAD and supported by a team of investigators. The decision to open an investigation is taken by agreement between the Head of RAD and the Head of Division or Director of the Supervisory area concerned. The matter

⁵⁰ As above at para.9.16.

⁵¹ As above at para 9.18.

then passes to the Investigation team in RAD to manage the investigation on a day-to-day basis, taking decisions about the direction of the investigation, what evidence needs to be gathered and whether interviews might be needed. Decisions to open a Stage 1 settlement are generally taken by the PRA's Supervision, Risk and Policy Committee (SRPC), which consists of senior staff at the regulator (including the Head of RAD), in accordance with the PRA's published policy on decision-making.⁵² The SRPC is also responsible for ratifying any settlement reached at Stage 1.

- 4.30** The PRA and the FCA will coordinate the provision of certain training to enforcement staff, including investigators, who are PRA/FCA employees. Training is not provided to external persons who may be appointed as investigators, e.g. professional services firms, as they are engaged on the basis of the specific expertise and services they offer. PRA and FCA employees, however, consistently provide regulator-specific advice and guidance to such appointees.
- 4.31** The Bank of England proposes to establish an Enforcement Decision-making Committee in the near future, which will be functionally independent of senior management and will take decisions in contested enforcement cases (see paragraph 3.29 above). As indicated at paragraph 1.13, the Bank will issue a separate consultation paper on this proposal.

Q10: *Do you agree with the proposed approach set out above to constructive engagement in the context of enforcement investigations?*

Time limits for responding to PIRs and warning notices

Rec. 24 To enhance transparency, the regulators should set out those factors that they might consider relevant to an application for extending the period for responding to a PIR or warning notice.

- 4.32** The HMT Review recommended that, to enhance transparency, the FCA and the PRA should set out those factors they might consider relevant to an application to extend the period for responding to a PIR or warning notice.
- 4.33** The FCA proposes to amend DEPP 3.2.16 G to include some non-exhaustive factors that the FCA would take into account when considering a request to extend time to respond to a warning notice. It also proposes to amend EG to reflect those similar factors that it would take into account when it considers a request for an extension of time to respond to a PIR.
- 4.34** These factors include the legal and factual complexity of the case, and the existence of any factors outside the firm's or individual's control that would materially impact on their ability to respond within the period set out in the warning or first supervisory notice. The FCA may also take account of any relevant comments from FCA staff responsible for the matter. In addition, in relation to a request to extend time to respond to a warning notice, the FCA will take into account whether the firm or individual has had the opportunity to respond to a PIR, or whether the case has substantially changed from the case set out in any PIR.
- 4.35** Having considered the issue, and recognising the advantage in the regulators having consistent policies in this regard, the PRA proposes to adopt the same factors in setting out those that

⁵² See online at: www.bankofengland.co.uk/publications/Documents/other/praproachenforcement.pdf

it would consider relevant to an application for an extension of time to respond to a PIR or warning notice.

- 4.36** It should be noted that even where some or all of these factors are evidenced in the application for an extension, the FCA and the PRA will have to take into account all the circumstances of the case when deciding whether to grant the application for an extension of time. In certain cases, it may be more appropriate to grant the proposed extension in part only; for example, where an application is made for a one-month extension, the regulator may consider that only a two-week extension is objectively justified.

Q11: *Do you agree with the proposed list as constituting those factors that the regulators will take into account when considering whether to grant an extension of time to respond to a PIR or warning notice, in full or in part? Are there any further factors that you consider should be taken into account?*

5. Settlement

- 5.1** The HMT Review noted the importance of settlement to both the regulators and subjects of enforcement action. The Review did not recommend a longer Stage 1 period in settlement discussions, but focused on the effectiveness of the Stage 1 period itself. This chapter sets out the FCA's response to those recommendations and sets out a proposal for the issue between the FCA and the subject to be narrowed by agreement, with the contested issues being decided by the RDC. The PRA will bring forward proposals in due course and expects to consult on these later this year.

Early notification of Stage 1

- 5.2** The Review recommended that the FCA should aim to give 28 days' notice of Stage 1 beginning, so that administrative arrangements can be made and that if service of settlement papers is likely to be delayed, subjects should be notified. The FCA proposes to amend EG to incorporate this early notification to allow administrative arrangements to be made, such as ensuring that key staff will be available.

Pre-Stage 1 preliminary without-prejudice meetings

- 5.3** The Review also recommended that, where appropriate, the FCA should offer preliminary meetings on a without-prejudice basis in the period between notification of the date on which Stage 1 will begin, and its commencement. The Review recommended that the investigators should summarise key legal and factual bases of the case at preliminary meetings and identify key evidence.
- 5.4** The Review also noted that preliminary meetings will usually take place prior to decision makers' approval of any proposed penalty and disciplinary outcome, so that subjects understand that there is the potential for the case to change.
- 5.5** The FCA proposes to amend EG to allow for the incorporation of pre-Stage 1 preliminary meetings. The purpose of the meeting would not be to start Stage 1 discussions, but to explain the FCA's view of what went wrong, and for the firm to indicate the extent to which they agree with outline findings. It will also be an opportunity for firms to indicate where they believe there are factual errors and to identify any inadvertent mistakes.

Information provided at Stage 1

- 5.6** The Review recommended that at the commencement of Stage 1, regulators should continue to ensure that they identify and, where necessary, give subjects the key evidence on which

their case relies. The Review also suggested that the FCA may wish to provide more specific guidance about the circumstances in which they will provide PIRs.

- 5.7** In the majority of discussions at Stage 1, the FCA will have provided a draft warning notice that will help set out the issues that need to be discussed. Whether the FCA will produce a PIR will depend on the stage of the investigation at which the FCA feels that it is in a reasonable position to make an assessment of the extent and nature of the misconduct. We will keep under review whether it would be helpful to give more guidance about the circumstances when we will provide PIRs, once we have had the opportunity to consider the responses to this consultation.
- 5.8** The FCA proposes to amend EG to note that when it is necessary to help resolve factual disputes or to assist the firm or individual to make an informed decision about whether to resolve the dispute by agreement, the FCA will identify the key evidence on which its case relies at the commencement of Stage 1, unless the firm or individual already has that information, (e.g. a PIR has already been sent to them). However, this is not meant to be a disclosure exercise. So, while the FCA will identify the key evidence that underpins its view of the case, it will not generally provide evidence if the firm or individual already possesses it.

Q12: *Do you agree with the proposed changes to the pre-Stage 1 process?*

Q13: *Do you have any comments on the proposed approach to the information provided at Stage 1?*

Partly contested cases

- 5.9** A number of respondents to the HMT Review Call for Evidence felt that we should create a process that allows a discount for early settlement when the subject
- agrees with the majority, but not all, of the FCA's findings; or
 - agrees on the facts but not the liability (e.g. whether they are a breach of a relevant rule or Principle) or what the appropriate penalty should be
- and** the RDC's decision effectively matches the subject's representations on the appropriate outcome.
- 5.10** The HMT Review rejected this approach on the basis that it would be difficult to decide whether a decision was more or less favourable than the original enforcement proposal. The FCA agrees that it would be very difficult to carry out such a process if the question of whether a 30% discount should still be applied meant comparing:
- the proposed outcome discussed in settlement, and
 - the decision made by the RDC on a fully contested basis

and then coming to a judgement that the subject would have settled on the basis of the findings and penalty ultimately decided by the RDC. Few cases are likely to be so clear cut, particularly where factual issues still need to be decided and liability has not been accepted.

- 5.11** In order to respond to these concerns, however, the FCA proposes introducing a streamlined procedure to narrow the issues between the FCA and the subject by entering into a ‘focused resolution agreement’ on the facts and liability, with the RDC then determining only the action to be taken (the “Proposal”).
- 5.12** With this Proposal, the outstanding issues to be determined by the RDC can be clearly, simply and workably defined. As all relevant facts and issues about the breach have been accepted by the subject, the role of the RDC would be to determine the appropriate regulatory response, akin to a defendant pleading guilty in criminal proceedings. This includes whether the action taken should be a financial penalty or public censure, prohibition order or suspension, restriction, condition or limitation and the appropriate level or scope of any such action. This Proposal should increase the transparency and clarity of how financial penalties are calculated and give a clearer message, as they will be accompanied by a reasoned decision from the RDC.
- 5.13** Under this streamlined procedure, the subject must accept all facts relevant to the proposed enforcement action **and** all issues of whether those facts amount to a breach or more than one breach. This should ensure that this Proposal still keeps much of the savings in time and costs to both subjects and the FCA that are currently made by settlement at Stage 1.
- 5.14** There will still be the opportunity to settle all issues, including the appropriate sanction at Stage 1 without the involvement of the RDC; the FCA is not proposing any changes to the process for agreeing a full settlement of all issues which will continue to have a 30% discount applied to the penalty.
- 5.15** The FCA proposes that the same fixed discount of 30% applies where a focused resolution agreement is reached during Stage 1 and the only contested issue is penalty, on the basis that this is akin to a guilty plea and will still have resulted in substantial savings in time and resources. While this is the same discount for settlement of all issues at Stage 1, settlement at that stage has a greater inbuilt saving in terms of time and resources and the benefit of certainty that flows from a full settlement.
- 5.16** In outline, the FCA proposes to amend DEPP and EG to provide for a focused resolution agreement that would allow a subject to make submissions on the appropriate outcome before the RDC and which would be dealt with under the following procedure:
- As with current Stage 1 settlement, the Settlement Decision Makers (SDMs) will decide whether to accept the proposed resolution.
 - If the SDMs accept the resolution, they will give a warning notice setting out the facts and liability, and set out the FCA’s position on penalty.
 - After giving a warning notice, the SDMs will inform the RDC that they have done so and the RDC will then make any necessary arrangements for representations. If the SDMs decide to give a warning notice, they will also be responsible for deciding whether or not to exercise the powers to publish information about a warning notice after consultation with the person to whom the warning notice is given or copied.
 - After the RDC has received written/oral representations from both the FCA and the subject on the appropriate penalty, it will then decide whether to give a decision notice. DEPP will be amended to make clear that the RDC must accept, and not in any circumstances depart from, the agreed position on the agreed issues set out in the focused settlement agreement.

- 5.17** The focused resolution agreement will include agreement by the FCA and the subject that they will not seek to contest the facts and liability as set out in the warning notice when making representations to the RDC or on any subsequent reference of the matter to the Tribunal. We do, however, recognise that the Tribunal has the power to revisit issues of its accord, so a focused resolution agreement will allow representations and hear evidence where the Tribunal requires it.
- 5.18** The focused resolution agreement will also include an agreement to waive rights under section 394 FSMA to disclosure of material relied upon by the FCA and any undermining material on areas where agreement is reached.
- 5.19** The FCA has also considered two alternative types of agreement:
- Alternative 1 – the subject agrees all facts relevant to the proposed enforcement action but wishes to make submissions and contest whether the breaches as alleged by the FCA arise from those facts. In these circumstances there would also be a dispute about the appropriate outcome.
 - Alternative 2 – the subject agrees one or more issues relevant to the proposed enforcement action, but not all, and wishes to contest narrowed down issues. The issues which may be agreed include, but are not limited to, issues of:
 - questions of fact
 - whether specified facts amount to a breach (or more than one breach)
 - whether action for a financial penalty and/or public censure is warranted
 - the appropriate level of a financial penalty
 - whether action for a suspension, restriction, condition or limitation (as defined for the purposes of DEPP 6A) is warranted
 - the appropriate length of a suspension, restriction, condition or limitation (as defined for the purposes of DEPP 6A)
 - whether a prohibition order is warranted, and
 - the appropriate scope of a prohibition order
- 5.20** The FCA considers that the two alternative proposals may have some benefits, as follows:
- There may be an increase in cases against individuals in the future. This is consistent with the commitment to taking action where appropriate against individuals and the introduction of the Senior Managers and Certification Regime (which will give greater clarity over an individual's responsibilities and increase accountability). These cases tend to have more issues in dispute because the impact of any disciplinary sanctions on an individual's financial position and reputation can be greater than for cases against firms, and the ability to narrow those issues may help assist in resolving those cases more efficiently.
 - Contesting facts and/or the breaches that arise from those facts before the RDC under the focused settlement agreement procedure may also help develop a body of more detailed decisions that can be understood and translated into clear advice to firms and individuals.

Decisions that are the result of a contested process tend to be more detailed, as the RDC will not only set out the findings that underpin the decision but will also refer to any representations made by the subject and its view on those representations.

- 5.21** However, the main issue with Alternatives 1 and 2 is the potential breadth of the number of issues that would remain unresolved and need to be contested before the RDC. Unless the issues are narrowed considerably, the saving in resources for both the FCA and the subject compared with a fully contested case may be limited.
- 5.22** In addition, if some material facts or liability issues remained to be resolved, the question of how much credit ought to be given to a subject who is found liable by the RDC is more complex and less suitable for a fixed and guaranteed discount. In order to give appropriate credit to different cases, it is likely that the discount scheme would have to give the RDC a discretion to set the appropriate discount.
- 5.23** For example, in cases where there is agreement on all relevant facts but not on whether they amount to a breach (Alternative 1), the appropriate approach to penalty might be to give the RDC a discretion to award a discount within a specified range (perhaps 15% - 30%). However, where there is a greater range of contested issues that could still leave a number of issues of fact, liability and penalty unresolved (Alternative 2), it may be that the appropriate approach may be to allow the RDC a discretion to award a discount within a range of 0% – 30%. The RDC would take into account the significance of the agreed issues to the case as a whole, the degree to which the RDC considers the concessions have reduced time and cost, and the extent to which the narrowing of the issues satisfies the RDC that the subject has earned credit.
- 5.24** The FCA considers that the Proposal should lead to greater transparency in how a penalty is calculated, but without resulting in any significant loss in efficiency or increase in resources used to resolve the investigation. However, as both Alternatives 1 and 2 leave the extent of any agreement of the issues undecided, it is more difficult to come to the same conclusion. We are minded to take the Proposal forward, but welcome views on Alternatives 1 and 2.

Q14: *Do you agree that the FCA should amend DEPP and EG to make provision to contest penalty only before the RDC?*

Q15: *Do you have any comments on the proposed framework and procedure for contesting penalty only?*

Q16: *Do you have any comments on Alternatives 1 and 2?*

Extending Stage 1

- 5.25** The Review recommended that, to enhance transparency, the regulators should set out those factors that they might consider to be relevant to an application for extension of Stage 1.
- 5.26** The FCA's view is that in most cases, 28 days is a reasonable period in which to respond to a Stage 1 letter. That period is not fixed, and in complex cases – i.e. those involving multiple jurisdictions or multiple parties or both – a longer Stage 1 period will be appropriate. However, the FCA remains of the view that any extensions should be in exceptional circumstances only. It proposes to amend EG to note that these will generally be circumstances where factors outside the firm's or individual's control will have a material impact on their ability to engage

in settlement discussions in the Stage 1 period. Where new information has come to light that would have such a material effect on the FCA's findings or proposed disciplinary outcome that it makes the previously set Stage 1 period unreasonable, it may be more appropriate to consider withdrawing the Stage 1 letter and consider issuing a new Stage 1 letter when the new facts have been assessed.

- 5.27** As indicated above, the PRA will be consulting separately in respect of this recommendation later in 2016.

Q17: *Do you have any comments on this approach to extending Stage 1?*

Making representations in settlement negotiations

- 5.28** The Review sought to address the concern that representations made during settlement, where material to the regulators' assessment of the case or penalty and not previously considered or given sufficient weight, should be assimilated by the regulator prior to it reaching a decision. The Review suggested that this may be best achieved, in the case of the FCA, by the relevant Enforcement Head of Department, where necessary, acting as a suitably senior conduit between the case team and the SDMs. The Review also recommended that, in most cases, the Head of Department should attend a without-prejudice settlement meeting during Stage 1. Where attendance at this level is not possible, an appropriately senior substitute should attend in their place.

- 5.29** The FCA proposes to clarify the involvement of senior management in settlement negotiations in EG. In all cases, senior management, including heads of department, will be aware of the nature and content of settlement negotiations. However, the FCA will consider how their involvement can be made more transparent and will address the concern that insufficiently senior staff are involved in the discussions and in liaising with the settlement decision makers. The senior member or members of staff acting as the case sponsor will liaise, where appropriate, with the settlement decision makers and, where appropriate, having regard to the size complexity and seriousness of the case, attending a without-prejudice meeting during negotiations or arranging for the attendance of an appropriately senior FCA representative.

Q18: *Do you have any comments on our proposed approach to implementing the Review's recommendations on representations in settlement discussions?*

Settlement discounts

- 5.30** The Review considered that 'removing the discounts currently available at Stages 2 and 3 will assist in demarcating, at an early stage, between those cases that can be settled, and those that must be contested'.
- 5.31** The present settlement discount scheme is set out in DEPP 6.7. Settlement can be reached at any stage of an investigation, but the settlement discount scheme provides for graduated reductions in penalty depending on the stage at which settlement is reached.

- Stage 1: 30% reduction if settlement is reached between the start of an investigation and the point at which the FCA has a sufficient understanding of the nature and the gravity of the breach to make a reasonable assessment of the appropriate penalty, has communicated our assessment to the person under investigation and has allowed a reasonable opportunity to reach agreement about the amount of the penalty
- Stage 2: 20% reduction if settlement is reached between the end of Stage 1 and the date when the period for making written representations to the RDC has expired (or the date on which written representations were sent in response to a warning notice)
- Stage 3: 10% reduction if settlement is reached between the end of Stage 2 and the date when a decision notice is given
- Stage 4: 0% reduction if settlement is after the end of Stage 3 (which would also include proceedings before the Tribunal and any subsequent appeals)

5.32 The Review recommended that the FCA should consider reviewing the graduated discount scheme and applying a discount only to those cases that settle in Stage 1, but retain the ability to apply a discretionary discount in cases that settle outside Stage 1, where we consider it appropriate. The reason for this was a general view from the consultation, that cases either settle or do not, and that an extended graduated discount scheme may not optimise settlement prospects. As the Review noted, between 2012 and 2014, only nine cases settled in Stage 2 or beyond.

5.33 Implementing other recommendations, such as periodic updates during the investigation, notice of the likely start of Stage 1, and pre-Stage 1 meetings, should provide sufficient focus on the substantive issues in settlement discussions to allow both the FCA and the subject to establish which matters can be agreed and those that remain in dispute, at an early stage.

5.34 The FCA considers that in fully settled cases the discount of 30% should remain where agreement is reached during Stage 1. As noted above, the FCA also proposes that the same fixed discount of 30% is applied where a focused settlement agreement to contest penalty only is reached during Stage 1. For the reasons set out in the HMT Review, we propose to adopt the recommendation to abolish the Stage 2 and 3 discounts.

Q19: *Do you have any comments on the proposed discount for entering into a focussed resolution agreement to contest penalty only? In particular, should there be a difference in discount between cases that settle fully and those that contest penalty only?*

Q20: *Do you agree with the proposal to accept the Review's recommendation to abolish Stage 2 and Stage 3 discounts?*

Ongoing settlement review

- 5.35** The Review recommended that the contested case decision makers (in the FCA's case, the RDC) should regularly review the regulator's processes in settled cases. It recommended that the review should include seeking comments from all or a sample of those who have settled cases and speaking with the relevant Enforcement staff. The RDC should monitor the effectiveness of the recommended changes to the settlement process, identify whether there may be settlement process lessons to be learned, and make generic public recommendations.
- 5.36** The FCA proposes that the RDC's review should be based on a sample of cases the RDC consider sufficient to enable it to form a view on the effectiveness and fairness of the revised settlement process from the perspective of all interested parties and the extent to which it contributes to a consistency of approach.
- 5.37** Similarly to end-of-case feedback meetings, the review will focus on practical and procedural aspects of the settlement process. It will only consider the substantive facts of the case and its outcome to the degree necessary to consider the effectiveness and fairness of the process and how much it contributes to a consistent approach. Where that review identifies scope for improvement of the process, it may lead to further consultation on changes to EG, and is likely to be included in the RDC's report, which we propose will form part of the FCA's Annual Report (see Chapter 6).

Q21: *Do you agree with the proposed approach to ongoing settlement review?*

6. Contested decision-making

Access to the Upper Tribunal

- 6.1** This chapter sets out the FCA's proposed implementation of Chapter 6 of the HMT Review only. As explained above at paragraph 1.13, the PRA will be separately consulting on the contested decision-making recommendations later this year.
- 6.2** When the FCA is proposing to exercise its regulatory enforcement powers, FSMA generally requires statutory notices to be given to the firm or individual under investigation. In an enforcement action, this will be a warning notice and decision notice. The RDC generally takes the decisions to issue such notices in contested enforcement cases. The RDC becomes involved after enforcement has formed the view that it is appropriate for the FCA to use particular powers against a firm or individual. The division will submit its proposed warning notice or supervisory notice, and the supporting evidence to the RDC. The RDC will review the evidence before coming to a decision. Then the firm or individual may make representations to the RDC, after which the RDC may issue a decision notice. The firm or individual may refer that decision to the Tribunal.
- 6.3** The Review recommended that the regulators put in place a clearly signposted, expedited procedure for subjects to proceed straight to the Upper Tribunal if they choose to challenge the regulator's case within a tribunal environment without first making representations to the regulator's decision maker.
- 6.4** As the Review noted, a person who has received a decision notice and has not previously made any response or representations to the FCA, may nevertheless refer the FCA's decision to the Upper Tribunal (DEPP 2.3.2 G).
- 6.5** DEPP provides for a default procedure if no representations are made within the time set out in the warning notice, which allows the decision maker to regard the allegations or matters in that notice as undisputed and so proceed to issue a decision notice.
- 6.6** The FCA proposes to amend DEPP to provide for a person who has received a warning notice (whether from the RDC or SDMs in a partly contested case) to elect not to make representations to the RDC or SDMs and waive the period during which representations may be made to the FCA under section 387(2) of FSMA (provided that all third parties who have the right to make representations on a warning notice have already done so). This will allow the FCA to move straight to issuing a decision notice in substantially the same terms as the warning notice. Further, the FCA proposes to amend DEPP to allow a subject to choose even prior to the issue of a warning notice to use the expedited route to the Tribunal. If the subject uses the expedited route prior to the issue of a warning notice, the settlement decision makers will issue both the warning and decision notices and the subject can then seek to refer the matter or partly contested element to the Tribunal.

- 6.7** The FCA will draw attention to this option in the letter that accompanies the warning notice. If the FCA gives a decision notice under this procedure, it may decide to publish the decision notice, and will follow the policy on publication set out in EG 6.8–6.8B.

Q22: *Do you agree with the proposal for access to the Tribunal without representations being made to the FCA's decision maker?*

Performance

- 6.8** The Review recommended that the RDC reports annually on its performance, and that this report might include the results of the annual operational review and the review of settled cases. The FCA proposes that this annual report should be included in the FCA's Annual Report, and should include the matters suggested by the Review.
- 6.9** In addition, the Review recommended that the Treasury Select Committee might consider requiring the attendance of future RDC and DMC Chairs on a pre-commencement basis. However, this is a matter for the Treasury Select Committee, and not the regulators, to determine.

Efficiency

- 6.10** The Review recommended that a regular review of the RDC should take place and be published. It recommended that the review should consider:
- the extent to which the RDC membership includes expertise appropriate to the areas in which the FCA is likely to take enforcement action
 - its operational performance, including the time taken to deal with contested cases following submission of papers by investigators and
 - the sufficiency of resource generally (the size of membership, the available administrative and legal staff) to deal with cases efficiently
- 6.11** The RDC is accountable to the FCA Board through the Board's External Risk and Strategy Committee (ERSC). This committee reviews and is responsible for the effective operation of the RDC, which includes the RDC's composition and sufficiency of resources. The ERSC receives quarterly reports from the RDC Chair, who also attends ERSC meetings to discuss any significant matters in those reports.
- 6.12** The operational performance of the RDC is currently set out in the FCA's Annual Report, and provides details of the time taken to deal with contested cases. The FCA proposes that the annual review and report by the RDC on operational performance, its review of its membership, and the sufficiency of its resource will be published alongside the FCA's Annual Report.
- 6.13** The FCA also proposes that the panel considering the representations and deciding whether to give a decision notice will usually be the same members of the RDC who previously considered the matter. The usual practice at the initial, warning notice, stage is that this will be a panel of three, though this is not always the case. This is a change from existing DEPP 3.2.3G, which states that where representations are made, it will be usual for the panel to include additional

members who have not previously considered the matter. In exceptional circumstances – for example, particularly complex cases, or those raising novel points of law or practice – it might be appropriate for a larger panel to consider the case at both the warning notice and representations stage. The RDC will decide on the size and composition of the panel, taking into account its efficient operation and any specific experience needed in any particular case.

Q23: *Do you consider that there are other matters on which the RDC could usefully report?*

Q24: *Do you agree with the proposal that, usually, the panel that gave a warning notice will be the same panel that considered representations and decided whether or not to give a decision notice?*

Annex 1

List of questions

- Q1:** *Do you agree with this approach to referral decision-making?*
- Q2:** *Do you have any comments on the proposed implementation of the Green Report?*
- Q3:** *Do you agree with the approach outlined above? Are there any particular adjustments that you consider should be made in respect of the process of involving supervisors in the investigation phase?*
- Q4:** *Do you agree that the PRA and the FCA should identify the information requested by each regulator within the same information request?*
- Q5:** *Do you agree with the above approach in respect of the initial notice of investigation?*
- Q6:** *Do you agree with the regulators' proposals around the scoping meetings?*
- Q7:** *Pending consideration of whether it may be appropriate expressly to incentivise admissions at scoping meetings (in the context of the FCA's forthcoming review of its penalty policy and the PRA's forthcoming review of its settlement policy), do the regulators' current approaches to discounts for early settlement provide sufficient incentive for early admissions at scoping meetings?*
- Q8:** *Do you agree with the above approach to supervisory involvement in enforcement investigations?*
- Q9:** *Do you agree with the above approach to periodic updates in the context of enforcement investigations?*
- Q10:** *Do you agree with the proposed approach set out above to constructive engagement in the context of enforcement investigations?*

- Q11:** *Do you agree with the proposed list as constituting those factors that the regulators will take into account in considering whether to grant an extension of time to respond to a PIR or warning notice, in full or in part? Are there any further factors that you consider should be taken into account?*
- Q12:** *Do you agree with the proposed changes to the pre-Stage 1 process?*
- Q13:** *Do you have any comments on the proposed approach to the information provided at Stage 1?*
- Q14:** *Do you agree that the FCA should amend DEPP and EG to make provision to contest penalty only before the RDC?*
- Q15:** *Do you have any comments on the proposed framework and procedure for contesting penalty only?*
- Q16:** *Do you have any comments on Alternatives 1 and 2?*
- Q17:** *Do you have any comments on this approach to extending Stage 1?*
- Q18:** *Do you have any comments on our proposed approach to implementing the Review's recommendations on representations in settlement discussions?*
- Q19:** *Do you have any comments on the proposed discounts for partly contested cases? In particular, should there be a difference in discount between cases that settle fully and those that contest penalty only?*
- Q20:** *Do you agree with the proposal to accept the Review's recommendation to abolish Stage 2 and Stage 3 discounts?*
- Q21:** *Do you agree with the proposed approach to ongoing settlement review?*
- Q22:** *Do you agree with our proposal for access to the Tribunal without representations being made to the FCA's decision maker?*
- Q23:** *Do you consider that there are other matters that the RDC could usefully report on?*
- Q24:** *Do you agree with the proposal that, usually, the panel that gave a warning notice will be the same panel that considered representations and decided whether or not to give a decision notice?*

Annex 2

Cost benefit analysis and compatibility statement

FCA

Cost benefit analysis (CBA)

1. The proposals set out in this CP do not relate to rule changes or guidance on rules. Under section 138I of FSMA, when the FCA wishes to introduce any new rules it must publish a CBA along with the proposed rules. This is an estimate of the costs and benefits that will result from the rule being made. Since the requirements under section 138I are not applicable, the FCA is not required to carry out a CBA.
2. The FCA does not expect the proposed amendments to DEPP or EG to have to lead to any increase in costs, or the cost increase will be of minimal significance. Overall, the proposals should benefit the FCA and firms in promoting a consistent approach to the exercise of our enforcement powers.

Compatibility statement

3. Section 1B of FSMA requires the FCA to explain why it considers that the proposed rules are compatible with its strategic objective, advance one or more of its operational objectives, and promote effective competition in the interests of consumers.
4. The FCA believes the proposals set out above are compatible with its duties under section 1B of FSMA. The effective and appropriate use of enforcement powers plays an important part in pursuing the FCA's statutory objectives, as it increases compliance with rules by making market participants more aware of conduct that may breach these rules, and the potential for sanctions for such conduct.
5. The FCA has had regard to the regulatory principles set out in section 3B of FSMA. In particular, the proposals are consistent with the need to use resources in the most efficient and economic way, and the principle that the regulators should exercise their functions as transparently as possible.

PRA

Cost benefit analysis (CBA)

6. In accordance with section 138J of FSMA, before making any rules, the PRA must publish a draft of the proposed rules, accompanied by a CBA. The proposals set out in this consultation do not relate to rule changes or to guidance on rules, and a CBA is therefore not required.

Compatibility statement

7. In discharging its general functions, including its function of determining the general policy and principles by reference to which it performs particular functions under FSMA (section 2J(1)(c)), the PRA must, so far as is reasonably possible, act in a way which advances its general objective of promoting the safety and soundness of PRA-authorized persons (section 2B), and, where rules and policies are relevant to insurance activities, its insurance objective to contribute to the securing of an appropriate degree of protection for those who are or may become policyholders (section 2C). When discharging its general functions in a way that advances its objectives, the PRA must, so far as is reasonably possible, act in a way which, as a secondary objective, facilitates effective competition in the markets for services provided by PRA-authorized persons in carrying on regulated activities (section 2H).
8. In developing this proposal, the PRA has considered the regulatory principles set out in section 3B of FSMA, including:
 - the need to use the resources of the PRA in the most efficient and economic way
 - the principle that a burden or restriction that is imposed on a person or on the carrying on of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction
 - the principle that the PRA should exercise its functions as transparently as possible.

Appendix 1

Draft FCA Handbook text

**DECISION PROCEDURE AND PENALTIES MANUAL AND ENFORCEMENT
GUIDE (REVIEW) INSTRUMENT 2016**

Powers exercised

- A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000:
- (1) section 63C (Statement of policy);
 - (2) section 69 (Statement of policy);
 - (3) section 88C (Action under s.88A: statement of policy);
 - (4) section 89S (Action under s.89Q: statement of policy);
 - (5) section 93 (Statement of policy);
 - (6) section 124 (Statement of policy);
 - (7) section 131J (Imposition of penalties under section 131G: statement of policy);
 - (8) section 137T (General supplementary powers);
 - (9) section 139A (Power of the FCA to give guidance);
 - (10) section 192N (Imposition of penalties under section 192K: statement of policy);
 - (11) section 210 (Statements of policy);
 - (12) section 312J (Statement of policy);
 - (13) section 345D (Imposition of penalties on auditors or actuaries: statement of policy); and
 - (14) section 395 (The FCA's and PRA's procedures).

Commencement

- B. This instrument comes into force on *[date]*.

Amendments to the Handbook

- C. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- D. The Decision Procedure and Penalties manual (DEPP) is amended in accordance with Annex B to this instrument.

Amendments to material outside the Handbook

- E. The Enforcement Guide (EG) is amended in accordance with Annex C to this instrument.

Notes

- F. In the Annex to this instrument, the "notes" (indicated by "**Note:**") are included for the convenience of readers but do not form part of the legislative text.

Citation

- G. This instrument may be cited as the Decision Procedure and Penalties Manual and Enforcement Guide (Review) Instrument 2016.

By order of the Board
[*date*]

ANNEX A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Insert the following new definition in the appropriate alphabetical position. This text is not underlined.

<i>focused resolution agreement</i>	(in <i>DEPP</i>) a <i>settlement agreement</i> that: <ol style="list-style-type: none"> (1) concerns proposed action that requires the <i>FCA</i> to issue a <i>warning notice</i>; (2) contains an agreement on all relevant issues of fact and all issues as to whether those facts amount to a <i>breach</i> (or more than one <i>breach</i>); and (3) leaves one or more other issues outstanding.
-------------------------------------	--

Amend the following existing definitions as shown.

<i>Settlement agreement</i>	(in <i>SYSC 18</i>) (Whistleblowing) an agreement between the <i>firm</i> and the <i>worker</i> which sets out the terms and conditions agreed by these parties for the purposes of settling a potential employment tribunal claim, other court proceedings or employment disputes. <u>(in <i>DEPP</i>) an agreement reached between a <i>person</i> who is or may be subject to enforcement action and <i>FCA</i> staff as part of the <i>settlement decision procedure</i>.</u>
<i>Settlement decision makers</i>	<u>(in <i>DEPP</i> and <i>EG</i>) two members of the <i>FCA</i>'s senior management, one of whom will be of at least director of division level (which may include an acting director) and the other of whom will be of at least head of department level, with responsibility for deciding whether to give <i>statutory notices</i> in the circumstances described in <i>DEPP 5</i>. At least one of the decision makers will not be from the Enforcement and Financial Crime Division.</u>
<i>Settlement discount scheme</i>	(in <i>DEPP</i> and <i>EG</i>) the scheme described in <i>DEPP 6.7</i> by which the financial penalty that might otherwise be payable,

or the length of the period of suspension or restriction that might otherwise be imposed, in respect of a person's misconduct or contravention may be reduced to reflect the timing of any ~~settlement agreement~~ settlement agreement.

ANNEX B

Amendments to the Decision Procedure and Penalties Manual (DEPP)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless indicated otherwise.

1 Application and Purpose

...

- 1.1.1 G This manual (*DEPP*) is relevant to *firms, approved persons* and other *persons*, whether or not they are regulated by the *FCA*. It sets out:

...

- (1B) the *FCA's* decision-making procedure where it is deciding under section 391(1)(c) of the *Act* to publish information about the matter to which a *warning notice* relates (see *DEPP* 3.2.14AG to *DEPP* 3.2.14HG and *DEPP* 5.1.8LG to *DEPP* 5.1.8RG);

...

3 The nature and procedure of the RDC

...

3.2 The operation of the RDC

RDC meetings and composition of panels

...

- 3.2.3 G The composition and size of panels of the RDC may vary depending on the nature of the particular matter under consideration. ~~In cases in which representations are made, it~~ It will be usual for the panel that is to consider the representations and decide whether to give a *decision notice* to ~~include additional~~ comprise the same members of the RDC who ~~have not~~ previously considered the matter. In particularly complex cases, or those raising novel points of law or practice, it might be appropriate for a larger panel to consider the case at both the warning notice and representations stage.

...

Procedure: general

...

3.2.11A G Where a *warning notice* is given on the basis of a *focused resolution agreement*, the *RDC* shall accept and not in any circumstances depart from the agreed position on the issues set out in that agreement.

...

3.2.14A G If *FCA* staff consider that it is appropriate to publish information about the matter to which a *warning notice* falling within section 391(1ZB) of the *Act* and given by the *RDC* relates, they will make a recommendation to the *RDC* that such information should be published.

3.2.14B G The *RDC* will then consider whether it is appropriate in all the circumstances to publish information about the matter to which a the *warning notice* falling within section 391(1ZB) of the *Act* relates. The *FCA*'s policy on publishing such information is set out in *EG* 6.

...

Procedure: representations

...

- 3.2.16 G (1) The recipient of a warning notice or a first supervisory notice may request an extension of the time allowed for making representations. Such a request must normally be made within ~~sevendays~~ seven days of the notice being given.
- (2) If a request is made, the Chairman or a Deputy Chairman of the *RDC* will decide whether to allow an extension, and, if so, how much additional time is to be allowed for making representations. In reaching his decision he will take into account all relevant factors including the legal and factual complexity of the case, as well as whether there are any factors outside the control of the firm or individual that would materially impact on their ability to respond within the period set out in the warning or first supervisory notice, and may take account of any relevant comments from the *FCA* staff responsible for the matter.

...

...

- 3.2.18 G The chairman of the relevant meeting will ensure that the meeting is conducted so as to enable:
- (1) the recipient of the *warning notice* or first *supervisory notice* to make representations;
 - (2) the relevant *FCA* staff to respond to those representations;

- (3) the *RDC* members to raise with those present any points or questions about the matter (whether in response to particular representations or more generally about the matter); and
- (4) the recipient of the notice to respond to points made by *FCA* staff or the *RDC*;

but the chairman may ask the recipient of the notice or *FCA* staff to limit their representations or response in length or to particular issues arising from the *warning notice* or first *supervisory notice*. If the *warning notice* was given on the basis of a *focused resolution agreement*, the recipient will be required to limit their representations to the issues that remain in dispute.

...

Procedure: decision notices and second supervisory notices

...

3.2.22A G If the *person* subject to enforcement action notifies the *RDC* that he wishes to make an expedited reference to the *Tribunal* under *DEPP* 5.1.8GG, the *RDC* shall decide whether to give a *decision notice* in light of any representations by any third party under section 393 of the *Act* and any interested party under section 63 or 67 of the *Act*: see *DEPP* 5.1.8IG.

3.2.23 G ~~However, if representations are made,~~ In any case in which representations are made and in accordance with *DEPP* 2.3.1G the *RDC* will consider whether it is right in all the circumstances to give the *decision notice* or a second *supervisory notice* (as appropriate).

...

5 Settlement decision procedure

...

5.1 Settlement decision makers

Introduction

- 5.1.1 G (1) A *person* subject to enforcement action may agree all issues relevant to a financial penalty or other outcome rather than contest formal action by the *FCA*. He may instead enter into a *focused resolution agreement* and in this way partly contest the proposed action: see *DEPP* 5.1.8AG to 5.1.8EG below.
- (1A) Further, even if the *person* subject to enforcement action wishes to fully contest the proposed enforcement action, he may choose to do so by agreeing to the *FCA* issuing the required *statutory notices* and then making an expedited reference of the matter to the *Tribunal*: see *DEPP* 5.1.8FG to 5.1.8KG below.

- (2) The fact that ~~he~~ a *person* does ~~so~~ any of these things will not usually obviate the need for a ~~statutory notice~~ *statutory notices* recording the *FCA's* proposal and decision to take ~~that~~ action. ~~Where, however, the person subject to enforcement action agrees not to contest the content of a proposed statutory notice, the decision to give that statutory notice will be taken by senior FCA staff. As set out in this chapter, senior FCA staff have a role to play in giving the requisite statutory notices:~~
- (a) where a person enters into a settlement agreement (other than a focused resolution agreement), senior FCA staff will give both the warning notice and decision notice;
 - (b) where a person enters into a focused resolution agreement, senior FCA staff will give the warning notice and the RDC will decide whether to give the decision notice; and
 - (c) where a person elects to make an expedited reference to the Tribunal before a warning notice has been issued, senior FCA staff will give the warning notice and decision notice.
- (3) These decisions by senior FCA staff will be taken jointly by two members of the *FCA's* senior management, one of whom will be of at least director of division level (which may include an acting director) and the other of whom will be of at least head of department level (the "*settlement decision makers*").

...

...

All the text is new and not underlined.

Procedure: focused resolution agreements

- 5.1.8A G A *focused resolution agreement* must include agreement on:
- (1) all relevant issues of fact; and
 - (2) all issues as to whether those facts amount to a *breach* (or more than one *breach*).
- 5.1.8B G Accordingly, where a *focused resolution agreement* is entered into, the *FCA* expects that the issue or issues remaining to be determined by the *RDC* in accordance with *DEPP* 5.1.8DG will normally be one or more of the following:
- (1) whether action for a financial penalty and/or *public censure* is

warranted;

- (2) the appropriate level of a financial penalty;
- (3) whether action for a suspension, restriction, condition or limitation (as defined for the purposes of *DEPP 6A*) is warranted;
- (4) the appropriate length of a suspension, restriction, condition or limitation (as defined for the purposes of *DEPP 6A*);
- (5) whether a *prohibition order* is warranted; and/or
- (6) the appropriate scope of a *prohibition order*.

5.1.8C G The terms of any proposed *focused resolution agreement*:

- (1) will be put in writing and be agreed by *FCA* staff and the *person* concerned;
- (2) may refer to a draft of the proposed *warning notice*; and
- (3) may, depending upon the stage in the enforcement process at which agreement is reached, include an agreement by the person concerned to:
 - (a) waive and not exercise any rights under sections 387 (Warning notices) and 394 (Access to Authority material) of the *Act* to notice of, or access to, material relied upon by the *FCA* and any secondary material which might undermine the *FCA* decision to give the *statutory notice*, save in relation to material that is relevant to issues which remain in dispute; and
 - (b) not dispute the issues agreed with the *FCA* when:
 - (i) making representations to the *RDC* in respect of a *warning notice* (whether in exercise of rights under section 387 of the *Act* or otherwise); or
 - (ii) on any subsequent reference of the matter to the *Tribunal* under section 208 of the *Act* (save insofar as the *Tribunal* decides of its own motion to reopen an issue or issues).

5.1.8D G Where the proposed settlement is on the basis of a *focused resolution agreement*, the role of the *settlement decision makers* shall be as follows:

- (1) The *settlement decision makers* will decide whether or not to give a *warning notice*. (For the avoidance of doubt, the *settlement decision makers* may meet the relevant *FCA* staff or the *person* concerned in accordance with *DEPP 5.1.5G* and any such meeting shall not affect the *settlement decision makers*' ability to decide whether or not to

give a *warning notice*).

- (2) If the *settlement decision makers* decline to give a *warning notice* based on the proposed settlement, they may invite *FCA* staff and the *person* concerned to enter into further discussions to try to achieve an outcome the *settlement decision makers* would be prepared to endorse.
- (3) If the *settlement decision makers* are satisfied with the proposed settlement, they shall give a *warning notice* recording the agreed position on agreed issues and the position of the *FCA* on issues which remain in dispute.
- (4) Where the *settlement decision makers* give a *warning notice*, the notice will specify the time allowed for making representations. This will not be less than 14 days.
- (5) The *settlement decision makers* will promptly inform the *RDC* that a *warning notice* has been given. The *RDC* shall then specify a time within which the recipient of the notice is required to indicate whether he wishes to make oral representations.
- (6) It will then be for the *RDC* to decide whether to give a *decision notice* under the procedure set out in *DEPP* 3.2.16G to 3.2.25G.

- 5.1.8E G For the avoidance of doubt, the decisions whether to agree a proposed *focused resolution agreement* and whether to approve any such proposed agreement are entirely within the discretion of the *FCA* staff and the *settlement decision makers* respectively.

Procedure: expedited references to the Tribunal

- 5.1.8F G (1) The purpose of this section is to define a procedure (the “expedited reference procedure”) enabling a *person* subject to enforcement action to challenge the proposed action before the *Tribunal* without engaging with the *FCA*’s internal decision-making process.
- (2) *DEPP* 5.1.8FG to *DEPP* 5.1.8IG set out the circumstances in which the expedited reference procedure is available, the steps a *person* must take to make use of the procedure, and how the procedure operates depending on whether it is invoked before or after the giving of a *warning notice*.
- 5.1.8G G The expedited reference procedure is available only if:
- (1) the proposed action requires the *FCA* to issue a *warning notice*;
 - (2) the *FCA* considers that it has a sufficient understanding of the nature and gravity of the *breach* to make a reasonable assessment of the appropriate penalty or other outcome; and

- (3) the *FCA* has communicated that assessment to the *person* concerned.
- 5.1.8H G In order to use the expedited reference procedure, the *person* subject to enforcement action must notify the *FCA* that he:
- (1) wishes to make an expedited reference to the Tribunal under *DEPP* 5.1.8HG; and
 - (2) waives and will not exercise any rights under section 387(2) of the *Act* in respect of the *warning notice* given (or to be given) in relation to the proposed action.
- 5.1.8I G To use the expedited reference procedure before a *warning notice* has been given:
- (1) the notification set out *DEPP* 5.1.8HG must be given to *FCA* staff;
 - (2) the decision to issue a *warning notice* will then be taken by the *settlement decision makers*; and
 - (3) the decision to issue a *decision notice* will also be taken by the *settlement decision makers*, in light of any representations by any third party under section 393 of the *Act* or any *interested party* under section 63 or 67 of the *Act*.
- 5.1.8J G To use the expedited reference procedure after a *warning notice* has been given:
- (1) the notification set out in *DEPP* 5.1.8HG must be given to the *RDC*; and
 - (2) the decision to issue a *decision notice* will then be taken by the *RDC* in light of any representations by any third party under section 393 of the *Act* and any *interested party* under section 63 or 67 of the *Act*.
- 5.1.8K G Once a *decision notice* has been given as part of the expedited reference procedure (whether by the *settlement decision makers* or the *RDC*), it is the responsibility of the *person* subject to enforcement action to seek to refer the matter to the *Tribunal* under the *Act* if he so wishes. If the matter is not referred to the *Tribunal* within the time required under section 390(1) of the *Act*, the *FCA* shall give a *final notice*.

Procedure: warning notice statements

- 5.1.8L G If *FCA* staff consider that it is appropriate to publish information about the matter to which a *warning notice* falling within section 391(1ZB) of the *Act* and given by the *settlement decision makers* relates, they will make a recommendation to the *settlement decision makers* that such information should be published.

- 5.1.8M G The *settlement decision makers* will then consider whether it is appropriate in all the circumstances to publish information about the matter to which the *warning notice* falling within section 391(1ZB) of the *Act* relates. The *FCA's* policy on publishing such information is set out in *EG 6*.
- 5.1.8N G If the *settlement decision makers* propose that the *FCA* should publish information about the matter to which a *warning notice* falling within section 391(1ZB) of the *Act* relates:
- (1) the *settlement decision makers* will settle the wording of the statement it proposes the *FCA* should publish (warning notice statement);
 - (2) the *FCA* staff will make appropriate arrangements for the warning notice statement that the *settlement decisions makers* propose the *FCA* should publish to be given to the *persons* to whom the *warning notice* was given or copied;
 - (3) the proposed warning notice statement will specify the time allowed for the recipient to respond in writing to the *settlement decision makers*. This will normally be 14 days;
 - (4) the recipient of a proposed warning notice statement may request the *settlement decision makers* to grant an extension of the time allowed for its response. Such a request must normally be made within seven days of the proposed warning notice statement being given; and
 - (5) the *settlement decision makers* will not normally grant a request by a person to whom the warning notice statement was given to make his response in person.
- 5.1.8O G If no response to the proposed warning notice statement is received, the *FCA* will make appropriate arrangements to publish the warning notice statement.
- 5.1.8P G However, if the *settlement decision makers* receive a response from the *person* to whom the proposed warning notice statement was given, the *settlement decision makers* will consider their response and decide whether it is appropriate in all the circumstances to publish information about the matter to which the *warning notice* relates.
- 5.1.8Q G If the *settlement decision makers* decide that the *FCA* should publish a warning notice statement:
- (1) the *settlement decision makers* will notify the relevant parties (including the relevant *FCA* staff) in writing of that decision;
 - (2) the *settlement decision makers* will settle the wording of the warning notice statement; and

- (3) the *FCA* will make appropriate arrangements for the warning notice statement to be published.

5.1.8R G If the *settlement decision makers* decide that the *FCA* should not publish a warning notice statement they will notify the relevant parties (including the relevant *FCA* staff) in writing of that decision.

...

In this text underlining indicates new text and striking through indicates deleted text, unless indicated otherwise.

6 Penalties

...

6.7 Discount for early settlement

...

The settlement discount scheme applied to financial penalties

6.7.2 G In appropriate cases the *FCA's* approach will be to negotiate with the *person* concerned to agree in principle the amount of a financial penalty having regard to the *FCA's* statement of policy as set out in *DEPP* 6.5 to *DEPP* 6.5D and *DEPP* 6.6. (This starting figure will take no account of the existence of the *settlement discount scheme* described in this section.) Such amount ("A") will then be reduced by a percentage of A according to the ~~stage in the process at which agreement is reached.~~ scheme set out in *DEPP* 6.7.3G. The resulting figure ("B") will be the amount actually payable by the *person* concerned in respect of the *breach*. However, where part of a proposed financial penalty specifically equates to the disgorgement of profit accrued or loss avoided then the percentage reduction will not apply to that part of the penalty.

6.7.3 G (1) ~~The *FCA* has identified four stages of an action for these purposes: A~~ settlement discount is available only in cases where a *settlement agreement* (which may be a *focused resolution agreement*) is reached during the period from commencement of an investigation until the *FCA* has:

(a) ~~the period from commencement of an investigation until the *FCA* has:~~ a sufficient understanding of the nature and gravity of the breach to make a reasonable assessment of the appropriate penalty; and

(i) ~~a sufficient understanding of the nature and gravity of the breach to make a reasonable assessment of the~~

~~appropriate penalty; and~~

- (ii) ~~communicated that assessment to the person concerned and allowed a reasonable opportunity to reach agreement as to the amount of the penalty ("stage 1");~~
 - (b) the period from the end of stage 1 until the expiry of the period for making written representations or, if sooner, the date on which the written representations are sent in response to the giving of a warning notice ("stage 2"); communicated that assessment to the person concerned and allowed a reasonable opportunity to reach agreement as to the amount of the penalty ("stage 1").
 - (c) ~~the period from the end of stage 2 until the giving of a decision notice ("stage 3");~~
 - (d) ~~the period after the end of stage 3, including proceedings before the *Tribunal* and any subsequent appeals ("stage 4").~~
- (2) The communication of the *FCA*'s assessment of the appropriate penalty for the purposes of *DEPP* 6.7.3G(1)(a) need not be in a prescribed form but will include an indication of the breaches alleged by the *FCA*. It may include the provision of a draft warning notice.
- (3) ~~The reductions in penalty will be as follows:~~

Stage at which agreement reached	Percentage reduction
Stage 1	30
Stage 2	20
Stage 3	10
Stage 4	0

In relation to any *settlement agreement* (including a *focused resolution agreement*) the reduction in penalty will be as follows:

- (a) 30% if the agreement is concluded during stage 1; and
- (b) 0% in any other case.

ANNEX C

Amendments to the Enforcement Guide (EG)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless indicated otherwise.

2 The FCA's approach to enforcement

...

2.2 Case selection and referral criteria ~~Firms and approved persons, market abuse cases and listing matters~~

2.2.1 Other than in the area of a *firm's* failure to satisfy the *FCA's Threshold Conditions* for authorisation (as to which, see paragraph 2.11), the selection method for cases involving *firms* and *approved persons*, *market abuse* and *listing matters* (for example, breaches of the listing, prospectus or disclosure *rules*) occurs at two main levels:

- (1) ~~strategic planning; and~~
- (2) ~~decisions on individual cases. [deleted]~~

...

2.2.6 ~~Before~~ In all cases, before it proceeds with an investigation, the *FCA* will satisfy itself that there are grounds to investigate under the statutory provisions that give the *FCA* powers to appoint investigators. ~~If the statutory test is met, it will decide whether to carry out an investigation after considering all the relevant circumstances. To assist its consideration of cases, the *FCA* has developed a set of assessment criteria. The current criteria (which are published on the Enforcement section of the *FCA* web site¹) are framed as a set of questions. They take account of the *FCA's* statutory objectives, its strategic/supervision priorities (see above) and other issues such as the response of the *firm* or individual to the issues being referred. Not all of the criteria will be relevant to every case and there may be other considerations which are not mentioned in the list but which are relevant to a particular case. The *FCA's* assessment will include considering whether using alternative tools is more appropriate taking into account the overall circumstances of the *person* or *firm* concerned and the wider context. Another consideration will be whether the *FCA* is under a Community obligation to take action on behalf of, or otherwise to provide assistance to, an authority from another *EU* member state. Paragraph 2.15 2.5.1 discusses the position where other authorities may have an interest in a case. If the statutory test is met, the *FCA* considers what is the most efficient and effective way of achieving the *FCA's* statutory objectives of protecting consumers, enhancing market integrity and promoting competition. A referral to Enforcement will be made if we consider that an investigation, rather than an alternative regulatory response, is the right course of action in all the circumstances. Enforcement action and other regulatory tools can be used in conjunction and are not mutually exclusive. To assist in making that decision, the *FCA* has developed~~

referral criteria that set out a range of factors we may consider in deciding whether to appoint enforcement investigators. The criteria are not exhaustive, and all the circumstances of a particular case are taken into account. Not all the criteria will be relevant to every case, and additional considerations may apply in certain cases. Any one of the factors alone may warrant the appointment of investigators and in some cases, including cases where breaches are self-reported, the misconduct may be so serious that there is no credible alternative to referral.

2.2.6A If a decision to refer an individual or firm to Enforcement is made, the *FCA* will explain and set out the criteria applied in coming to the decision to refer, and the reason(s) for the referral at the outset of the investigation.

Case selection: Disciplinary regulatory cases

2.2.6B The *FCA* has revised its referral criteria and these are published on the Enforcement section of the *FCA*'s website: <http://www.fca.org.uk/firms/being-regulated/enforcement/how-we-enforce-the-law/referral-criteria>. In considering whether an enforcement investigation is likely to further the *FCA*'s aims and objectives, the *FCA* considers factors that address the following issues:

- (1) the supporting evidence and the proportionality and impact of opening an investigation;
- (2) what purpose or goal would be served if the *FCA* were to end up taking enforcement action in the case; and
- (3) relevant factors to assess whether the purposes of enforcement action are likely to be met.

Case selection: Markets cases

2.2.6C In relation to non-criminal *market abuse* investigations, the revised referral criteria will be similarly applied in deciding whether to open such an investigation. However, given the often limited alternatives to enforcement action available to address *market abuse* (with many of the subjects typically unauthorised), greater emphasis will be given to the egregiousness and deterrence value of a particular case when making such decisions.

Case selection: Listing cases

2.2.6D As with *market abuse* cases, many of the non-enforcement tools are not available for use in cases involving listing regime *breaches*. This is because in many cases (aside from certain areas such as sponsors and primary information providers), there will be no on-going supervisory relationship with the listed companies in question, and no similar authorisation regime as there is with FSMA regulated firms and individuals. As a result, the ability to use many of the early intervention tools or restricting or limiting certain activities is not available and enforcement is likely to be the most effective (and sometimes only) regulatory tool available to address the misconduct.

...

2.12 Co-operation

...

2.12.2 On its web site, the *FCA* ~~has given~~ gives anonymous examples of where it has decided not to investigate or take enforcement action in relation to a possible *rule* breach because of the way in which the *firm* has conducted itself when putting the matter right. This is part of an article entitled ‘The benefits to firms and individuals of co-operating with the *FCA*’². However, in those cases where enforcement action is not taken and/or a formal investigation is not commenced, the *FCA* will expect the *firm* to act promptly to take the necessary remedial action agreed with its supervisors to deal with the *FCA*'s concerns. If the *firm* does not do this, the *FCA* may take disciplinary or other enforcement action in respect of the original contravention.

...

3 Use of information gathering and investigation powers

...

3.10 Liaison where other authorities have an interest

3.10.1 The *FCA* has agreed guidelines that establish a framework for liaison and cooperation in cases where certain other UK authorities have an interest in investigating or prosecuting any aspect of a matter that the *FCA* is considering for investigation, is investigating or is considering prosecuting. These guidelines are set out in Annex 2 to this guide.

Information requests in joint investigations with the PRA

3.10.1A In certain circumstances, it will be appropriate and expedient for the *FCA* and *PRA* to issue a joint information request where there is a joint investigation. Where a joint information request is issued to a *firm* or individual, the request will make it clear to which investigation(s) it relates.

...

4 Conduct of investigations

...

4.8 Scoping discussions

4.8.1 For cases involving *firms* or *approved persons*, the *FCA* will generally hold scoping discussions with the *firm* or individuals concerned close to the start of the investigation (and may do so in other cases). The purpose of these discussions is to give the *firm* or individuals concerned in the investigation an indication of: why the *FCA* has appointed investigators (including the nature of and reasons for the *FCA*'s concerns); the scope of the investigation; how the process is likely to unfold and an indication of the likely timing of the key milestones and next steps in the

investigation; the individuals and documents the team will need access to initially and so on. There ~~is~~ may be a limit, however, as to how specific the *FCA* can be about the nature of its concerns in the early stages of an investigation. The *FCA* team for the purposes of the scoping discussions will normally include the nominated supervisor if the subject is a fixed-portfolio relationship-managed firm.

- 4.8.2 In addition to the initial scoping discussions, there will be an ongoing dialogue with the *firm* or individuals throughout the investigative process. We will aim to give periodic updates at least on a quarterly basis covering the steps taken in the investigation to date as well as the next steps in the investigation and indicative timelines. Where the nature of the *FCA's* concerns changes significantly from that notified to the person under investigation and the *FCA*, having reconsidered the case, is satisfied that it is appropriate in the circumstances to continue the investigation, the *FCA* will notify the person of the change in scope.

4.9 Involvement of FCA supervisors during the investigation phase

- 4.9.1 A clear division between the conduct of the investigation ~~on the one hand~~ and the need to continue with the ongoing supervision of the *firm* ~~on the other may mean that the investigation does not~~ means that clarity as to who is carrying out what work and a focus on the different needs of the investigation and on-going supervisory work needs to be maintained. It is also important that the investigation can benefit as much as it might otherwise do from the knowledge of the *firm* or individuals that the supervisors will have built up, or from their general understanding of the *firm's* business or sector. ~~Before matters are referred to the Enforcement Division for investigation, FCA staff from its Enforcement Division will often work closely together with staff from the Supervision Division in order to determine the proper course of action to take.~~ Following a referral, the *FCA* takes the following general considerations into account in relation to the potential role of a supervisor in an investigation.

- (1) While it is clearly essential for the day-to-day supervisory relationship to continue during the course of any enforcement action, this need not, of itself, preclude a *firm's* supervisor from assisting in an investigation.
- (2) Such assistance will include: making the case team aware of the *firm's* business, history and compliance track record; the current supervisory approach to the area concerned; current issues with the *firm*; and acting as a sounding board on questions that emerge from the investigation about industry practices and standards and any market practice issues. Depending on the issues that arise, it may be appropriate for a supervisor to attend a progress meeting with the firm.
- (3) Equally, there may be circumstances where someone in the *FCA* other than the *firm's* supervisor can more effectively and efficiently provide information on the current supervisory approach to the area under investigation or current market standards. In this case it makes good sense for the *FCA* to draw on that other source of expertise.
- (4) In the event that a *firm's* supervisor becomes part of the investigation team, the *FCA* will notify the firm of this in the normal way.

- (5) Where a firm's supervisor does not become part of the investigation team, the investigation will keep the firm's supervisor (or referring area) updated as to the progress of the investigation.

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4.13 Preliminary findings letters and preliminary investigation reports

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- 4.13.3 In cases where it is sent, the preliminary findings letter will set out the facts which the investigators consider relevant to the matters under investigation (normally, as indicated above, by means of an annexed preliminary investigation report). And it will invite the *person* concerned to confirm that those facts are complete and accurate, or to provide further comment. *FCA* staff will allow a reasonable period (normally 28 days) for a response to this letter, and will take into account any response received within the period stated in the letter. They are not obliged to take into account any response received outside that period. If a firm or individual requests an extension to the period for responding to the preliminary findings report, the FCA will take into account the legal and factual complexity of the case, as well as whether there are any factors outside the control of the firm or individual that would materially impact on their ability to respond within the period set out in the preliminary findings letter.

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4.14 Joint investigations with the PRA

- 4.14.1 In some cases, it may be appropriate for both the *FCA* and the *PRA* to pursue investigations into different aspects of the same misconduct (see *EG 2.15A*).
- 4.14.2 In such cases, the guidance contained in this chapter will apply to the *FCA*'s investigation and the *FCA* will attempt to ensure that the subject of the investigation is not prejudiced or unduly inconvenienced by the fact that there are two investigating authorities. The PRA and the FCA investigation teams will keep each other and their respective supervisory teams informed as to the progress of the investigation. Discussions with the firm or individual under investigation should normally occur with the representatives of both regulators present.
- 4.14.3 Both the FCA and the PRA will seek to ensure that, as far as possible, their respective processes (whether for contested or settlement decision-making) occur in a coordinated and timely manner in a joint investigation. For example, the regulators will, where appropriate, endeavour to settle a joint investigation into a relevant firm or individual simultaneously.

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5 Settlement

5.1 Settlement and the FCA – an overview

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5.1.2 The possibility of settlement does not, however, change the fact that enforcement action is one of the tools available to the *FCA* to secure our *statutory objectives*. The *FCA* seeks to change the behaviour not only of those subject to the immediate action, but also of others who will be alerted to our concerns in a particular area. There is no distinction here between action taken following agreement with the subject of the enforcement action and action resisted by a firm before the *RDC* (including action taken following a *focused resolution agreement*). In each case, the *FCA* must be satisfied that its decision is the right one, both in terms of the immediate impact on the subject of the enforcement action but also in respect of any broader message conveyed by the action taken.

...

5.1.4 In recognition of the value of early settlement, the *FCA* operates a scheme to award ~~explicit discounts~~ a discount for early settlement of cases involving financial penalties, suspensions and restrictions. Details of the scheme, which applies only to settlement of cases where investigators were appointed on or after 20 October 2005, are set out in *DEPP* 6.7. This chapter provides some commentary on certain practical aspects of the operation of the scheme.

5.1.5 ~~Decisions~~ Some decisions on settlements and *statutory notices* arising from them are taken by two members of the *FCA*'s senior management, rather than by the *RDC* (*DEPP* refers to these individuals as the '*settlement decision makers*'). Full details of the special decision making arrangements for settlements are set out in *DEPP* 5.

5.2 When settlement decisions may take place

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5.2.3A The *FCA* will engage senior members of staff in discussions, by acting as the case sponsor, liaising where appropriate with the settlement decision-makers by attending a without prejudice meeting during discussions or arranging for the attendance of an appropriately senior *FCA* representative.

5.3 The basis of settlement discussions

5.3.1 ~~As described above, the *FCA* operates special decision-making arrangements under which members of *FCA* senior management take decisions on *FCA* settlements. This means that settlement discussions will take place without involving the *RDC*. As set out in *DEPP* 5, special decision-making arrangements apply in relation to settlement. The *person* concerned may agree all relevant issues with *FCA* staff (in which case the *settlement decision makers* will give all relevant *statutory notices*). Alternatively, a *focused resolution agreement* may be agreed (in which case the *settlement decision makers* are responsible for giving the *warning notice* and the *RDC* for giving the *decision notice*). The *FCA* would expect to hold any settlement discussions on the basis that neither *FCA* staff nor the *person* concerned would seek to rely against the other on any admissions or statements made if the matter is considered subsequently by the *RDC* or the *Tribunal* unless those admissions or statements are recorded in a *focused settlement agreement*. This will not, however,~~

prevent the *FCA* from following up, through other means, on any new issues of regulatory concern which come to light during settlement discussions. The *RDC* may be made aware of the fact negotiations are taking place if this is relevant, for example, to an application for an extension of the period for making representations.

- 5.3.2 If the settlement negotiations result in a proposed settlement of the dispute, *FCA* staff will put the terms of the proposed settlement in writing and agree them with the *person* concerned. The *settlement decision makers* (and, as the case may be, the *RDC*) will then consider the settlement matter under the procedures set out in *DEPP* 5. A settlement is also likely to result in the giving of *statutory notices* (see paragraphs 2.37 to 2.39).

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5.5 The settlement discount scheme

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- 5.5.2 Normally, where the outcome is potentially a financial penalty, the *FCA* will send a letter at an early point in the enforcement process to the subject of the investigation. This is what the *FCA* refers to as a stage 1 letter. The *FCA* will aim to give 28 days' notice of the beginning of stage 1 to allow the parties to make administrative arrangements, e.g. ensuring that key staff can be available to participate where necessary in any settlement discussions. Where appropriate, the *FCA* will offer a preliminary without prejudice meeting to explain the *FCA*'s view of the factual misconduct, and to give the *firm* or individual an opportunity to identify where they believe there are errors in the factual basis and to indicate the extent to which they agree with the outline findings.

[**Note:** Stage 1 is the period from commencement of an investigation until the *FCA* has a sufficient understanding of the nature and gravity of the *breach* to make a reasonable assessment of the appropriate penalty, and has communicated that assessment concerned and allowed a reasonable opportunity to reach agreement as to the amount of penalty.]

- 5.5.3 The scheme does not apply to civil or criminal proceedings brought in the courts, or to *public censure*, *prohibition orders*, withdrawal of *authorisation* or approval or the payment of compensation or redress.
- 5.5.4 There is no set form for a stage 1 letter though it will always explain the nature of the misconduct, the *FCA*'s view on penalty, and the period within which the *FCA* expects any settlement discussions to be concluded. In some cases, a draft *statutory notice* setting out the alleged *rule* breaches and the proposed penalty may form part of the letter, to convey the substance of the case team's concerns and reasons for arriving at a particular penalty figure. The *FCA* will identify the key evidence on which its case relies at the commencement of stage 1. While the *FCA* will identify the key evidence that underpins its outline findings, it will not generally provide evidence where that evidence is already in the possession of the *firm* or individual.
- 5.5.5 The timing of the stage 1 letter will vary from case to case. Sufficient investigative work must have taken place for the *FCA* to be able to satisfy itself that the

settlement is the right regulatory outcome. In many cases, the *FCA* can send out the stage 1 letter substantially before the *person* concerned is provided with the *FCA's* preliminary investigation report (see paragraphs 4.30 to 4.33). The latest point the *FCA* will send a stage 1 letter is when the *person* is provided with the preliminary investigation report.

- 5.5.6 The *FCA* considers that 28 days following a stage 1 letter will normally be the ‘reasonable opportunity to reach agreement as to the amount of penalty’ before the expiry of stage 1 contemplated by *DEPP* 6.7.3. Extensions to this period will be granted in exceptional circumstances only, and factors that will be taken into account in considering an application will include the extent to which factors outside the *firm's* or individual’s control will have a material impact on their ability to engage in settlement negotiations within the period set out in the stage 1 letter.

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6 Publicity

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6.2 Publicity during, or upon the conclusion of regulatory action

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Warning notice statements

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- 6.2.4 The decisions on whether to exercise the power to publish information about a *warning notice*, and if so what information to publish, will (subject to paragraph 6.2.4A) be taken by the *RDC* after it has consulted with the *persons* to whom the *warning notice* has been given or copied. The procedure the *FCA* will follow when making these decisions is set out in *DEPP* 3.

- 6.2.4A Where the *settlement decision makers* decide to issue a *warning notice*, they shall also take the decision on whether to exercise the power to publish information about a *warning notice* and if so what information to publish. The *settlement decision makers* will consult with the *persons* to whom the *warning notice* has been given or copied. The procedure the *FCA* will follow when making these decisions is set out in *DEPP* 5.



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY



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© Financial Conduct Authority 2016
25 The North Colonnade Canary Wharf
London E14 5HS
Telephone: +44 (0)20 7066 1000
Website: www.fca.org.uk
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