

FCA Doubles Down On New Priorities With Target ID Plan

By **James Tyler** (June 3, 2024)

On April 30, the Financial Conduct Authority's consultation on the public naming of investigation subjects closed.

The consultation followed a Feb. 27 speech^[1] by Therese Chambers, joint executive director of enforcement and market oversight at the FCA, announcing the proposal — widely referred to as a plan to name and shame.^[2]

This has provoked a significant backlash from the market, influential financial services trade body U.K. Finance,^[3] the House of Lords and, quite exceptionally, the U.K. chancellor.^[4] Even more unusual is that, on May 2, FCA Chief Executive Nikhil Rathi was summoned to appear before a House of Lords committee to explain why the regulator had failed to pause the proposal, in light of these concerns.



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Proposal

Presently, those subject to investigation are usually not named until the FCA completes its investigation and identifies misconduct.

The FCA proposes to provide information about investigations opened at an early stage, including updates on progress and announcing the closure of investigations that do not lead to further action being taken.

The announcements will give the identity of the investigation subject, their industry sector and a summary of the misconduct under investigation. Notably, the FCA intends to give firms one business day's notice before any announcement and, interestingly, has chosen to not implement any form of appeal system.

The FCA has qualified its approach to individuals who are subjects, suggesting that there will not be a presumption to name them, and will only do so when it is in the public interest.

This new approach is premised on transparency and deterrence. The FCA states in the consultation paper that the changes will "address risks to consumers and investors in increasingly fast-moving and emerging markets" and increase public confidence in the market.

All laudable objectives, so why the opposition?

Background

To understand why the proposals have generated such opprobrium, one must look to their genesis. The changes appear to be a response to criticism of the regulator made in a 2022 report by the House of Commons Public Accounts Committee, concerning its handling of the British Steel Pension Scheme scandal.^[5]

Indeed, in a letter dated April 25, 2024, from the FCA's joint executive directors of enforcement to the House of Lords, the FCA refers explicitly to the "report into the British

Steel Pension Scheme" to justify its proposed changes.[6]

The part of the committee's report highlighted in the letter required the FCA to consider "whether it would be an option to publish lists of those under investigation, where there are significant grounds to believe they are committing serious harm to consumers."

In fact, the committee's criticisms in its 2022 report were wider ranging, and found that FCA was "slow to respond at all stages of the [British Steel] case, for example it failed to take effective preventative action after identifying problems" and had too great a focus on "professional sanctions, rather than referrals for criminal activity."

Accusations that the FCA is slow to act and ignores criminality in favor of regulatory action are not new. These were covered in some detail by an independent review of the FCA's handling of another scandal — London Capital & Finance PLC — published in 2020.[7]

To some, it seems odd that the FCA has chosen to propose the significant changes that it has, without proposing substantial changes in the areas in which enforcement really requires improvement: Looking back to British Steel, the naming of investigation subjects would not have solved the problem of too little action, too late by the regulator.

FCA Objectives

To some, therefore, this is a solution in search of a problem.

The FCA's counterargument is that naming subjects would reduce the current timeline, often several years, between the opening of an investigation and the naming of a subject at the point at which it decides to take action.

The consultation paper and Chambers' February speech both provide helpful summaries of the wider objectives underpinning the proposals. These are:

- Making other firms aware at a much earlier stage of the process of important issues where they may need to examine their own conduct and processes and raise standards;
- Enhancing public confidence and demonstrating that the FCA is deploying its investigation tools for the protection of consumers and markets, building trust in the system — this includes providing assurance to investors who may have been subject to significant harm, or even fraud, that matters are being investigated;
- Tackling the delay between misconduct occurring and a penalty being imposed if the FCA is to boost confidence in our markets;
- Improving the FCA's own accountability, and enabling greater, more timely and more granular scrutiny of the FCA's effectiveness; and
- Encouraging witnesses to come forward.

No one could object to such noble aspirations, but few believe that the proposals are necessary to achieve this. For those looking for a detailed analysis of this, U.K. Finance, an organization rarely involved in spats with public bodies, has set out in detail why the FCA already has the required tools.[8]

In particular, the FCA already has, and has done for some time, a set of rules concerning publicity during its investigations in its Enforcement Guide.[9]

To see the extent to which these are already tailored to the objectives discussed, it is worth looking at the existing criteria. In exceptional circumstances the FCA will publicize names under these criteria in order to:

- Maintain public confidence in the financial system or the market;
- Protect consumers or investors;
- Prevent widespread malpractice;
- Help the investigation itself, for example by bringing forward witnesses; or
- Maintain the smooth operation of the market.

Any assessment under the current regime must also consider potential prejudice caused to current or potential investigation subjects.

The FCA also has a number of other tools to communicate good and poor practice, or identify areas of concern, such as its "Dear CEO" letters, policy documents and regular thematic reviews.

In terms of accountability, the FCA also regularly publishes its performance metrics, and could of course provide greater, anonymized detail, should it wish.

There are, however, two clear differences between the current regime and the proposal in the consultation paper. The first is the troubling notion that the latter will not have assessment of potential prejudice to the investigation subject as a specified criterion.

The second is that rather than publicity being the exception, there will now be a presumption in favor. Most obviously, the FCA clearly intends to identify as many subjects as possible and arguments concerning potential harm caused by this will not trump the FCA's objectives.

Collateral Damage

The force of feeling against these changes reflects a genuine fear that they may damage the U.K.'s economy. This is all the more acute where the changes appear to do little to address the regulator's actual problems.

Borrowing language from the U.K. House of Lord's Financial Services Regulation Committee's response to the proposal, which asked the FCA to halt the proposal pending further consideration, it "risks having a disproportionate effect on firms named in investigations ... risks the overall integrity of the market, including through possible unwarranted impacts on share prices," and risks that individuals' reputations may be "unfairly tarnished."[10]

Others, such as U.K. Chancellor Jeremy Hunt, are also concerned that because equivalent jurisdictions do not name investigation subjects in the same way, the FCA's changes would make the U.K. uncompetitive.[11]

As well as the impact on markets, there is also the small matter of procedural fairness. The allegations publicized will be unproven, yet will have an adverse impact on the subject,

including, potentially, their banking relationships, investor behavior and their ability to raise capital. The allegations could also have an inadvertent adverse effect on the confidence of employees, rating agencies and suppliers.

In many cases, the identity of individuals responsible for the matters under investigation will also be readily inferable.

Respondents to the consultation are concerned that the FCA's cost-benefit analysis has not considered the risks outlined above adequately, indicating that the FCA has either not thought through, or disregarded, the adverse impact of its plans.

FCA Response to Criticism

Despite strength of feeling, the FCA is holding firm and has responded to criticism in a letter to the House of Lords.[12]

The tone of the letter has exacerbated some feeling in the market. In particular, the FCA denies its policy is one of naming and shaming because the language used in announcement will be "factual and measured."

For some, this misses the point; the substance of the harm arises from being identified as a subject, however phrased. The letter also responds to the criticism that the proposals excluded prejudice to firms as one of the criteria to be applied when making publicity determinations, asserting that although not specified, this would fall within the relevant circumstances that would be considered.

The letter goes on to explain that harm was not specified as a criterion because the FCA had prioritized its statutory objectives and the public interest. This rather affirms that harm caused to firms will be a secondary consideration, at best.

FCA's Changing Approach to Enforcement

The consultation will also be particularly jarring to regulated firms that have lived through the FCA's recent changes to its approach to investigations.

In 2017, under Mark Steward, the FCA's former executive director of enforcement and market oversight, firms were told that investigations were a diagnostic tool used to identify where misconduct was occurring, rather than indicating where it has been found or areas of concern.[13]

Accordingly, very large numbers of investigations were opened without publicity, ran for long periods, and were frequently closed without enforcement action being taken.

This does not sit well with the authority's new approach — that being the subject of an investigation should be a deterrent to others — and is surprising when the authority still has a number of legacy investigations opened under Steward's tenure, with no suggestion that they will be expedited before the changes to publicity are implemented.

Additionally, and as observed by a number of consultees, if fewer enforcement cases are opened in the future, then the impact on those identified will be more significant; they are more likely to be viewed as likely to have committed misconduct.

However, his consultation should also be viewed as part of a wider change in the FCA's

focus. Since the appointment of the new joint executive directors of enforcement, there has been an emphasis on the authority's use of its wider powers in a more cohesive manner.

This is to be welcomed. It is also understood that the FCA intends to present plans for an integrated approach to regulation, with enforcement exercised as one facet of it. It may also be that, in the context of wider, impending changes, there is a rationale for greater publicity. This remains to be seen.

Nonetheless, the FCA has also amplified its message that it expects firms to be proactive and take responsibility for their failings, and has indicated that such behavior may help firms avoid regulatory penalties.[14]

It is difficult to see how this encouragement sits well with the risk that any consequent investigation, irrespective of findings or penalties, could result in public identification.

Conclusions

It seems likely that these changes will be implemented, one way or another. What does this mean for regulated firms and their advisers?

First, it means that publicity will be the rule, rather than the exception. Firms will have to consider how they respond to being named, and whether they require external expertise. They will also have to consider what they tell staff, counterparties and those with whom they bank.

This will be more complicated for those already subject to long-running investigations who, for good reason, may have decided to not inform counterparties, employees or other key stakeholders.

For those advising firms at the preinvestigation stage, there will be an even greater emphasis on the importance of avoiding an investigation.

Firms will have to consider carefully what diagnostic and remedial work can be done, at an early stage when making a report, or immediately afterward, to dissuade the regulator that enforcement action is necessary.

Firms and their advisers should also be ready to provide persuasive representations that they not be named, at very short notice.

Finally, considering the impact of publicity on firms, challenges via judicial review and applications for injunctive relief seem inevitable. Those affected should keep a beady eye on developments.

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[1] Speech by Therese Chambers, joint executive director of enforcement and market

oversight, delivered at The Market Abuse and Market Manipulation Summit on 27 February 2024.

[2] CP24/2 <https://www.fca.org.uk/publications/consultation-papers/cp24-2-enforcement-guide-publicising-enforcement-investigations-new-approach>.

[3] UK Finance has issued a highly critical response to the consultation: A response by UK Finance to the FCA's Consultation Paper 24/2 on its Enforcement Guide and publicising enforcement investigations – a new approach <https://www.ukfinance.org.uk/system/files/2024-04/UK%20Finance%20%20response%20to%20FCA%20enforcement%20guidance%20CP24-2.pdf>.

[4] Jeremy Hunt warns FCA against 'naming and shaming' business under investigation, Financial Times, 30 April 2024 <https://www.ft.com/content/21094236-73d0-4d40-aa64-4c298d0140a7>.

[5] House of Commons Committee of Public Accounts, Investigation into the British Steel Pension Scheme Fourteenth Report of Session 2022–23 Report, 21 July 2022. <https://committees.parliament.uk/publications/23164/documents/169426/default/>.

[6] Letter from Therese Chambers and Steve Smart, Joint Executive Directors of Enforcement, FCA to the Financial Services Regulation Committee, House of Lords, dated 25 April 2024 <https://committees.parliament.uk/publications/44575/documents/221409/default/>.

[7] The 'Gloster Report', Report of the Independent Investigation into the Financial Conduct Authority's Regulation of London Capital & Finance plc, by Dame Elizabeth Gloster, 23 November 2020 https://assets.publishing.service.gov.uk/media/5fda3d698fa8f54d60878b2f/Gloster_Report_FINAL.pdf.

[8] A response by UK Finance to the FCA's Consultation Paper 24/2 on its Enforcement Guide and publicising enforcement investigations – a new approach <https://www.ukfinance.org.uk/system/files/2024-04/UK%20Finance%20%20response%20to%20FCA%20enforcement%20guidance%20CP24-2.pdf>.

[9] FCA Enforcement Guide, EG 6.1 <https://www.handbook.fca.org.uk/handbook/EG/6/1.html>.

[10] Letter from House of Lords Financial Services Regulation Committee to FCA, dated 18 April 2024 <https://committees.parliament.uk/publications/44344/documents/220473/default/>.

[11] Jeremy Hunt warns FCA against 'naming and shaming' business under investigation, Financial Times, 30 April 2024 <https://www.ft.com/content/21094236-73d0-4d40-aa64-4c298d0140a7>.

[12] Letter from Therese Chambers and Steve Smart, Joint Executive Directors of Enforcement, FCA to the Financial Services Regulation Committee, House of Lords, dated 25 April 2024 <https://committees.parliament.uk/publications/44575/documents/221409/default/>.

[13] See, e.g., 'A better view' Speech by Mark Steward, Director of Enforcement and Market Oversight at the FCA, delivered at the AFME European Compliance and Legal Conference 2017: <https://www.fca.org.uk/news/speeches/better-view>.

[14] As articulated, for example, by Therese Chambers in her first speech in role, 'Do the right thing', delivered at the City & Financial FCA Investigations and Enforcement Summit on 1 June 2023 <https://www.fca.org.uk/news/speeches/do-right-thing>.