

To: HL Financial Services Regulation Committee

Subject: EMA response to Committee's call for evidence on FCA CP24/2 - Our Enforcement Guide and publicising enforcement investigations—a new approach

Date: 23 September 2024

This document has been prepared in response to the Committee's call for evidence regarding the inquiry into the FCA's proposed approach to publicly announce its launch of investigations into regulated firms, including electronic money institutions ("**EMIs**") and payment institutions ("**PIs**").

Publicising Investigations and the Impact on Regulated Firms

The EMA disagrees with the FCA's proposal to announce investigations including the names of subjects, and publish updates on those investigations, as it presents a risk of creating an unfair prejudice against them and impact their ability to retain customers. We do not consider these proposals are in the public interest nor are they consistent with the FCA's statutory objectives.

Before we proceed with addressing the specifics of the proposal we wish to put matters into context.

We note that the FCA has a strategic objective and three operational objectives (together "**Statutory Objectives**"), and would like to emphasise that the FCA's statutory objectives should always take priority over the FCA's strategic priorities:

- The "**Strategic Objective**" is to ensure that the relevant markets function well. [Section 1B of the Financial Services and Markets Act 2000 ("**FSMA**")]
- The operational objectives are:
 - to secure an appropriate degree of protection for consumers ("**Consumer Protection Objective**") [Section 1C(1) FSMA];
 - to protect and enhance the integrity of the UK financial system ("**Integrity objective**") [Section 1D(1) FSMA]; and
 - to promote effective competition in the interests of consumers in the markets for regulated financial services and services provided by recognised investment exchanges (RIEs) ("**Competition Objective**") [Section 1E(1) FSMA].
- The FCA's proposals to name and shame both firms and individual persons without any formal findings of wrongdoing will achieve the opposite of the Statutory Objectives.

Strategic Objective: The FCA's proposals will not "ensure relevant markets function well". The FCA's naming a firm as under investigation absent having finalised an investigation and reviewing all the relevant evidence of that firm's conduct is premature. Publicising a firm under investigation at the outset could result in unfair prejudice against that firm, affecting their ability to retain customers, engage new customers and defend themselves in the impending enforcement proceedings. By publicising a firm's name without a formal finding of responsibility, the FCA are risking turning viable businesses into insolvent ones. Customers and staff will lose faith, they will struggle to raise equity, find it harder to obtain loans or otherwise be given loans on less favourable terms than would have been the case had the firm's reputation not been unfairly prejudiced by the FCA. In the case of EMIs and PIs, an unfairly prejudicial publicising of a firm's name could result in that firm being terminated by strategic contractual partners such as banks who provide safeguarding accounts, resulting in immediate regulatory non-compliance and immediate discontinuation of business. Furthermore, the collapse of one EMI or PI could cause the risk profile of all other EMIs and PIs not subject to FCA investigation, to be reassessed by their contractual partners (notably banks), with the potential for a cascade of de-risking of EMIs and PIs that were not even subject to an FCA investigation – these would be the collateral damage of the announcement.

This is clearly not in the furtherance of markets "functioning well".

Consumer Protection Objective: The FCA's proposals to publicise a firm's name at the outset of an investigation prior to all evidence having been reviewed and absent a finding of responsibility will not have the effect of securing an appropriate degree of protection for consumers.

Considering the circumstances described above, firms experiencing turbulence because of a public announcement are likely to scale back their product offerings including the number and types of consumers they serve as they deal with the fall out. This would not increase consumer protection but constitute a loss of opportunity and a loss of capacity in the financial (and payments) services industry.

Integrity Objective: The FCA's proposals to publicise a firm's name at the outset of an investigation prior to all evidence having been reviewed and absent a finding of responsibility will affect the legitimacy and integrity of the UK financial system.

The FCA's continuously publicising the names of firms or individuals under investigation will result in consumers forming a particular view of the financial (and payments) services industry. Whilst the FCA can publicise the name of a firm under investigation on their own webpage and craft language carefully, the FCA has no control of how this announcement will be subsequently portrayed in the main stream media or by "citizen journalists" on social media. How will the FCA's announcement be portrayed in the Daily Mail or The Sun? Can the FCA guarantee that subsequent reporting of the FCA's announcement by media outlets such as these will not result in misinformation and unfair prejudice against the firm?

What is the FCA's impact assessment of how UK consumers will respond to such announcements?

First, we consider that an increase in the number of announcements of investigations into firms will result in UK consumers forming a negative view of the financial (and payments) services industry or certain sectors within the industry. It would not be unreasonable for consumers to think: Why does the financial watchdog have to investigate all of these financial firms? They must be really dodgy to warrant all of this investigating ...

Second, generally speaking, an FCA investigation from the outset to formal finding can take several years. Investigations could involve several instances of requesting information on the part of the firm, carrying out interviews, on-site audits, document review etc.

To financial services industry insiders (such as such as the FCA, regulated firms and their advisors) it is feasible that an investigation may not be resolved for several years. It is likely that consumers (who do not work in the industry or otherwise have industry experience) would view the FCA as ineffectual and slow if the FCA did not resolve an investigation in a short period of time (certainly no more than a year), which contradicts the FCA's ambition to significantly improve the pace and focus of investigations. We also note that MPs, generally speaking, are in the same position as consumers and are also likely to be alarmed by the FCA appearing to be ineffectual and slow, which could result in the FCA being subject to a political review.

In summary, the FCA's proposals to publicise the names of firms at the outset of investigations not only run the risk of unfairly prejudicing firms, they run the risk of unfairly prejudicing the FCA with consumers losing faith in the financial (and payments) services industry entirely when suddenly a lot of announcements of FCA investigations are made when the proposals are launched. Accordingly, in our view, the proposals could affect the integrity of the market for financial services and, therefore, is inconsistent with the Integrity Objective.

Competition Objective: The FCA's proposals to publicise a firm's name at the outset of an investigation prior to all evidence having been reviewed and absent a finding of responsibility will not promote effective competition – it will make the market for financial services less competitive. For example, as previously discussed above, by publicising a firm's name without a formal finding of responsibility, the FCA are risking turning viable businesses into insolvent ones. Customers and staff will lose faith, they will struggle to raise equity, find it harder to obtain loans or otherwise be given loans on less favourable terms than would have been the case had the firm's reputation not been unfairly prejudiced by the FCA.

UK banks, whose values generally fall between hundreds of billions of pounds and hundreds of millions of pounds, can likely withstand this – especially the CMA 9. Smaller players, such as EMLs and PIs cannot – these are more likely to fall within the category of SMEs.

From a revenue perspective, there is a disproportionate impact on SME financial institutions whose customers are not as sticky as the customers of the big retail banks and who do not have the deep

pockets to survive a potential temporary reduction in revenue arising from an announcement.

An unfairly prejudicial publicising of a firm's name could result in a small payment service provider being terminated by strategic contractual partners, such as banks who provide safeguarding accounts, resulting in immediate regulatory non-compliance and immediate discontinuation of business. This is not a risk that faces large UK retail banks. Large UK retail banks hold significant capital, can withstand loss and, unlike EMI and PIs, are not required to engage banking partners in order to provide their services to consumers.

Overall, if smaller players, such as EMI and PIs, become insolvent that means less market participants, which means less competition for the benefit of consumers.

Strategic, Integrity and Competition: Further to the points made above, we note that in specialised sectors of the industry, there may only be two or three market participants operating. If one of them were to fail because of the public announcement of an investigation, the customers of that firm would naturally migrate to the other participants, however, this would be an unexpected influx which these firms could not have anticipated and may not have an adequate framework to deal with (such as, in the case of EMI and PIs, sufficient safeguarding capacity, own funds and customer due diligence capacity). This could potentially push these firms into regulatory non-compliance and create market instability. The creation of such collateral damage by the FCA would not be in line with its Strategic, Integrity and Competition Objectives.

Conduct of the investigations

As a general comment, publicising a firm's name at the outset of an investigation prior to all evidence having been reviewed and absent a finding of responsibility will always prejudice the firm and, if the FCA is incorrect or otherwise unfounded in bringing an investigation, such prejudice will be unfair.

We note that the FCA does not always get its investigations right – there are legitimate concerns about the FCA's ability to conduct investigations and its ability take instructions from the courts. This is indicated in recent FCA enforcement decisions that have been overturned by the Upper Tribunal. For example:

In the case of Thomas Seiler, Louise Whitestone, Gustavo Raitzin and the Financial Conduct Authority [2023] UKUT 00133 (TCC) ("**Julius Baer 3 Case**"), the Upper Tribunal ("**UT**") stated:

- “It is therefore exasperating that basic errors still seem to occur ... There are only so many times that the Authority can apologise for its failings, insist that lessons have been learned and then expect that those affected should simply move on.”
- “there clearly seems to be a **continuing problem with the competence** of those to whom the Authority delegates the disclosure process and therefore the **adequacy of their supervision**. This is therefore a matter that the Authority should review in the light of the

failings identified in this decision, particularly the **unacceptable late disclosure** which occurred after the conclusion of the hearing of these references”

The above comments in the Julius Baer 3 Case points to a repeated failure by the FCA to conduct an investigation with a negative effect on the subject of its investigations and a waste of its own limited resources.

In the case of BlueCrest Capital Management (UK) LLP and the Financial Conduct Authority [2023] UKUT 140 (TCC) (“**BlueCrest Case**”), the UT stated:

- “The DN is not an impressive document. It demonstrates a **considerable amount of muddled thinking** on the part of the Authority and a **lack of clarity** as to the reasons it gives for its conclusion”

As with the Julius Baer 3 Case, the comment in the BlueCrest Case points to another failure by the FCA to conduct an investigation with a negative effect on the subject of its investigations and a waste of its own limited resources.

In the case of Mr Markos Markou and the Financial Conduct Authority [2023] UKUT 00101 (TCC) (“**Markou Case**”), in response to the UT’s decision, the FCA stated on its webpage addressing the Markou Case:

- “The Tribunal has published its decision in relation to our investigation into Mr Markos Markou. The FCA believes that **the decision is incorrect and irrational**. We will be seeking permission to appeal the decision.”

The same FCA webpage does not publish the decision of the UT or even a summary of the decision. However, it does have a link to FCA’s own decision notice. This paints a very misleading one-sided picture of the Markou case. This does not bode well for the FCA’s proposals.

Furthermore, it is unacceptable for the FCA to **use inflammatory language** about the UT in the way it does. It may well disagree with the UT’s decision and by appealing the decision it would argue the decision is incorrect and potentially irrational but until such time as such an appeal is granted the decision is the law – the wording should be along the lines of the FCA will challenge the decision as ... As a matter of law and fact, the UT is a superior court of record of equivalent status to the High Court of England and Wales, while the FCA’s views and beliefs are such that views and beliefs and do not hold any special status under the law.

Given these incorrect instances of enforcement, we consider there is material risk that the FCA could erroneously bring an investigation and publicise the name of a firm unfairly. We consider the risk of unfairly prejudicing a firm with an unsubstantiated or otherwise erroneous announcement is too great and the proposals set out in the CP should not proceed. We note that firms as legal person have a right to fair hearing under Article 6 of the ECHR (which is also set out the Human Right Act 1998).

Public Interest Framework and the Risk to Firms

The EMA does not agree with the structure and content of the proposed new public interest framework (“PIF”). While the FCA acknowledges that a public announcement may have a potential impact on its investigation subject, it deliberately does not include this as a specific factor in the PIF. The absence from the PIF of the FCA explicitly considering the impact on the firm that is the subject of investigation is not a case of the FCA complying with its Consumer Protection Objective but failing to meet any of its Statutory Objectives for the reasons given in our response to *Publicising Investigations and the Impact on Regulated Firms* (above). We would expect the FCA’s rebuttal to cite PIF as a mechanism for preventing publication where it might trigger the collapse of a firm.

We are of the view that public interest is insufficiently defined and that the factors that indicate whether something is in the public interest grant the FCA too much discretion especially in the absence any formal requirement to consider the impact on the firm. We would like to stress that if the PIF is to be implemented, it must undergo significant development in order to ensure it covers the matters that may be taken into account by the FCA comprehensively and precisely. There needs to be a clear published threshold for launching an investigation and incorporated into the PIF and clear threshold for publicly announcing that a firm is being investigated.

Accordingly, the PIF does not meet the FCA’s stated object of the PIF being “flexible, fair and proportionate”.

Handling Investigations Involving Individuals

The EMA considers the FCA’s approach to individuals to be broadly appropriate. We agree that individuals’ names should not be published from both a data protection perspective and an ECHR perspective, as this should limit the circumstances in which individuals are named to circumstances where, for example, the lawfulness of publicising the name is confirmed by an independent adjudicator, such a court. We note the FCA’s comment that there will be instances when the FCA can lawfully make such an announcement, when this is in the public interest. We assume that the FCA will obtain some kind of dispensation from a relevant decision maker prior to doing this (such as a court order) in order to ensure the FCA are correct in their determination that an individual’s name may be published in the circumstances. This would be a prudent approach due to the gravity of the situation and to ensure the FCA does not breach an individual’s data protection rights and / or a firm’s right to a fair hearing under Article 6 of the ECHR.

Content of FCA Announcements

We have set out our arguments above why investigation into firms should not be publicised generally – see our response to *Publicising Investigations and the Impact on Regulated Firms* (above). However, more specifically, we do not agree with the FCA’s including of a “summary of the suspected breach, failing or other misconduct being investigated”. If an investigation must be publicised, it is sufficient for the FCA to publish (i) the identity, and (ii) regulatory provisions to which the investigation relates

only. It is nascent to make any representations relating to the potential breach, failing or other misconduct. At the time of the publication, the FCA has not yet carried out a full investigation or reviewed all of the evidence. The FCA, at this early stage, is not able to substantiate a representation relating to “the potential breach, failing or other misconduct”.

We note that the FCA would be setting out its case without the firm under investigation being able to set out its explanation. This would likely lead to all the problems we have highlighted earlier in this response and is unlikely to be compatible with the right to a fair hearing under Article 6 of the ECHR.

The FCA’s announcements are meant to make clear that the opening of an investigation does not imply that it has reached a conclusion that there has been a breach, failing, or other misconduct unless it is inappropriate to do so.

The firm will be unfairly prejudiced by the initial announcement and on an ongoing basis throughout the investigation process. In the very least the statement needs to be considerably more robust to reduce the risk of harm by the announcement. An FCA announcement should give full effect to the firm’s procedural rights by indicating, for example, that the FCA has not yet reviewed all evidence, that the investigation can result in no action being taken against the firm, and that the presumption is that the firm is not in contravention of its obligations.

Timeframes for Public Announcements and Firm Notification

The EMA disagrees with the proposed method of providing only one day's notice prior to public announcements. The EMA urges the FCA to provide firms with sufficient time to respond and prepare, particularly for large or complex organizations that need to manage communications with various stakeholders. Notice is a fundamental right in the UK and the FCA must not curtail it. One day’s notice is not sufficient notice from a procedural fairness perspective. It does not give the firm sufficient time to prepare or otherwise respond. Large or complex organisations will face difficulties in responding to such a notice in an appropriately-governed and timely manner, with factors including that such organisations may need to: brief a large range of stakeholders, from directors to customer-facing staff, consider whether it is required to notify other regulators and prepare such notifications, prepare and approve a communications strategy and reactive media statements, and seek external advice from PR and legal experts.

Please note that the FCA have tacitly admitted that one day’s notice is inadequate and unfairly prejudicial to firms in their approach to listed firms. The FCA’s approach is that if an announcement or update is potentially market sensitive, the FCA will generally inform the subject of the announcement or update after markets have closed, publishing on their website at 7.00am and via an FCA-approved primary information provider.

If the subject is a listed company in another jurisdiction, and the announcement or update is potentially market sensitive, the FCA will, where possible, try to avoid publication during stock exchange hours in that jurisdiction.

This indicates the FCA knows that an announcement will negatively affect a firm’s reputation and

overall value, whether that firm is a listed or private company. If an FCA announcement would not have the effect of unfairly prejudicing a firm, what would be the nature of the market sensitivity at play?

Publicising Investigation Outcomes and Closures

The EMA disagrees with the FCA's proposal that where the FCA have published an announcement and subsequently close the investigation without regulatory, civil or criminal action; it will publish an announcement to that effect and/or amend the original announcement on its website.

It is unlikely that a statement from the FCA that a firm under investigation has the case closed without any enforcement action being taken will be considered as the firm being cleared – this is not a finding of innocence. Consumers will first and foremost read the initial publication naming and shaming the firm and this will form their view. Any subsequent announcement that rectifies or retracts the earlier announcement will not nearly be as impactful. The damage to the firm's reputation will already have been done.

We also note the FCA's conduct in the Markou Case (see our response to *Publicising Investigations and the Impact on Regulated Firms* above) where the FCA's comments on the UT's decision and the lack of a link to the UT's decision has a misleading effect.

Comments on the Revised Enforcement Guide

The EMA has concerns regarding the FCA's proposal to bar certain legal representatives from a compelled interview (Chapter 2), could have a negative impact on the interviewee and the candour with which they participate in such interviews. This is likely in circumstances where, as is common, interviewees will be supported by a firm's legal representatives in preparing for an interview, and the FCA is explicitly proposing that it be able to exclude such legal representatives on the basis that they owe a duty of disclosure to the firm.

The FCA's changes to the Enforcement Guide in relation to the use of privileged reports or supporting materials (Chapter 3) provided to the FCA on a limited waiver of privilege basis are concerning too. We understand the FCA will not accept any condition or stipulation about the use of material provided in such circumstances, and that it cannot "close its eyes" to information it receives. The FCA also states that the unfettered provision of such materials "may" be taken into account when determining any applicable penalty. It is apparent that such reports or materials are useful to the FCA, but they should be drafted for the sole purpose of providing the firm with legal advice and not with the intention of mitigating some later penalty.