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COMPLIANCE OFFICER BULLETIN

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ANNUAL REVIEW 2011

1. Introduction

2012 famously marks "the end of time" in Mayan calendars and the less reputable outreaches of the internet are awash with "prophecies" that there will be some form of transformative or apocalyptic event during the year. It seems unlikely that these prophets had in mind the end of the FSA's once much vaunted "light-touch" regulation, but we can now be certain that 2012 will mark the beginning of a new era of prescriptive and interventionist financial regulation in Europe and the United Kingdom.

This *Bulletin* reviews the creation of the new European regulatory bodies and, in particular, the powers granted to European Securities and Markets Authority ("ESMA"). In this context, the *Bulletin* discusses some of the significant European and UK regulatory changes that are expected to come into force and be implemented during 2012.

In particular the *Bulletin* considers the European Union's proposed Short Selling and Market Infrastructure regulations, each of which are expected to come into force in 2012 and will be directly applicable to UK firms. The *Bulletin* also highlights some of the proposals that have been made by the European Commission for legislation amending and/or replacing both MiFID and the Market Abuse Directives.

2012 will also be the year in which the Coalition Government's decision to replace the Financial Services Authority ("FSA") will be implemented. The *Bulletin* reviews the new UK regulatory structures that will come into being in 2012 and considers some of the new powers that have been granted to the FSA's replacement regulator under the revised Financial Services and Markets Act 2000 ("FSMA"), including significant interventionist

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powers in respect of investment products and financial promotions. The *Bulletin* also notes that the requirement imposed by FSMA on the FSA to consult the market when considering the application of new rules will remain in place (without any carve-out for European rules) and contrasts this with the European Union's increasing use of regulations with direct effect on UK firms (is it possible that the requirements of the regulations will simply not be included within the FSCA rulebook?).

Despite the changes expected in 2012, the work of the regulators has continued apace in 2011. The *Bulletin* analyses the significant reinforcement of principles-based regulation found in the High Court's judgment in respect of the BBA's application for judicial review of the FSA in respect of the PPI matter. Finally, we distil some of the key enforcement actions of 2011 with a view to identifying the regulator's key areas of activity and corresponding risk areas for firms.

2. EU developments

January 1, 2011 marked the coming into force of the new European financial services regulatory architecture. This was an unheralded but significant shift in the way in which financial services law and regulation applicable to the industry in the United Kingdom will be developed, promulgated and enforced. The European Union replaced advisory bodies, such as the Committee of European Securities Regulators ("CESR"), with regulatory authorities armed with not just influence but also significant power.

In this section of the *Bulletin* we intend to revisit the new European financial services regulatory architecture and take a detailed look at the governance and powers of the European Securities and Markets Authority ("ESMA"). Space does not allow for a similar discussion in respect of the banking or insurance authorities (the European Banking Authority ("EBA") and the European Insurance and Occupational Pensions Authority ("EIOPA") respectively), but these two bodies have analogous powers to ESMA within their respective industries.

We will then consider some of the key regulations and directives that the European Union has been developing in 2011 and which are likely to come into force during 2012 (noting where appropriate, the additional powers of ESMA embodied within them).

2.1 The role of ESMA within the new European financial services regulatory architecture

In January 2011 the three existing "Committees of Supervisors" were replaced with three "European Supervisory Authorities" ("ESAs") each sitting beneath the European Systemic Risk Board (the "ESRB") of the European Central Bank. The EBA, EIOPA and ESMA have similar functions and roles within their respective industry sectors in that they are responsible for developing and implementing European-wide legislation. They are each additionally required to report any developing risks within their sector to the ESRB which has a mandate to set the regulatory agenda with a view to mitigating systemic risk within the European financial services industry.

ESMA has widespread powers and responsibilities that it must exercise with a view "to protect[ing] the public interest by contributing to the short, medium and long-term stability and effectiveness of the financial system".[1] ESMA is required to cooperate with each of the EBA and EIPA so as to ensure that the rules applicable to the financial sector are adequately implemented to preserve financial stability and to ensure confidence in financial services as a whole.

ESMA is governed by a Board of Supervisors comprising the heads of the national authorities from each Member State (i.e. currently, the FSA in the United Kingdom). Representatives from each of the European Commission, the ESRB, EBA, and EIOPA sit on the board in a non-voting capacity. Most decisions will be taken by simple majority, on the basis of one country, one vote. As a result, the United Kingdom will have the same weighting as Malta or Latvia (i.e. just one of 27 voices). The main exception is for decisions on technical standards, where qualified majority voting will be used (and the United Kingdom has 8.4 per cent of the votes, rather than 3.7 per cent).[2] (For comparison, it is interesting to note that the United Kingdom accounts for 36.3 per cent of the European Union's wholesale finance market.[3])

ESMA has key powers in respect of:

- *Decisions and technical standards:* ESMA is responsible for providing draft technical (implementing and regulatory standards) for endorsement by the Commission and for making certain key decisions under the directives for which it has responsibility.
- *Powers of investigation and enforcement:* ESMA has general powers to investigate allegedly incorrect applications of law (including technical standards) and enforce compliance. Moreover, it may do so both on its own initiative, and at the request of the European Parliament ("the Parliament"), European Council ("the Council"), European Commission ("the Commission"), Stakeholder Group, or one or more national authorities. Furthermore, where "the orderly functioning and integrity of the markets" is under threat,[4] or even merely "to maintain or restore neutral conditions of competition in the market", ESMA has the power to require market participants in a particular jurisdiction to do or refrain from taking particular action in the event that a national authority has first failed to comply with a request from ESMA to impose such a requirement.[5] This power is separate from the "emergency powers" discussed below, and has a lower trigger point.
- *Dispute settlement:* ESMA is empowered to settle disputes between national authorities by taking a decision requiring them to take or refrain from specific action. It can do this either on the request of an authority, or on its own initiative, and its mediation role is legally binding.
- *Monitoring and assessing market trends:* ESMA will be able to seize the regulatory initiative as a result of its responsibility for monitoring new and existing financial activities and collecting information from national authorities. As it will inform the ESA, EIOPA, the ESRB, the Parliament, the Council and the Commission about relevant micro-prudential trends, potential risks and vulnerabilities, it will set the regulatory agenda. It will report on the impact of potential market developments on participants, the need to prohibit or restrict certain types of financial activities, and may conduct inquiries into particular financial activities. It is therefore likely that ESMA will propose future regulatory initiatives.
- *Third country issues:* ESMA will take the lead role with respect to third country issues. It will be responsible for the registration and withdrawal of AIFMs from outside the European Union, mediating any difference among national authorities in respect of non-EU AIFMs' compliance and conduct, recognising non-EU CCPs, and registering and withdrawing registration of depositories located in third countries approved by the Commission.
- *Emergency powers:* ESMA has further powers that will give it direct jurisdiction over firms in the United Kingdom in "emergency situations".[6] ESMA may adopt individual decisions requiring national authorities, such as the FSA, to take specific action to address risks. In the event that the FSA (or any other national regulator) does not comply, ESMA can also adopt individual decisions addressed directly to a financial market participant.

Although the effects have not been fully felt by the industry, this summary of the powers granted to ESMA may help to illustrate why the creation of the ESAs was an event that may have been even more momentous for the United Kingdom's financial services industry's than the changes to the UK regulatory framework that are proposed to come into force in 2012 (and which are discussed later in this *Bulletin*).

It is clear that ESMA and the other ESAs will have a significant role in shaping the detailed rulebooks to which UK financial services firms are subject and that, indeed, their creation paves the way to a common European rulebook.

2.2 European legislative proposals

The increased power and influence of European regulatory bodies can be seen both in the number and scope of European directives and regulations affecting the financial services industry that have been under discussion in 2011 and which are expected to come into force in 2012. Some of the key legislative proposals are discussed below.

2.2.1 Short Selling Regulation

In October 2011, the Commission of the European Union (the "European Commission") and the European Parliament Committee on Economic Affairs ("ECON") reached a political agreement on the broad scope of the regulations restricting short sales of shares, sovereign debt and sovereign debt-related credit default swaps ("CDSs"). It is expected that the resulting "EU Short Selling Regulations" will have been approved by the European Parliament shortly before publication of this *Bulletin* and that they will come into effect by the end of 2012. When they do come into force, the EU Short Selling Regulations will have direct effect (meaning that they will be legally binding on all market participants, without the need to be implemented by laws in each of the Member States of the EC). Accordingly, when they do come into force the EU Short Selling Regulations will replace, or override, the UK's existing rules on short selling that can be found in Pt 8A of the FSMA and the FSA's Financial Stability and Market Confidence Sourcebook.

The EU Short Selling Regulations will apply to the short selling of the shares listed on an exchange or a market in the European Union ("Relevant Shares"), even where the actual trading may take place outside the European Union, although, as discussed below, there is a limited exemption for shares whose principal listing is outside the European Union.

The EU Short Selling Regulations also restrict the short selling of derivatives that relate to Relevant Shares and cover debt instruments issued by or on behalf of one or more EU state ("Sovereign Debt"), as well as CDSs issued for the purpose of hedging against risks associated with Sovereign Debt ("Relevant CDSs").

2.2.1.1 Disclosure requirements

A person engaged in short selling Relevant Securities is subject to two levels of notification requirement—private and public. When a short position reaches or exceeds the relevant 0.2 per cent of issued share capital and upon changes to such positions of 0.1 per cent or more (i.e. at 0.3 per cent, 0.4 per cent etc), that position will be notified to the relevant EU regulator on a confidential basis.

However, when the position exceeds 0.5 per cent, disclosure will be required to the market as a whole.

A person engaged in short selling Sovereign Debt and Relevant CDSs is required to notify the relevant regulator of its short position if it exceeds the relevant threshold (to be set by the ESMA). There is no related public disclosure obligation.

The notification and disclosure obligations described above expressly apply to persons domiciled or established within or outside the European Union.

2.2.1.2 Naked short selling

Naked shorting of Relevant Securities, Sovereign Debt or Relevant CDSs is not permissible under the EU Short Selling Regulations.

A person engaging in short selling of shares will be regarded as engaging in naked short selling where he has not borrowed or otherwise made reasonable arrangements to ensure that settlement can be effected when due. ESMA will be required to implement technical standards as to what amounts to a "reasonable arrangement".

A person shall be considered to be engaging in naked short selling in respect of Sovereign Debt if he enters into a Relevant CDS which is not being used to hedge against either the risk of default where that person has a long position in the Sovereign Debt to which the Relevant CSD relates, or against the risk of a decline in the value of sovereign debt if that person holds assets, or is subject to liabilities, the value of which is correlated to the value of the relevant Sovereign Debt. It is expected that there will be secondary legislation or guidance issued by ESMA which will define the meaning of "correlated" for this purpose.

A central counterparty in an EU state responsible for clearing short sale transactions must ensure that there are arrangements in place for a buy-in of shares if the person selling short cannot settle within four days of due settlement date. To the extent the buy-in is not possible, the buyer must receive a payment as compensation (i.e. market price of shares plus losses arising from failure to settle). The person selling short must be liable for the buy-in costs or payments made to the buyer. A person engaged in short selling who fails to settle as agreed must also be liable to make daily payments for each day of failed settlement until buy-in or compensation.

2.2.1.3 Suspension of restitution

As partial recognition of concerns expressed by market participants that restricting the use of Relevant CDSs would make it more difficult for Member States to sell bonds, the EU Short Selling Regulations permit a national regulator temporarily to suspend the naked short selling restrictions on Sovereign Debt for an initial period of six months, subject to further renewals, if the liquidity of relevant Sovereign Debt falls below a certain threshold. A national regulator may also temporarily suspend the naked short selling restrictions on Relevant CDSs for an initial period of 12 months, subject to further renewals, if it believes that the restrictions may damage the sovereign debt market in the relevant EU state (e.g. by increasing the cost of borrowing).

It is unclear whether the EU Short Selling Regulations are intended to have extraterritorial applicability to prevent naked short selling of Sovereign Debt within and outside the European Union, or if the EU intends to rely on cooperation agreements with non-EU regulators to enforce the naked short selling restrictions.

2.2.1.4 Exemptions

An exemption from the disclosure and notification obligations, as well as from the ban on naked short selling, is available for Relevant Securities (but not for Sovereign Debt or Relevant CDSs) where the principal trading venue of the Relevant Shares is an exchange or market outside the European Union. The Regulations specify that the turnover of the Relevant Shares on different exchanges or markets will be assessed in order to determine the "principal trading venue".

The Regulations also provide an exception in respect of Relevant Securities, Sovereign Debt and Relevant CDSs applies to market making. In addition, authorised primary dealers of Sovereign Debt are exempt from the notification obligations and the naked short selling restrictions regarding Sovereign Debt and Relevant CDSs. Both of these exemptions are subject to a requirement on the person intending to short to notify the relevant regulator of his intention prior to entering into a naked short selling transaction, and to the regulator not prohibiting the use of the exemption by that person.

Certain other exemptions are also available, notably in relation to lawful stabilisation and buy-back activities. Persons operating under an exemption are liable to provide information to the relevant regulator at the regulator's request.

2.2.1.5 Exceptional circumstances

The EU Short Selling Regulations grant wide powers to national regulators to determine that certain financial instruments or certain classes of financial instruments are subject to the disclosure and notification obligations and the naked short selling restrictions. A national regulator may also suspend all shorting of such specified financial instruments or classes of financial instruments in exceptional circumstances (i.e. where there are adverse events of developments which constitute a serious threat to financial stability or market confidence in the state of the relevant regulator or in one or more other EU states, and where the measure is necessary to address the threat).

National regulators may also temporarily suspend short selling activities of Relevant Securities in case of significant falls in the price of the Relevant Shares over a trading day. A significant fall in value is described as 10 per cent or more of share value for liquid shares. A significant fall in value is yet to be determined in relation to illiquid shares.

In addition, ESMA may, if there is a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system in the European Union, and there are cross-border implications, require persons who have short positions on specific financial instruments or class of financial instruments to notify the relevant national regulator or publicly disclose the position(s), or prohibit persons from entering into short positions on certain financial instruments, or impose conditions on certain persons' short selling activities in order to address such threat.

2.2.2 European Market Infrastructure Regulation

Throughout 2011 there have been continued negotiations between the European Commission, Parliament and the Council of Ministers in respect of the European Market Infrastructure Regulation ("EMIR") which have most recently manifested themselves in the form of a compromise text proposed by the Polish presidency of the European Union in August 2011.[7]

EMIR is intended as the European Union's fulfilment of the agreement between G-20 leaders that all standardised OTC derivative contracts should be cleared through Central Clearing Counterparties ("CCPs") by the end of 2012, while non-centrally cleared contracts should be subject to higher capital requirements and be reported to trade depositories. This agreement was reached in the aftermath of the 2007–08 financial crisis and was intended to address perceived weaknesses in the derivatives market, particularly regarding transparency around a derivative trader's cumulative positions and exposure which makes it difficult for both counterparties and regulators to monitor and assess risk.

Although EMIR has still not been finalised, it is clear that it will require that (i) "eligible" OTC derivatives (i.e. contracts which have met pre-defined eligibility criteria) will have to be cleared through CCPs; (ii) certain details of non-eligible OTC derivative transactions will need to be reported to registered trade repositories; and (iii) financial counterparties and non-financial counterparties who exceed the clearing threshold that enter into an OTC derivative contract which is not cleared by a CCP will be required to ensure that appropriate procedures and arrangements are in place to measure, monitor and mitigate operational and credit risk. Each of these requirements is discussed in more detail below.

EMIR will also establish mechanisms for the authorisation and supervision of the CCPs themselves, in particular requiring that the CCP has sufficient liquidity and capital to ensure the effective operation of the market.

2.2.2.1 The clearing obligation

EMIR will require ESMA to maintain a public register (accessible on its website) that "unequivocally" indentifies the classes of derivatives eligible for central clearing and the CCPs that have been authorised to clear them.[8] ESMA will be required to determine whether to admit a class of derivatives to this register when (i) it has been informed by a national regulator that it has authorised a CCP to clear a particular type of contract in accordance with implementing technical standards to be adopted by the Commission (following advice to be delivered by ESMA by July 2012); or (ii) having identified a particular class of contracts that may be suitable on its own initiative. In either case, such determination may only be made following a public consultation and following endorsement by the Commission of implementing standards prepared by ESMA that take account of the overarching aim of reducing systemic risk and criteria including the degree of standardisation of the relevant class of contracts, the volume and liquidity of those contracts and the availability of fair and generally accepted pricing information.[9]

Once ESMA has determined that a class of derivatives should be cleared centrally, all financial counterparties (i.e. all banks, insurance companies and investment firms, including investment funds authorised pursuant to UCITS or the Alternative Investment Fund Managers Directive, authorised within the European Union) will be required to clear any transactions in that class of contracts (other than intragroup transactions) that are entered into with either another financial counterparty or any entity established outside the European Union that would be subject to the clearing obligation if it was established in the European Union through a CCP.[10] A non-financial counterparty may also become subject to the obligation to clear its contracts through a CCP to the extent that its cumulative derivative positions exceed a "clearing threshold" that will be determined by ESMA on a periodic basis (and, where its cumulative positions fall below that threshold for at least 30 days in a three-month period, it will no longer be subject to the requirement).[11]

2.2.2.2 The reporting obligation

EMIR will introduce a requirement for certain details of OTC derivative transactions that are not eligible for central clearing to be reported to registered trade repositories with a view to ensuring that information in respect of the risks associated with those contracts will be centrally stored and easily accessible to ESMA, regulators and relevant central banks. Accordingly, financial counterparties will be required to report the details of any OTC derivative contract entered into, modified or terminated to a registered trade repository. The report should be made no later than the working day following conclusion, modification or termination of the contract. The information that is to be contained in the report remains to be determined (by the Commission following a recommendation from ESMA), but is likely to include the parties to the contract and a description of its main characteristics (including the underlying reference asset or contract, maturity and notional value).[12]

2.2.2.3 Arrangements to measure, monitor and mitigate operational and credit risk

EMIR will additionally require counterparties, whether or not they are financial counterparties, that enter into OTC derivative contracts which are not eligible to be centrally cleared to ensure that they put in place appropriate procedures and arrangements to measure, monitor and mitigate operational and credit risk including at least the timely confirmation of the terms of the OTC contract and "robust, resilient and auditable processes in order to reconcile portfolios, to manage the associated risk and to identify disputes between parties early and to resolve them and to monitor the value of outstanding contracts".[13] This requirement is clearly (and is clearly intended as) a significant disincentive to use contracts that have not been approved by ESMA for central clearing.

2.2.3 MiFID II

In October 2011 the EU Commission published the results of its review of the Markets in Financial Instruments Directive ("MiFID") in the form of a proposal for a new replacement directive and a supplementary regulation (together "MiFID II").[14] MiFID has been in force since November 2007 and establishes the regulatory framework in Europe for the provision of investment services (such as brokerage, investment advice and management, dealing and underwriting) by banks and investment firms and for the operation of regulated markets. The European Commission had initiated its review of MiFID in the context of the financial crisis of 2007–08 and the G-20 commitment to improve the organisation, transparency and oversight of various segments of the financial services markets. It was therefore inevitable that the proposals made by the EU Commission for MiFID include various extensions of the directive's scope and a reduction in the discretions available to individual Member States.

For reasons of space it is not possible to detail all of the changes to MiFID proposed by the EU Commission. However, some of the proposals that are most likely to have a significant impact, including new consumer protection requirements, detailed requirements for the management of investment firms, specific rules around high-frequency trading and market integrity, and a new third country regime are considered below.

Other proposals made by the EU Commission within MiFID II include the creation of a new category of capital markets for small and medium-sized enterprises, extension of the MiFID regime to the market in emissions trading created by the EU emissions trading scheme, extended powers in respect of derivatives and harmonised sanction powers for regulators across the European Union.

The Commission has also proposed that the MiFID II regulation be used to extend pre- and post- trade transparency requirements and the application of those requirements to trading in bonds and derivatives.

Many of the changes proposed in MiFID II are based on advice provided by ESMA to the Commission and the draft directive envisages a significant role for ESMA in preparing the technical implementing measures (likely to be the first significant step to a single European rulebook) and will have an increased role in certain supervisory tasks such as, for example, determining the conformity with MiFID II of a market operator's application to waive pre-trade transparency requirements ("dark pools"). ESMA will also be mandated to take any steps necessary to coordinate actions by national competent authorities regarding investment products that it deems may put either investor protection or financial stability at risk.

The timeline for implementation of MiFID II is not clear. The Commission's proposal is in the form of both a re-casting of the existing directive, which will need, once adopted, to be passed into national laws, and a regulation which will have direct effect shortly after it is adopted. It is therefore possible that these proposals will be introduced in a phased manner and that firms may be required to comply with some of them (in particular the extended transparency requirements) as soon as 2012.

2.2.3.1 Corporate governance requirements

MiFID currently requires the persons who "effectively direct" an investment firm to be of good repute and sufficiently experienced to ensure the sound and prudent management of the firm. The Commission proposes to develop this requirement so that individual directors will not only have reputation and experience, but also "sufficient knowledge, skills … and commit [to] sufficient time to perform their duties".

The Commission also proposes that limitations are imposed on the number of directorships that may be held at any one time (no more than two non-executive positions for an individual who is also an executive director).

Furthermore, investment firms will be required to ensure that their management body collectively has "adequate … knowledge, skills and experience to be able to understand the investment firm's activities, and in particular the main risk involved in those activities". The management body will have regulatory responsibility for ensuring that the firm is managed in a sound and prudent way and in a manner that promotes the integrity of the market and the interests of its clients (but the proposal does not address how this may conflict with the duties of directors to shareholders).[15] ESMA will be required to develop technical standards establishing detailed criteria for the satisfaction of these requirements.

2.2.3.2 High-frequency trading

The Commission has proposed that investment firms that engage in "algorithmic trading", that is where a computer algorithm automatically determines individual parameters of orders (including timing, price quantity and post-order management) with little or no human intervention, be subject to a requirement to ensure that its trading systems are resilient and have sufficient capacity, are subject to appropriate trading thresholds and limits, do not send erroneous orders or otherwise function in a way that may "create or contribute to a disorderly market" (including trading in any manner that is contrary to the market abuse regime).

A requirement that is likely to prove particularly controversial with the fund managers that rely on their proprietary trading systems and which tend to regard them as highly confidential commercial information, is the compulsory disclosure to the regulator, on an at least an annual basis, of a description of the algorithmic trading strategies that they use together with the details of the compliance and risk controls (including trade limits etc) that they have put in place.[16]

Further restrictions on high-frequency trading will be introduced by requirements on market operators to introduce systems that limit the ratio of unexecuted orders to transactions that may be entered onto the system by a trader and which are able to slow down the flow of orders if there is a risk that its system capacity is reached.[17]

2.2.3.3 Market Integrity

MiFID II will require the operators of markets to put in place "effective system, procedures and arrangements to ensure that its trading systems are resilient" and in particular to ensure that it has systems and arrangements to reject orders that exceed pre-determined volume and price thresholds or which are clearly erroneous. This must include an ability temporarily to halt trading if there is a "significant" price movement in a particular security.[18]

2.2.3.4 Consumer protection requirements

Clearly motivated by losses suffered by retail investors during the financial crisis, the Commission has proposed significant extensions of MiFID's consumer protection regime. Accordingly, MiFID II will require that where investment advice is provided, the consumer must be provided with information confirming whether it is provided on an independent basis and whether it is based on a broad or more restricted view of the market. Where advice is provided on an independent basis a firm will be required to "assess sufficiently large numbers" and diverse types of financial instrument and may not limit the review to issuers or product providers linked to the firm. Firms providing independent investment advice or portfolio management will not be permitted to accept fees, commissions or other monetary benefit from any person other than their client (i.e. firms will be required to charge a fee to clients for independent advice).[19] The interaction of this requirement with the detailed requirements of the FSA's RDR is not yet entirely clear.

2.2.3.5 Best execution

The current best execution regime will be maintained, but investment firms will need to publish their top five execution venues on an annual basis and execution venues will be required to make available to the public, on a free of charge basis, information about the quality of trade execution on that venue.[20]

2.2.3.6 Third country regime

The EU Commission proposes in MiFID II a new regime for relationships with "third country" firms (i.e. firms incorporated outside the European Union). At present, Member States have their own laws in this area—in the United Kingdom there is the "overseas person" regime encapsulated in art.72 of the Regulated Activities Order. However, MiFID II will allow third country firms to provide investment services into the United Kingdom only where the third country has "equivalent" (as determined by ESMA) protection for investors.

Further, firms that wish to provide services to retail customers will be required to establish branches in the European Union. Authorisation for the branches will only be available where the "third country" has tax and regulatory cooperation arrangements in place with the host EU Member State, the branch has sufficient initial capital at its free disposal and management who satisfy the corporate governance requirements outlined above. However, once authorised branches will be permitted to passport that authorisation throughout the European Union.[21]

2.2.4 Market Abuse II

The EU Commission also published in October 2011 its proposals for amendments to the existing Market Abuse Directive ("MAD"). These proposals took two forms.

The first is a draft regulation which will effectively replace MAD[22] (the "MAD II Regulation"). Perhaps the most significant impact of this will be that the regulation will have direct effect throughout Europe and will replace (or supplement) existing market abuse regimes in all Member States (including the civil market abuse regime currently provided for by FSMA, s.118). In general terms, the MAD II Regulation replicates the existing market abuse regime under MAD but then extends it in important and far-reaching ways. For example, the draft regulation extends the application of the market abuse regime to include not just financial instruments admitted to listing on a regulated market but also to financial instruments traded on multilateral trading facilities and to other trading venues and to OTC financial instruments and commodity derivatives; includes a new abusive behaviour of attempting to manipulate the market (although MAD, and the current FSMA, s.118, defines market abusive behaviour to include attempts to deal on inside information it does not include (unsuccessful) attempts to manipulate the market); and seeks to harmonise the sanctions that may be imposed by the Member State's local regulators on persons who commit market abuse.

In what might be seen as something of a compliment to the United Kingdom, the Commission, in art.6 of the MAD II regulation, seeks to extend the definition of inside information to include information which is not of a precise nature, but which "if it were available to a reasonable investor, who regularly deals on the market ... would be regarded by that person as relevant when deciding the terms on which transactions ... should be effected".[23] The United Kingdom of course has, since the coming into force of the FSMA in 2001, maintained a market abuse offence in respect of trading on this type of "relevant" information, despite not being required to so by MAD. The Commission intends that this offence be used to prosecute trading based on information that is not subject to the requirement on issuers to disclose inside information because it is not yet precise (e.g. private information about advanced but not finalised contract negotiations).

The second is a draft directive[24] (the "MAD II Directive") which will require Member States to make it (to the extent they have not already) a criminal offence to intentionally trade on the basis of inside information, to improperly disclose inside information or to manipulate a market by giving false or misleading signals as to the supply or demand for a financial instrument, using fictitious devices or other forms of deception to enter into a transaction, securing the price of one or several financial instruments at an abnormal or artificial level or disseminating false or misleading information. Attempting to abuse the market in these ways or inciting, aiding or abetting others to do so will all also be required to be criminal offences. This marks a very significant departure from the original "civil" market abuse regime which was introduced, in the United Kingdom, as a parallel series of offences to the existing criminal insider dealing offences and which were intended to provide the regulator with a mechanism for pursuing cases of market abuse without being required to demonstrate to a jury that the offence had been committed "beyond reasonable doubt". It is to be assumed that, in the United Kingdom, these parallel civil and criminal insider dealing regimes will continue to operate alongside each other (albeit as amended in accordance with the MAD II Directive and Regulation).

As with MiFID II, the timetable for the implementation of MAD II is not yet clear. Each of the MAD II Directive and Regulation have been passed to the Parliament and Council of Ministers for negotiation and adoption. It should be borne in mind however that that the MAD II Regulation will have immediate applicability to market participants very shortly after it is adopted.

3. UK regulatory reform

3.1 New regulatory architecture

The government's reform of the UK regulatory architecture has been widely reported on and the form of the new institutional structure was set out in the HM Treasury White Paper published in June 2011 (the "June White Paper"). The June White Paper set out the draft Financial Services Bill ("the Bill") which is envisaged to come into force by the end of 2012. The Bill provides the framework for the new regulatory framework for financial regulation in the United Kingdom, and amends existing legislation, including the Financial Services and Markets Act 2000.

The Bill assigns the responsibility for protecting and enhancing the stability of the financial system of the United Kingdom to the Bank of England. In addition, the Bill introduces three new regulatory institutions which shall replace the Financial Services Authority ("FSA"). We outline below the new regulatory structure and main features of the new regulators.

3.1.1 New regulatory bodies

3.1.1.1 Financial Policy Committee

The Financial Policy Committee ("FPC") will be a macro-prudential regulator within the Bank of England. The FCP will be established as a committee of the Court of the Bank of England[25] and it will be concerned with protecting and enhancing the stability of the UK financial system. The FPC has been tasked with identifying and monitoring systemic risks and taking action to remove or reduce the same.

3.1.1.2 Prudential Regulation Authority

The Prudential Regulation Authority ("PRA") will be a subsidiary of the Bank of England, but will be operationally independent of the Bank. The general statutory objective of the PRA is "promoting the safety and soundness of PRA-authorised persons" and the insurance objective of the PRA is to contribute to the "securing of an appropriate degree of protection for those who are or may become policyholders".

The PRA will be responsible for micro-prudential regulation[26] of financial institutions that are deemed systemically significant due to the size of the risks they carry on their balance sheets and that require a sophisticated level of prudential regulation. This will include banks and insurance undertakings as well as complex investment firms. A number of firms will therefore be dual regulated by the PRA and by the FCA for conduct purposes. The definitions as to which firms will be regulated by PRA is still unclear.

The Treasury will be empowered to issue secondary legislation designating certain kinds of activities as "PRA-regulated activities" and to allow the PRA in due course to develop its own designation criteria to determine which firms should properly be supervised by it. It is expected that at least deposit-taking activities and insurance activities will fall within the remit of the PRA. It will be necessary to wait for the secondary legislation in order finally to confirm the scope of the activities regulated by the PRA. For example, although the PRA will be the lead regulator the Society of Lloyd's and Lloyd's managing agents, Lloyd's members agents and Lloyd's brokers are expected to be FCA-regulated firms.

The Bill provides that the PRA shall be the lead regulator in respect of dual-regulated firms subject to supervision by both the PRA and the FCA. The PRA would be permitted to veto an action to be taken by the FCA if it is likely to lead to the disorderly failure of a firm under its supervision or threaten the stability of the UK financial system.[27]

3.1.1.3 Financial Conduct Authority

The Financial Conduct Authority ("FCA") will be a company limited by guarantee, like the FSA. The operational objectives of the FCA are the "securing of an appropriate degree of protection for consumers", the "protecting and enhancing the integrity of the UK financial system", and "promoting efficiency and choice in the market".[28]

The strategic objective of the FCA is "protecting and enhancing confidence in the UK financial system".[29]

The regulatory remit of the FCA will include conduct of business supervision across the spectrum of regulated persons, and it will regulate the conduct of banks, insurers and complex investment firms which fall under the prudential supervision of the PRA. However, as noted above, the exercise by the FCA of its supervisory powers will be subject to the veto rights of the PRA with respect to PRA-authorised firms.[30] Although the FCA will be the sole regulator of firms which are not PRA-authorised firms, if the FCA-regulated firm's immediate group (i.e. the firm's parent and subsidiary undertakings, and any subsidiary of its parent undertaking or vice versa) includes a dual-regulated firm, the FCA may need to consult with the PRA in certain circumstances.

In addition, the FCA will be the prudential regulator for all entities required to be authorised and regulated which are not supervised by the PRA. The FCA will also be responsible for matters such as short-selling and market abuse. The FCA will succeed the FSA as the UK listing authority.

3.1.2 Enhanced powers

The Bill provides the FPC, the PRA and the FCA with a range of powers to discharge their obligations and sets out the statutory principles according to which the regulators are required to operate. Existing powers, exercised by the FSA, will be transferred to the appropriate new regulatory institutions. The Bill also creates certain new powers for the regulators.

It is currently envisaged that, with respect to the FPC, its powers will include a power to make public pronouncements and warnings, make recommendations to the PRA and the FCA, but also to other bodies, including perimeter recommendations to the Treasury (to determine which entities or activities should be regulated, and by which regulator), and the power to direct the PRA and the FCA where explicitly provided for by a Treasury order approved by the Parliament.[31]

The reforms seek to foster a more proactive approach to, and a more interventionist mode of regulation for, the conduct of business regulation of the financial services. In light of this aim, the Bill gives certain new powers to the FCA. Such powers include a power to intervene with the sale or promotion of financial products,[32] the sales and marketing materials for the financial products and the early publication of details of the start of enforcement proceedings against a firm for breaches of rules or failure to comply with regulatory requirements[33] (each of which is discussed below).

In addition, with regard to the FCA's role as the UK listing authority, the government has provided certain enhanced regulatory powers with respect to listed entities and sponsors.

3.1.3 Principles

The regulators are required to act according to the statutory principles,[34] including principles requiring the resources of each regulator to be used in the most efficient and economic way, proportionality, consumer responsibility, senior management responsibility for compliance, and transparency.

3.1.4 Coordination

Coordination by the regulators of actions and decisions generally, and with respect to dual-regulated undertakings specifically, will be key to the success of the new regulatory framework. Each regulator will have separate rule-making powers and a separate rulebook, although the PRA is under a statutory obligation to consult with the FCA before making rules to ensure regulatory consistency and minimise overlap for dual-regulated firms.

The PRA and the FCA are under a statutory obligation to coordinate the exercise of their respective qualifying functions with a view to ensuring mutual consultation before exercising their powers in a way that may adversely affect the other regulator's operations or objectives, on matters within the remit or expertise of the other regulator and on matters of common regulatory interest.[35] The regulators are also required to enter into and maintain a memorandum of understanding setting out the role of each regulator in relation to the exercise of its functions.[36] In addition, the boards of each regulator shall have representation of the other regulator in order to ensure proper communication on high-level, strategic issues.

3.1.5 Coordination with Europe

The Bill also requires that the memorandum of understanding between the regulators will contain provision coordinating the PRA and FCA's relations with the ESMA.

The Bill also retains FSMA's requirement for the regulators to consult on all rules, with no exceptions being made in Europe.

It will be interesting to see how this position is reconciled with the promulgation of EU regulations which will have direct effect in the United Kingdom (e.g. the EU Short Selling Regulations).

3.2 Changes to existing legislation

As described above, the June White Paper includes the draft Financial Services Bill ("the Bill") which sets out a number of changes to the current framework of financial regulation in the United Kingdom. The bulk of the changes are attributable to the changes in the regulatory architecture (i.e. the creation of the PRA and the FCA as successors to the FSA). However, the Bill also introduces certain new powers and requirements applicable to authorised firms or to the new regulators by introducing a number of changes to the FSMA, and an overview of the most significant changes is set out below.

3.2.1 Product intervention

The new s.137(c) of the FSMA as set out in the Bill grants the FCA new product intervention powers, allowing the FCA to make rules prohibiting or restricting authorised persons from exposing consumers to certain financial products.

The FCA will be able to restrict or prohibit consumer exposure to certain products by making rules that ban or restrict (e.g. by exposing conditions or specific requirements) an authorised person from (i) entering into such agreements as the FCA may specify in its rules ("specified agreement") with any person or with persons specified by the FCA in its rules (e.g. retail customers), or (ii) entering into a specified agreement without having complied with the specified conditions or requirements imposed by the FCA in the rules, or (iii) taking any action which could result in the entry into a specified agreement by the persons specified by the FCA or such persons holding an economic interest of any kind in a specified agreement, or (iv) taking any action described above in (iii) without having complied with the specified conditions or requirements imposed by the FCA in the rules.

The FCA may determine that, similarly to the existing provisions on unenforceability of agreements resulting from unlawful financial promotions, agreements or obligations created in breach of the product intervention rules may be unenforceable against the consumer, and that the money or property paid by the consumer under the relevant agreement or obligation may be recovered by the consumer, and that the authorised person in breach of the product intervention rules must pay compensation for any loss incurred by the consumer as a result of acquiring the product.

The product intervention rules will be effective irrespective of whether the entering into a "specified agreement" itself constitutes a regulated activity, and whether the specified agreements are with the relevant authorised person or with another person.

The FCA may exercise its power to make product intervention rules when it deems that an intervention is "necessary or expedient" for advancing its consumer protection, or efficiency and choice objectives, that is, broadly, to prevent significant consumer detriment. This gives the FCA wide discretion to determine when to invoke its powers to ban or restrict the sale and distribution of products.

The Bill expressly states that the power to make product intervention rules can only be used to advance the FCA's integrity objective by a separate order of the Treasury, in relation to which the Financial Policy Committee may advise the Treasury. This reflects the concerns expressed in the consultation responses that the product intervention power is unlikely to be appropriate to the protection of professional or wholesale customers.

3.2.1.1 Temporary product intervention rules

The FCA will also be able to make temporary product intervention rules, valid for up to 12 months, without prior consultation or a cost–benefit analysis.[37] However, such temporary rules may only be made in previously established circumstances in accordance with a published policy statement. The FCA will be required to consult on the policy statement. The FCA may also not use its temporary product intervention powers to re-issue rules which have lapsed after the expiry of the 12-month period, or to issue rules the content or effect of which are substantially the same as the content or effect of the lapsed rules. If the FCA wishes to extend a temporary rule beyond the 12-month period, it must carry out a prior public consultation and a cost–benefit analysis.

3.2.1.2 Scope

The FCA's product intervention power is sufficiently wide to capture all types of exposure by consumers to the specified product, including providing, selling, arranging and providing investment advice in respect of the specified product. The product intervention rules may apply to all types of circumstances, agreements, arrangements or products, including to circumstances or products resulting in indirect exposure to the product (e.g. exposure to a product through a complex product chain, or through a trust arrangement).

It is the government's intention that the definition of "specified agreement" be sufficiently wide to capture all arrangements, and there is an express provision which specifies that references to an "agreement" include "arrangements", such that the product intervention rules can, if appropriate, cover collective investment schemes, described in FSMA as "arrangements", and other ways of structuring the provision of or exposure to the product which might not otherwise fall within the general definition of an "agreement".

3.2.2 Financial promotions

The Bill allows the FCA to make rules, subject to restraints determined by the Treasury, if any, applying to authorised persons in respect of financial promotions, pursuant to the prohibition on financial promotions by unauthorised persons other than where the financial promotion has been approved by an authorised person.[38]

In addition, if the FCA considers that there has been, or is likely to be, a contravention of financial promotion rules in respect of a communication, or an approval of a communication, the FCA will, under the Bill, have the power to give a direction to an authorised person, in respect of a communication to be made by another person, to (i) withdraw a communication it has made or to refrain from making a communication it is intending to make, or (ii) withdraw the approval it has given, or refrain from approving a communication it is intending to approve. In addition, a direction given by the FCA may also require the authorised person to make public details of the FCA's direction and to do anything else that the FCA specifies in the direction in relation to the communication or approval.

Therefore, an authorised person who has issued or approved a communication that breaches the FCA's rules on financial promotions may be directed to actively withdraw such communication from the market and/ or make a public announcement stating it is withdrawing the material and, if required by the FCA, take other steps (e.g. contact customers or distributors or other intermediaries to inform them of the withdrawal of the communication or approval and explain reasons for such withdrawal, and to contact consumers who have acted upon the promotion). An authorised firm must also not make or approve a financial promotion that is effectively the same as the financial promotion in relation to which the FCA has previously made a direction.

The purpose of giving the FCA the power to make the financial promotions directions is to allow the FCA to intervene without delay to avoid or minimise detriment or loss to consumers, including to prevent consumers from being misled.

The FCA is required to give written notice to the authorised person receiving a direction relating to a communication. The notice must be given to the authorised person and, if the direction relates to an approval, also to the person whose communication the approval relates to. The notice must include details of the direction, state that the direction is immediately effective, note the FCA's reasons for giving the direction, and state that the authorised person is entitled to make representations to the FCA within a certain time period.

3.2.2.1 Publishing directions

During the time period when the authorised person may make representations, the FCA cannot make public that it has given such notice. After the period for making representations has expired, the FCA must amend, revoke or confirm its original direction. Actions required by the FCA for the authorised person to take, set out in the direction, are effective immediately, except for any requirement for the authorised person to publish information about the direction, which requirement will be effective at such time as the FCA makes a final decision regarding the direction.

Once the FCA has decided which action to take, it must publish such details of the direction and the action it has taken as it considers appropriate. The FCA's duty to publish directions made under the new power seeks to increase the visibility of the FCA's activities and to make public instances of poor and good market practices.

Certain provisions in the Bill will afford a measure of protection to authorised persons from reputational damage as a result of regulatory action. In addition to the requirement that the FCA must give written notice setting out certain matters as discussed above, the FCA will also have discretion as to the contents of the direction that it will publish (although the FCA does not have discretion to decide not to publish the direction) and, where it deems it appropriate, the published direction may include, for example, the firm's representations (or a description or summary of the same) where it challenges the direction.

3.2.3 Regulated activities

The Bill inserts the concepts of "PRA-regulated activity" and "PRA-authorised person" in s.417 of the FSMA (definitions). New s.22A of the FSMA provides that the Treasury may make an order to specify which activities are "PRA-regulated activities" for the purposes of the FSMA ("the Order"). The Order may also confer powers on the PRA to, *inter alia*, designate other activities as PRA-regulated activities, and it is expected that the Order will confer such powers.

It is understood that deposit-taking and insurance activities will be PRA-regulated activities. In addition, the Bank of England has stated that it is currently envisaged that investment firms authorised to deal in investments as principal on their own account would be eligible for PRA designation. However, as most such firms are unlikely to pose a significant risk to the stability of the financial system, the PRA is expected to develop additional criteria for designation. Such criteria are likely to include the size of a firm, the substitutability of its services, the complexity of its activities, and its interconnectedness with the financial system and any PRA-supervised companies within its group. The PRA will consult on its proposed policy in due course.

Reflecting the changes in regulatory architecture, the amended s.20 of the FSMA specifies that an authorised person (other than a PRA-authorised person) who carries out regulated activities outside its permission is in breach of the requirements imposed by the FCA, and a PRA-authorised person who carries out regulated activities outside its permission is in breach of the requirements imposed by the FCA and the PRA. It is expected that the Order will confer powers on each of the FCA and the PRA to make their own rules, and that, consequently, there will be two separate regulatory rulebooks. PRA is required to consult the FCA in making its rules, in order to avoid regulatory inconsistency and to minimise regulatory overlap for dual-regulated firms.

3.2.4 Authorisation

It is proposed that the new authorisation process, set out in the draft Bill, will substitute the existing Pt IV authorisation regime with the new Pt 4A.[39] The new authorisation process would require an applicant to first determine which regulator would be the "appropriate regulator". Although certain authorised firms will be dual regulated (such that the PRA will be the prudential regulator and the FCA will be the conduct of business regulator), it will not be necessary to apply to both regulators separately for authorisation.

3.2.4.1 Appropriate regulator

Pursuant to the new authorisation process, a person applying for a permission to carry out regulated activities under the FSMA ("Pt 4A permission") will apply to the PRA if it is applying for a permission to carry out regulated activities which consist of or include a PRA-regulated activity, or if the applicant is a PRA-authorised person otherwise than by virtue of having been granted a Pt 4A permission. The appropriate regulator for all other firms will be the FCA. The appropriate regulator will then manage the application process and ultimately grant or refuse permission.

3.2.4.2 Inter-regulator consultation

In the case of dual-regulated firms, the PRA will be required to receive consent from the FCA regarding an applicant prior to granting the Pt 4A permission. It is expected that the FCA will, in such instances, be fully involved in the authorisation process. This may well mean that, at least in more complex cases, the FCA will request the applicants to provide information additional to that requested by the PRA. The FCA may also conduct an additional fitness and propriety assessment taking into account its own statutory objectives.

As all PRA-authorised persons will also be regulated by the FCA, the PRA requires the FCA's consent in order to grant a Pt 4A permission in all cases. The FCA may make its consent conditional (e.g. it may request that the PRA impose certain limitations on the applicant's permission in order to address the concerns the FCA may have). The PRA does not have the authority to grant a Pt 4A permission to a person who, as a result of the Pt 4A permission granted by the PRA, would be an authorised person other than a PRA-authorised person.

Where an applicant applying to the FCA for authorisation is a member of a group which includes a PRA-authorised person, the FCA must consult the PRA before granting authorisation. The obligation on the FCA in these instances is, however, merely an obligation to consult the PRA and not to gain consent from the PRA before granting the Pt 4A permission. This reflects the aim of establishing a regulatory structure whereby each firm will have a primary regulator which, for PRA-authorised firms would be the PRA, with a separate layer of conduct of business regulation by the FCA.

3.2.4.3 Threshold conditions

The regulators must be satisfied that the applicant meets the threshold conditions set out in Sch 6 of the FSMA before granting Pt 4A permission under the amended FSMA, including the requirements as to close links, adequate resources and suitability. The Bill also introduces new a threshold condition; the applicant must satisfy the regulator that its business model (i.e. its strategy for doing business) is suitable having regard to the regulated activities that the applicant carries on or seeks to carry on.[40]

The arrangements regarding appointed representatives, notably the arrangements exempting appointed representatives from the need to receive authorisation, will be carried over into the new regime, and it is expected that the FCA will be the relevant authority for most approved representative applications. Please see the discussion regarding the approved persons regime below. In addition, the FCA will regulate and authorise the provision of financial services by members of the professions.

3.2.5 Variation and removal of permissions

As is the case under the existing regime, the regulators may vary the Pt 4A permission of a firm at the request of the authorised person, or at the initiative of the regulator. The powers of the regulators must be exercised in a manner which reflects the regulator's statutory objectives (in the case of the PRA, all of the objectives of the PRA, and in the case of the FCA, the operational objectives of the FCA).

If an authorised person (other than a PRA-authorised person) applies to the FCA to cancel its permission, or to vary its permission by adding or removing a regulated activity (other than a PRA-regulated activity) or to vary the description of a regulated activity, the FCA may grant such application without reference to the PRA, provided that, if the relevant activity is a PRA-regulated activity, the variation does not widen the description of that PRA-regulated activity. Where an applicant who is a member of a group which includes a PRA-authorised firm applies to the FCA to vary its Pt 4A permission, the FCA must, however, consult the PRA before determining the application.[41]

On the application of a PRA-authorised person, the PRA may cancel or vary its permission. The variation of permission may include the addition, removal, or the variation of the description of a PRA-regulated activity. The PRA may vary the permission of an authorised person such that the varied permission includes one or more regulated activities which include a PRA-regulated activity. The PRA may refuse an application for variation of permission if it deems it to be desirable in order to advance any of its objectives.[42]

Where an applicant who is not a PRA-authorised firm applies to the PRA to include one or more PRA-regulated activities to its Pt 4A permission, the PRA may vary the applicant's permission accordingly, but it is required to gain the FCA's consent prior to determining the application. The FCA may withhold its consent to a proposed variation if it deems it to be desirable to do so in order to advance any of its operational objectives.[43]

The regulators are required to ensure that, after it has been authorised, an authorised person continues to satisfy the threshold conditions in relation to all regulated activities for which the person has a Pt 4A permission. To support this duty, the regulators have the power to self-initiate a variation or a cancellation of an authorised person's Pt 4A permission.[44]

The PRA must exercise this power in light of all its objectives, and the FCA must exercise this power in light of its operational objectives. In addition, the regulators may determine *inter se* (but subject to any order issued by the Treasury) which regulator takes the responsibility for ensuring the compliance by the relevant PRA-authorised firm with one or all threshold conditions in circumstances where the variation or cancellation of the permission of the PRA-authorised firm would require the consent of the other regulator.

Actions pursuant to the duty to ensure authorised persons' compliance with the threshold conditions are taken in light of the objectives of the PRA and the operational objectives of the FCA. For example, if the PRA decides to cancel the Pt 4A permission of a bank, if it deems appropriate, it may delay the cancellation of the permission for such a (short) period as would allow the deposit-taker to fail in an orderly manner.

3.2.6 Approved persons

The amendments to s.59 of the FSMA specify that the PRA and the FCA may each make rules designating controlled functions with respect to persons for whom either is the appropriate regulator. As is the case under the existing regime, a person proposing to perform the controlled function must be approved by the appropriate regulator prior to performing the relevant controlled function.

With respect to dual-regulated firms, both the PRA and the FCA will be the appropriate regulator, but the PRA will only be the appropriate regulator in respect of controlled functions which are significant-influence functions. The FCA will be the appropriate regulator for the customer-dealing function for all firms, including PRA-authorised firms.

The proposed new sub-section 3A of s.61 of the FSMA requires the regulators to determine an application for approved person status made by a person applying for Pt 4A permission at the same time within the same time period as the application for the Pt 4A permission.

3.2.6.1 Significant-influence function

Significant-influence function is defined in the new sub-section 7B of s.59 of the FSMA in relation to the carrying on of a regulated activity by an authorised person as "a function that is likely to enable the person responsible for its performance to exercise a significant influence on the conduct of the authorised person's affairs, so far as relating to the activity".

The new s.59A of the FSMA requires the regulators to consult each other before specifying controlled functions in order to avoid overlap or duplication of the regulatory requirements on approved persons. In addition, the FCA is required to exercise its power to specify controlled functions in a manner that minimises cases where a person would have to seek approval for effectively the same controlled function from both the PRA and the FCA. In practice, the FCA would likely not specify as a significant-influence function a function which has already been specified by the PRA, or would carve out PRA-authorised firms from the scope of the significant-influence functions it specifies.

Although the PRA will have primary responsibility for designating significant-influence functions for PRA-authorised firms, where the PRA has not designated a significant-influence function and the FCA wants to designate one, the FCA will be able to do so. The PRA will specify and approve the significant-influence functions it has designated with respect to PRA-authorised firms, and make and enforce its code of conduct for approved persons in PRA-authorised firms. The FCA will specify and approve the significant-influence functions it has designated (with due consideration to avoiding regulatory overlap or duplication) with respect to all authorised firms (including PRA-authorised firms), and make and enforce its code of conduct for approved persons in respect of all authorised firms. The FCA will also specify and approve the customer-dealing functions it has designated with respect to all authorised firms, and enforce its code of conduct for approved persons in respect of all persons who are approved to perform a customer-dealing function.

3.2.6.2 Withdrawal of approval

Under the amended s.63 of the FSMA, both the PRA and the FCA will be able to remove an individual's approval to perform a significant-influence for a PRA-authorised firm. This means that the approval of an approved person in a dual-regulated firm may be removed under the fitness and propriety criteria of either the PRA or the FCA. Either the PRA or the FCA may withdraw the approval it has given or the approval given by the other regulator in respect of a significant-influence function of a person engaged by a dual-regulated firm. However, only the FCA will be able to withdraw an individual's approval for performing a customer-dealing function, whether the individual in question is engaged by a dual-regulated firm or by a firm regulated only by the FCA.

3.2.6.3 Conduct of approved persons

Both the PRA and the FCA will be able to issue statements of principle regarding the conduct of, and standards applicable to, approved persons performing a significant-influence function. However, only the FCA will be able to issue statements of principle regarding the conduct of, and standards applicable to, persons performing other controlled functions.[45] If either regulator issues a statement of principle, it is also required to issue a code of practice for the purpose of "helping to determine whether or not a person's conduct complies with the statement of principle".[46]

Before either regulator issues a statement of principle or a code of conduct it is required to consult the other regulator, albeit, in the case of the FCA, the consultation obligation only applies in so far as the provisions in the statement or principle or code of conduct apply to an approved person performing a significant-influence function in relation to the carrying on of regulated activities by a PRA-authorised firm.[47]

3.2.7 Passporting

Firms passporting out from the United Kingdom within the European Economic Area will continue to be able to do so through the notification procedure substantially in its existing form, save as discussed below. Notices in relation to the exercise of outgoing passporting rights must be given to the appropriate UK regulator, which, for PRA-authorised firms, is the PRA and, for all other authorised firms, is the FCA.

Although the Bill does not expressly state who the appropriate regulator is in each case for incoming passporting purposes, stating merely that the exercise of passport rights must be given to "the appropriate UK regulator" and that the appropriate UK regulator means "whichever of the FCA and the PRA is the competent authority, the White Paper notes that this will be specified in the future by notice to the European Commission. The designation of the appropriate regulator for incoming passporting purposes will reflect the domestic scope and responsibilities of the PRA and the FCA respectively. It is expected that notifications from overseas regulators in relation to the Banking Consolidation Directive, the Reinsurance Directive, the Consolidated Life Assurance Directives or the First, Second or Third Non-Life Insurance Directives will be required to be addressed to the PRA. Notifications in relation to all other directives will be required to be addressed to the FCA.

Where the PRA receives a consent notice from an EEA regulator, it must, without delay, give a copy of the same to the FCA. When the FCA receives a consent notice from an EEA regulator it must, in relevant circumstances, provide a copy of the same to the PRA without delay. The relevant circumstances are where the consent notice relates to an insurance intermediary who wishes to carry out a PRA-regulated activity, is a PRA-authorised person, or is a person whose immediate group includes a PRA-authorised person. The FCA must receive the PRA's consent before such insurance intermediary may be allowed to passport into the United Kingdom.

3.2.8 Information sharing with HMRC

The White Paper states that the government intends to extend the information-sharing arrangements with HMRC. Under the existing arrangements, HRMC may only share information with the FSA with respect to a few specific types of regulatory investigations.

As the information held by HMRC in respect of authorised persons may be relevant and useful for regulatory purposes in a number of ways, including for authorisation and approval purposes and information relating to a firm's or an individual's integrity, the purpose of the proposed extended information-sharing arrangements is to facilitate more effective regulation of the financial services industry by the regulators having access to the information HMRC holds of persons active in financial services.

The proposal is to enable an information-sharing system through which HMRC may pass information to the PRA and the FCA for the purposes of all of the regulators' public functions. The new information-sharing arrangements shall be subject to the requirements of the Data Protection Act, including that any disclosure should be relevant, necessary and proportionate to the purpose. Criminal sanctions will continue to apply to any wrongful disclosure.

The proposed extended information-sharing arrangements will only be applicable to information held by HMRC and passed on to the PRA and the FCA. The scope of information held by the regulators which can be shared with the HMRC will not be extended from the existing information-sharing arrangements.

3.2.9 Warning notices

The Bill provides for the reduction from 28 days to 14 days of the minimum period in which persons issued with a warning notice may make representations to the relevant regulator. Although the Bill retains the safety mechanisms included within FSMA in that it requires that the warning notice must provide a "reasonable period" for a response and may extend the period within their own discretion, recipients of warning notices in particularly complex cases will be concerned that they and their advisers will not have adequate time to thoroughly review and respond to any allegations contained within the notice.[48] This concern may be exacerbated by the power granted to the FCA and PRA by the Bill to publish warning notices, albeit after consultation with the person to whom it is directed.[49]

3.2.10 Past conduct

The Bill places onto a statutory footing the FSA's current practice of requiring firms whom it has found to be in breach of conduct of business requirements to undertake past reviews of its business and to act on their own initiative with regard to the position of customers who may have suffered detriment from, or been potentially disadvantaged by such factors, but who have not complained. Accordingly, s.55N provides that the FCA or PRA may require an authorised person to review or to take remedial action in respect of past conduct.

3.2.11 Tribunal referrals

The Bill retains the right of a person to refer any regulatory decision to the financial services Tribunal. However, other than in the case of a disciplinary reference, the Tribunal will no longer be empowered to substitute the regulator's decision with its own opinion but must instead refer the matter to the regulator with a direction to reconsider.[50]

3.2.12 Regulatory Decisions Committee (RDC)

As with the current Act, the Bill does not expressly refer to the RDC but instead provides that each of the FCA and PRA must determine the procedure that it proposes to follow in relation to the giving of supervisory notices and warning and decision notices. However, while the current Act insists that the decision is made by a person who was not involved in establishing the evidence on which the evidence was based, the Bill provides that the decision may be made by two or more persons only one of whom was not directly involved in establishing the evidence.[51] It is unlikely that this will appease the concerns of those who already believe that the FSA acts as prosecutor, judge and jury. The Bill leaves open the possibility of the FCA and PRA sharing a decision-making procedure and body, or each establishing their own mechanisms.

4. The PPI judgment—a reinforcement of principles-based regulation

Notwithstanding the proposal to restructure the United Kingdom's regulatory framework, the courts and the current regulator have continued throughout 2011 to make decisions that will have an ongoing impact on the way in which regulated firms run their business. In the following sections of the *Bulletin*, we review some of those key decisions, starting with that of the High Court in respect of the BBA's judicial review of the FSA in respect of PPI.

The decision of the Administrative Court in British Bankers' Association, *R (on the application of) v Financial Services Authority and Another* [2011] EWHC 999 (Admin) (April 20, 2011) is of obvious significance to firms which have sold Payment Protection Insurance ("PPI") policies and to customers who bought them. The key practical effect of the decision is that the measures regarding past sales of PPI set out in the FSA's August 2010 Policy Statement on the assessment and redress of PPI complaints ("PS 10/12"),[52] and the approach of the Financial Ombudsman Service ("FOS"), as set out in its online PPI technical guidance (the "Online Resource"), available on its website since November 2008, will stand. The ruling opens the way for an estimated 3 million customers to receive between £3 and £8 billion in compensation for being mis-sold PPI.[53] However, the decision is also interesting in the broader context of principles-based regulation ("PBR"). The court's conclusion that there is no reason in principle why the specific obligations in the detailed rules set out in the FSA Handbook (the "Handbook") should not be subject to the wider role of the high-level Principles for Businesses (the "Principles") and that the specific obligations in the Handbook are not to be seen as exhausting the requirement to comply with the Principles constitutes judicial confirmation of the legitimacy of a regulatory approach the effectiveness of which has been questioned in the aftermath of the global financial crisis. The outcome therefore provides the FSA with an ideal opportunity to restate the benefits of PBR (and its successor, "outcomes-focused regulation" ("OFR")) and is likely to reinforce the regulators' reliance on principles when taking enforcement action under the new regulatory regime.

4.1 Background: Principles-based regulation

The Principles have formed part of the Handbook since 2001. However, it was in late 2006 that the FSA began to market itself forcefully as a "principles-based regulator". The FSA described PBR as being, in essence, "about regulating with the emphasis on principles and high-level rules, not prescription of processes; it relies on setting out the outcomes we want to see achieved in the financial services market and then directing our supervision to assessing how they are being achieved"[54] and described the move towards PBR as: "focusing on the outcomes that really matter rather than on procedural box-ticking".[55] By implementing PBR, the FSA regarded itself as committing to: "where possible, moving away from dictating through detailed, prescriptive rules and supervisory actions how firms should operate their business" and said that it would "increasingly shift the balance of our activity towards setting out desirable regulatory outcomes in principles and outcomes-focused rules, enabling our people to engage with firms' senior management in pursuit of these outcomes".[56] The FSA offered four main reasons for adopting PBR:

- effectiveness—detailed rules, it argued, had proved incapable of preventing misconduct in a range of areas, including the mis-selling of retail financial products;
- durability—regulation which focused on outcomes was more able to adapt to a rapidly changing market environment than an approach based on prescriptive rules;
- accessibility—principles were far more accessible to firms, and in particular to senior management and smaller firms lacking deep compliance and/or legal resource, than a mass of detailed requirements; and
- fostering substantive compliance—a large volume of detailed provisions could divert attention towards adhering to the letter rather than the spirit of the rules, encouraging a legalistic and tactical attitude to compliance.[57]

The FSA was, however, clear that, whilst the Principles set out the highest level outcomes the FSA was seeking to achieve, they nevertheless needed to be underpinned with detailed rules, which would therefore remain a part of the regulatory toolkit. Detailed rules were required to some extent to implement detailed EU regulatory requirements in the United Kingdom, over which the FSA had no discretion. However, the FSA also recognised that there would be factual scenarios in which detailed rules would be the most appropriate way to secure the desired regulatory outcome. Examples included situations where the effect of firms' behaviour was not readily observable or only observable over a very long period. The FSA also accepted that a prescriptive approach might sometimes be appropriate to ensure consistency across an industry, such as for the purposes of consumer protection, where it may be appropriate for the FSA to "continue to define the format and content firms must use to provide certain kinds of information to consumers, allowing easy comparability between different products".[58] It was clear, however, that, despite maintaining some detailed rules, the FSA intended the move towards PBR to change the way in which firms experienced FSA regulation and was clear that PBR would have significant implications for the interaction between firms and the regulator. As the FSA put it, it was "looking for firms to take greater responsibility for how they meet their regulatory obligations" and it would, going forward, "give greater recognition to firms' own management and controls".[59] The FSA also made it clear that PBR would change the FSA's approach to enforcement: "Our Principles have the status of rules and we will, as we have always done, take enforcement action on the basis of a breach of them. Increasingly such action has been taken on the basis of the Principles alone, and this will continue".[60]

By 2008, the FSA was considered a global leader on PBR.[61] However, PBR suffered a significant reputational setback in the wake of the financial crisis. The FSA's approach to regulation, characterised by a commitment to PBR, was deemed "light touch" and blamed for the serious weaknesses the crisis revealed in the risk-management systems of many large UK financial institutions. It became common ground that the core assumptions on which PBR was based, that markets were self-correcting and that firms were best placed to manage their own risk, were fundamentally flawed. The crisis opened up a global debate about the correct approach to regulation, and what changes should be made to existing regulatory systems in order to prevent a further crisis in the future. For many, the obvious response seemed to be a heavy dose of prescriptive regulation, removing regulatory discretion from senior management (as Hector Sants, FSA chief executive, put it in early 2009: "[A] Principles-based approach does not work with individuals who have no principles").[62] The benefits of a system based on high-level principles underpinned by detailed rules were called into question.

4.2 The BBA's judicial review

The ongoing debate about the correct approach to regulation post-crisis returned to the spotlight in early 2011 when the benefits of PBR, the inter-relation between the Principles and the detailed rules underpinning them and the problems with an entirely prescriptive approach to regulation became the subject of judicial scrutiny in *British Bankers' Association, R (on the application of) v Financial Services Authority and Another* [2011] EWHC 999 (Admin) (April 20, 2011). The action concerned part of the regulatory response to the mis-selling of PPI policies, which provide insurance against the risk that a borrower will be unable to maintain loan repayments. PPI is a profitable and widely purchased product, sold extensively in the United Kingdom by banks and other financial services firms, whose sale has generated tens of thousands of customer complaints.

The case was brought by the British Bankers' Association ("BBA"), representing the banks, against the FSA and the FOS in connection with PS 10/12.[63] PS 10/12, which the FSA published in August 2010, comprises a package of measures arising from the FSA's concerns about widespread weaknesses in previous PPI selling practices to the detriment of many consumers. The package includes amendments to the rules in the Dispute Resolution: Complaints ("DISP") part of the Handbook, guidance about how PPI sales complaints should be handled and the basis on which they should be decided, and an open letter identifying what the FSA regards as common failings in the selling of PPI policies. The measures also include guidance on root cause analysis, the mechanism by which customers who have not complained may also receive redress for losses suffered.

The aim of PS 10/12 was to ensure that firms handled complaints about PPI mis-selling fairly. In order to achieve the fair handling of complaints, the FSA considered it essential that the regulator and the industry have a common understanding of what was and was not a compliant sale. The open letter was intended to ensure this, as it sought to provide examples of behaviour which the FSA considered to be generally indicative of a breach of its rules absent any other consideration.

The BBA challenged the lawfulness of PS 10/12 on three grounds, all of which were rejected by the court. However, it is the second of the BBA's grounds, the FSA's responses and the courts conclusions, which gave rise to a discussion of PBR.[64]

The BBA's concern was that, in some cases, the Principles were being used by the FSA to contradict specific Handbook rules, namely those set out in the Insurance Conduct of Business part of the Handbook ("ICOB")[65] and that, as a result, firms would be required by PS 10/12 to compensate customers for mis-selling of PPI policies even though the sales complied with the letter of the detailed rules in force at the time. The BBA alleged that, even if the FSA and the FOS are entitled to rely on the Principles as creating obligations owed by firms to their customers, the breach of which would lead to a requirement for the firm to pay the customers compensation (which the court agreed that they were), it was nevertheless unlawful for the FSA and the FOS to interpret or apply the Principles in such a way as to "contradict or augment" specific rules governing the sale of and handling of complaints about PPI. The BBA argued that it was also unlawful for the open letter common failings, as reflected in the amendments to DISP, to be interpreted or applied so as to "contradict or augment" specific rules in the Handbook. In the BBA's view, this was the effect of the new guidance in PS 10/12, the open letter common failings and the required standards of behaviour implied from them, and of the FOS' Online Resource.[66]

The BBA contended that the Principles could be used as aids to the interpretation of specific but ambiguous rules, and accepted that where a regulated activity was not covered by a specific rule or detailed rules, the Principles could be used to impose obligations on firms. However, where a regulated activity was governed by specific, detailed rules, the only obligation of the firm was to comply with those rules. In the context of PPI sales, this meant that, if a firm had complied with the detailed rules in ICOB, then it could not be held to have breached any provision leading to redress (i.e. it could not be held to have breached the Principles). To hold otherwise would be to use the Principles to conflict with the rules or augment them.[67] The BBA argued that this meant that the FOS in its turn should not use the Principles to augment or contradict the obligations owed by firms to customers when deciding on complaints, and should not advise either side, as they did in the Online Resource, that this was how complaints should be handled. The FOS' duty to reach decisions on the basis of what was fair and reasonable should not permit it to misinterpret the role of the Principles in that way. Fairness and reasonableness also required the FOS to apply the specific rules and not to augment and contradict them by relying on the high-level Principles. [68]

In response, the FSA referred to the key features of its regulatory approach: PBR. The FSA argued that it had always taken the view that firms' regulatory obligations (in this case, firms' obligations towards their PPI customers) extended beyond those set out in the detailed Handbook rules (in this case, ICOB) to compliance with the Principles. The FSA pointed out that there were certain factual situations in the course of PPI sales where the rules did not cover the point and that in those circumstances recourse had to be had to the Principles, which served to prevent "regulatory gaps" opening up.[69] It was not the FSA's case that it would seek to enforce the Principles where to do so would conflict with specific rules on the same subject. However, the FSA took issue with the BBA's argument that the Principles could not be used to augment the specific provisions of the Handbook, short of a conflict with them. This was to the FSA "the opening up of a regulatory gap which lay at the heart of its concerns about the BBA's arguments".[70] The FSA was also concerned that these regulatory gaps would increase if Principles were excluded from having any role on the basis that specific rules had been created to cover some aspects of the sales process. The FSA contended that this would mean that specific rules would be required to govern every aspect of a sale, when not every method, least of all one devised with the avoidance of the rule in mind, could be anticipated and provided for.[71] The FSA's arguments before the Administrative Court constituted a restatement of some of its original, pre-crisis arguments in favour of PBR (effectiveness, durability and fostering a substantive compliance) and, in emphasising the importance of maintaining a set of detailed rules in order to buttress the high-level Principles (the FSA argued that it would be "unwise" for a regulator to rely simply on high-level Principles alone), the FSA restated its belief in PBR.

The court accepted the FSA's arguments and, in explaining the basis for its decision, made several interesting observations about the Principles and the inter-relation between the Principles and Handbook rules.[72] Ouseley J described the Principles as "the overarching framework for regulation"[73] and said that they could be "best understood as the ever present substrata to which the specific rules are added"[74] and that they "stand over the specific rules".[75] He made it clear that in the court's view the Principles "always have to be complied with" and "[T]he specific rules cannot be used to supplant them and cannot be used to contradict them. They are but specific applications of them to the particular requirements they cover. The general notion that the specific rules can exhaust the application of the Principles is inappropriate. It cannot be an error of law for the Principles to augment specific rules".[76]

Crucially, Ouseley J said that this was "for good reason", observing that the FSA had clearly not published (and had chosen not to publish), "a detailed all-embracing comprehensive code of regulations to be interpreted as covering all possible circumstances" and pointing out that "the industry had not wanted such a code" either.[77] He agreed with and emphasised the FSA's concern, originally voiced in 2007, that an all-embracing code of regulations "could be circumvented unfairly, or contain certain provisions which were not apt for the many varied sales circumstances which could arise".[78] The Principles would, however, as the overarching framework, "always be in place to be the fundamental provision which would always govern the action of firms, as well as to cover all those circumstances not provided for or adequately provided for by specific rules".[79] In other words, and importantly, the court accepted the FSA's concerns about the opening up of regulatory gaps which might occur if detailed rules did not operate against the backdrop of high-level Principles which imposed wide regulatory obligations on firms.

4.3 Conclusion

The decision of the Administrative Court in British Bankers' Association, *R (on the application of) v Financial Services Authority and Another* [2011] EWHC 999 (Admin) (April 20, 2011) serves as a timely vindication of a regulatory system made up of high-level Principles underpinned by detailed, prescriptive rules. This will no doubt please the FSA, whose post-crisis regulatory approach, OFR, constitutes exactly this, albeit accompanied by a more intensive, intrusive and sceptical supervisory process, a renewed commitment to achieving "credible deterrence" and a shift from "regulation based on facts to regulation based on judgments about the future".[80] It remains to be seen whether the court's decision will see the combination of detailed rules and overarching principles being carried forward into the new regulatory regime, however this seems likely.

5. Contentious regulatory law 2011: key FSA enforcement actions

2011 has seen the FSA continuing to pursue its credible deterrence objective, using its full range of enforcement powers to take robust action against individuals and firms.

5.1 Market abuse and insider dealing

The FSA has continued its commitment to using criminal powers to target insider trading. In February, the FSA concluded its sixth criminal successful insider dealing prosecution. Christian Littlewood, Angie Littlewood and Henry Olmar Sa'id pleaded guilty to eight counts of insider trading in a number of different LSE and AIM listed shares, contrary to s.52 of the Criminal Justice Act 1993.[81] All three received substantial custodial sentences, with Christian Littlewood receiving a record sentence of three years and four months. The case is the latest in a line of prosecutions involving professionals working in financial institutions. This suggests that the FSA is starting to address criticisms regarding perceived past failures to tackle institutional insider dealing. It was also the first case in which the FSA sought an extradition (Mr Sa'id, a Singaporean national, was extradited from the French territory of Mayotte in the Comoros Islands pursuant to a European Arrest Warrant issued at the FSA's request), which underlines the FSA's determination to use its full suite of powers to secure convictions for insider trading.

During the course of 2011, the FSA also imposed financial penalties on a number of individuals for market abuse. Senior equity research analyst Christopher Gower[82] was fined £50,000 for making misleading and inaccurate disclosures to the market via a Bloomberg instant message. The case shows that the FSA includes research analysts among those who can, in principle, influence the market and is an important reminder that Bloomberg and other instant chat messages can be distributed far more widely than their intended audience and that staff should take care to remember this. Samuel

Kahn[83] was fined £1,094,900 after being found to have coordinated a scheme to deliberately inflate the share price of a PLUS quoted company. Kahn successfully perpetrated repeated impersonations and succeeded in placing trading orders on their behalf, which emphasises the importance of robust customer identity procedures so that firms know and are able to verify exactly who they are dealing with and have procedures in place to verify customer identity before taking telephone orders. Kahn also saw the FSA exercise its powers under the FSMA to obtain for the first time a final injunction restraining Kahn from committing further market abuse. The FSA took a similar approach against Barnett Michael Alexander,[84] an experienced trader and former private client stockbroker found to have manipulated the price of shares on the LSE. In addition to obtaining an interim injunction against him (which the High Court later made permanent) the FSA imposed a £700,000 financial penalty and separate restitution and prohibition orders. Alexander was, at the time of his abuse, operating on a self-employed basis dealing in shares and retail derivatives products from his home address, placing his orders using a Direct Market Access ("DMA") provider. The FSA published concerns in relation to order book conduct and the intentional pattern of behaviour known as "spoofing" or "layering"[85] in 2009 and has recently decided to impose an £8 million financial penalty on Swift Trade Inc for similar behaviour.[86] Alexander highlights the need for DMAs to ensure adequate monitoring is in place to identify abusive trading strategies and to ensure that they meet suspicious transaction reporting requirements.

Several market abuse cases were considered by the Upper Tribunal (Tax and Chancery Chamber) ("the Tribunal"). The Tribunal directed the FSA to impose a prohibition order and financial penalty of £150,000 on David Massey,[87] having found that he had committed the market abuse offence of insider dealing by short selling shares in an AIM listed company on the basis of inside information concerning the availability of discounted shares. Massey's reference to the Tribunal was dismissed, save that the financial penalty was reduced to reflect the amount of profit made through the trading, plus 50 per cent. As a result of the Tribunal's decision in Massey, information that is consistent with or similar to information concerning an issuer or a security which is already generally available may nevertheless be inside information if it is not in fact information which is generally known to the market. For non-public information to constitute inside information, it is probably necessary to know that it would, if made generally available, be likely to have a significant effect on price in "a particular direction", that is, it may not be inside information if its effect on price is likely to be significant, but it is genuinely not clear whether the effect would be positive or negative. Regarding the statutory defence to market abuse, it is probably not sufficient for the firm or individual concerned simply to believe genuinely that a particular course of conduct does not constitute market abuse—objectively reasonable grounds for that belief are required.

The Tribunal also published its decision regarding whether it was appropriate for the FSA to impose a financial penalty on Graham Betton[88] for his involvement in a share-ramping scheme. The FSA had originally determined the appropriate financial penalty to be £500,000 but had reduced this to £100,000 to take into account the economic impact of the prohibition order also imposed on Betton. The Tribunal took the view that, due to Betton's financial position, this should be further reduced to £25,000. The Tribunal found that the fact that Mr Betton made nothing out of the share-ramping exercise and was not well off in no way excused his actions and the seriousness of the behaviour demanded a penalty, but that an amount of penalty that "forces him into bankruptcy" would be "disproportionate and unproductive".

The Tribunal also reduced the penalty imposed by the FSA on Oluwole Fagbulu[89] on the grounds of financial hardship.[90] However, it unanimously decided to raise the £1.7 million fine imposed on Michiel Visser[91] and held that they would also have raised Fagbulu's penalty had it not been for his financial circumstances. Visser and Fagbulu were the chief executive and chief finance officer of a UK FSA-authorised company that managed a hedge fund domiciled in the Cayman Islands. Fagbulu was also responsible for compliance oversight. They were found to have manipulated the market in order to bolster the fund's net asset value ("NAV"), falsely inflated the fund's NAV, and breached the fund's mandate. The case is one of the first in which the FSA has taken action against a hedge fund manager, and sends a clear message that FSA-approved persons operating hedge funds will face serious consequences if they disguise the performance of their fund. FSA-authorised hedge fund managers should review their systems and controls in order to ensure that they are not at risk of individuals fundamentally misleading them, and investors, about the value of the fund.

The Tribunal disagreed with the FSA's proposed action against Jason Geddis,[92] a trader with responsibility for London Metal Exchange ("LME") trading on behalf of his firm and its clients. The FSA had sought to impose a prohibition and financial penalty on Geddis for committing market abuse by securing the price of lead contracts on the LME at an abnormal and artificial level. However, the Tribunal determined that, while Geddis' conduct in creating a disorderly market fell below the proper standard of care, it was not the result of a premeditated plan to act improperly. The Tribunal therefore concluded that a public censure was appropriate. The Tribunal also rejected the FSA's finding that Geddis was not fit and proper and so should be prohibited. On the contrary, the Tribunal found him to be a person of integrity. The case underlines the importance of the independent scrutiny of FSA disciplinary decisions that the Tribunal affords.

5.2 Other financial crime and financial crime risk

The FSA secured its first criminal convictions for boiler room fraud over the summer against David Roger Mason[93] and, in a separate action, against three members of the Wilmot[94] family. Firms should remember that boiler rooms pose a threat to companies as well as individuals. To minimise the risk of exposure to this type of fraud, compliance officers and senior management should ensure that policies and procedures are reviewed and that the purchase of shares is monitored. Some practical considerations include being aware of the identity of individuals who have purchased large amounts of shares and what they plan to do with them; being aware of inflated commissions and brokerage companies wanting to buy large amounts of shares with the promise of raising capital or the share price; identifying whether the purchaser is authorised by the FSA; and being aware that, if the company is not listed, the fact that its shares may not be suitable for a small individual investor. Legal advice at the earliest opportunity, or even as part of a business risk review, assessment or investigation, can also help to minimise exposure and/or help the company to respond more effectively if approached by a regulator.

The FSA continued to focus on unauthorised land banking schemes, winding up one and obtaining the continuation of a world-wide injunction against another.[95] In a separate action, the FSA secured a summary judgment against a further land banking operation.[96] The increased action against unauthorised land banking schemes is one example of the FSA taking robust action to protect consumers.

The FSA fined Willis Ltd, the global insurance broker, £6.895 million in relation to its anti-bribery systems and controls, having found that Willis did not conduct adequate due diligence to assess the risk of dealing with overseas third parties to which it made payments to help it secure and retain business, and did not record an "adequate commercial rationale" for the payments.[97] The FSA concluded that Willis's approach caused an unacceptable risk that overseas payments could be used for corrupt purposes. Importantly, although Willis did have anti-bribery procedures in place, the firm was criticised for failing properly to implement them. The Willis fine is the largest fine the FSA has ever imposed in relation to financial crime risk, surpassing the £5.25 million levied against Aon in 2009 for similar failings,[98] and is a reminder to firms that they must ensure they can evidence, on a robust, consistent and coherent basis, full compliance with their anti-bribery and corruption policies and procedures, which must themselves be adequate. Another key warning in the Willis fine is the fact that the net commission earned by Willis in relation to overseas third parties in high-risk jurisdictions represented only approximately 1 per cent of its total net revenue during the period in question. This shows that firms cannot afford to ignore any potentially high-risk areas of their business, even if they only represent a small aspect of their overall operations.

5.3 Complaints handling

The FSA imposed substantial financial penalties on Royal Bank of Scotland and NatWest[99] (£2.8 million) and Bank of Scotland[100] (£3.5 million) for failures relating to the handling of complaints about retail investment products. At the time of the action, Bank of Scotland had paid £2.4 million in compensation to customers whose complaint was upheld following its own internal review and expected to pay out a further £15 million following completion of other internal review work. RBS and NatWest were ordered to work with a skilled person to undertake an extensive review of their complaints-handling processes. Shortly after announcing its decision to fine Bank of Scotland, the FSA confirmed new complaint-handling rules as part of a package of new measures designed to push up standards in the industry, including the abolition of the "two-stage" complaints-handling rule; requiring firms to identify a senior individual responsible for complaints handling; additional guidance to help firms understand the processes they might need in place to meet FSA requirements on root cause analysis; and further guidance requiring firms to take account of ombudsman decisions and previous customer complaints. Firms will need to incorporate the new requirements and expectations into their existing policies and procedures and ensure that complaint handlers are adequately trained and have access to all relevant information. Firms should also ensure that comprehensive management information is reported to the senior manager accountable for oversight of complaints handling as well as the information needed to undertake root-cause analysis on an ongoing basis. In the Royal Bank of Scotland and Bank of Scotland cases the FSA found that the complaint-handling systems and controls focused on compliance with a prescribed process rather than considering the quality and appropriateness of the overall outcome for the customer, which is a reminder to firms that direct and visible senior manager responsibility combined with an ongoing review of the quality of the practical outcomes delivered is the expected benchmark.

5.4 Suitability of advice

The FSA continued to take robust action against a large number of firms and individuals for suitability of advice failings throughout 2011. Barclays Bank Plc[101] was fined £7.7 million for failings in relation to the sale of two investment funds. Later in the year, Norwich & Peterborough was fined £1.4 million for failing to give its customers suitable advice in relation to Keydata products.[102] Both firms also agreed very substantial sums in additional compensation for customers. More recently, Credit Suisse (UK) Ltd[103] was fined £5.5 million for systems and controls failings in relation to sales by its private bank of structured capital at risk products, which are complex financial products that provide income to customers but also expose them to the risk that they lose all or part of their initial capital. Credit Suisse also agreed to carry out a past business review, overseen by a skilled person, to allow the identification of and payment of redress to affected customers. Between January 2007 and December 2009, Credit Suisse UK customers invested over £1 billion in SCARPs. However, during that period the FSA determined that there were a number of serious failings in the systems and controls in respect of those sales, as a result of which customers were exposed to an unacceptable risk of being sold a SCARP that was unsuitable for them. The FSA also took action against several smaller firms and senior management for suitability of advice and related systems and controls failings across a range of market sectors, including investments, insurance and pensions.[104]

The raft of FSA enforcement action against firms for suitability of advice failings provides some basic reminders for firms. Firms must have policies and procedures in place to ensure that they have a good understanding of the products they recommend and are aware of distinctive features and risks of specialist products (and that sales staff are properly trained and have the requisite knowledge and understanding) and that they are able properly to assess the risks their customers are willing and able to take. Firms should also remember the need to take swift action to follow up all compliance findings, particularly where these show evidence of customer harm. (In Norwich & Peterborough, the FSA emphasised that the majority of customer detriment could have been avoided if the compliance findings arising from the review of Keydata sales had been acted on and similarly, in Barclays, risks identified as part of the approval process for the previous versions of the two funds which, if not mitigated during the sales process, were likely to lead to unsuitable sales were not followed up in relation to the successor funds.) The fact that the FSA is increasingly requiring firms to undertake past business reviews in addition to paying significant financial penalties is also noteworthy.

2011 also saw the FSA follow up its 2009 review into the promotion and sale of unauthorised collective investment schemes ("UCIS") (the findings of which were published in July 2010 along with a good and poor practices report for UCIS firms)[105] with several enforcement actions against firms promoting and advising retail customers on UCIS for UCIS-related failings leading to customers being exposed to the risk of receiving unsuitable advice.[106] The cases remind firms promoting and advising on UCIS of the importance of ensuring that they have adequate systems and controls in place to ensure that UCIS are promoted and sold appropriately. Firms should ensure that they are familiar with the FSA's July 2010 report and good and poor practices guide and that senior management and sales staff understand the regulatory requirements relating to UCIS (a lack of senior management understanding of relevant regulatory requirements was a recurring theme in this area) including what constitutes a financial promotion (and in particular that a promotion can be communicated through verbal as well as written communications); that the firm is complying with the statutory restrictions on the sale of UCIS by authorised persons to the general public under FSMA and the exemptions to these restrictions and that the exemptions relied on (and why) when promoting a UCIS, are adequately recorded. This is particularly important given the FSA's identification of UCIS as an emerging risk in its 2011 Retail Conduct Risk Outlook, which suggests that UCIS is likely to remain an area of FSA focus going forward.

5.5 Client money

Client money continued to be high on the FSA's agenda and the FSA took action against several firms for breaches of the client money rules set out in the Client Asset Sourcebook ("CASS"). Barclays Capital Securities Ltd[107] was fined in excess of £1.1 million for failing to segregate client money placed on GBP money market deposits intra-day in a segregated trust account. Foreign exchange broker ActivTrades was fined £85,750 for similar failings[108] and Towry Investment Management Ltd[109] was fined £494,000 for various CASS breaches and for providing misleading information to the FSA in response to the FSA's "Dear CEO" letter and Client Money and Asset Report 2010. [110]

These cases are evidence of the FSA's continuing focus on client money. Firms should have adequate systems and controls in place to ensure that client money is properly segregated from firm money in accordance with the CASS rules and to enable them to monitor and assess the adequacy of their client money arrangements. It is also worth noting that, while to date the FSA's enforcement actions in relation to client money have focused on investment firms, the FSA commented in its recently published Smaller Wholesale Insurance Intermediaries Newsletter that it has identified high-level concerns regarding client money compliance in insurance firms, which suggests that insurance firms may soon become the focus of FSA scrutiny in this area.

5.6 Disclosure of information and transaction reporting

The FSA fined JJB Sports Plc[111] £455,000 for failing to disclose information to the market about two acquisitions, which led to a false market in JJB shares for over nine months. The FSA said that in both instances the purchase cost of the companies was inside information and should have been disclosed to the market as soon as possible. The case highlights the need for issuers to have proper systems and controls in respect of disclosures to the market, particularly for identifying inside information and ensuring that it is properly released. The FSA also fined City Index Ltd[112] £490,000 for failing to report approximately 55,000 transactions to the FSA over a two-year period and for reporting a large number of transactions with data fields completed incorrectly. Firms should ensure that they review the integrity of transaction reports on a regular basis, and firms that outsource the submission of transaction reporting should remember that they retain ultimate responsibility to ensure the accuracy and completeness of the reports and to make sure they have adequate monitoring procedures in place.

Sir Ken Morrison[113] was fined £210,000 for failing to disclose his reduced shareholding and voting rights in Wm Morrison Supermarkets Plc. In setting the level of financial penalty, the FSA applied its new penalty setting policy. Given that Sir Ken did not financially benefit from the misconduct and had no relevant income, the FSA started at £0, adjusting the level upwards to account for the seriousness of the behaviour and the need for credible deterrence. The case demonstrates that the FSA is prepared to enforce against individuals as well as firms for disclosure failings.

5.7 The mortgage market

The FSA has continued to prioritise the mortgage market. A financial penalty was imposed on Swift 1st Ltd[114] for the unfair treatment of customers facing mortgage arrears, the FSA having found that Swift had breached various rules in the FSA's Mortgages: Conduct of Business Sourcebook. In addition to the financial penalty, Swift has been required to carry out a customer redress programme to provide redress to customers in arrears who were charged excessive fees and charges, the cost of which is estimated as likely to be approximately £2.25 million. The case demonstrates that the FSA will, in addition to enforcement action against the firm, act to ensure that disadvantaged customers are identified and compensated. Firms must establish and implement systems and controls to ensure that their customers are treated fairly, taking the profile of their customer base into account. Many of Swift's customers were in a vulnerable position, which exacerbated the effect of Swift's misconduct.

The FSA also continued to act on its commitment, set out in its 2010/11 Business Plan, to reduce mortgage fraud, taking regulatory action against a large number of individuals and firms.[115] The FSA clearly expects firms to ensure that they have robust systems and controls in place to minimise the risk of loss from fraudulent behaviour which poses a risk both to customers and to financial stability more generally. 2011 also saw the Tribunal give judgment in two mortgage fraud cases: Alistair Curren of B-Assured Financial Services; and Nazia Bi and Quadim Mohammed.[116] In both cases, the Tribunal directed the FSA to impose financial penalties and prohibition orders on the individuals involved and in Nazia Bi and Quadim Mohammed the Tribunal substantially raised the level of the penalties originally imposed by the FSA, following a similar approach to the Tribunal in Visser and Fagbulu.

5.8 Round-up—other decisions

Several other enforcement actions taken by the FSA in 2011 are noteworthy. The FSA imposed a prohibition order on Daniel Hassell[117] on the basis that he knew that the FSA was not satisfied that he was a fit and proper person to perform a significant-influence function but nevertheless performed a function at Vantage Capital Markets LLP, an inter-dealer broker, for four years without obtaining FSA approval. The action against Hassell follows the financial penalty imposed against Vantage in 2010 for the same issue.[118]

This action makes it clear that, while it is the firm's responsibility to ensure that the relevant individuals are approved for their controlled functions, some responsibility lies with the individual. It is interesting to note that, at the time the action against Hassell was commenced, the FSA did not have the power to impose a financial penalty on him for this misconduct. This has now changed as a result of the Financial Services Act 2010. It is unclear whether the FSA will take advantage of this new power in similar cases going forward; however, it seems likely, given the FSA's tendency to combine prohibition orders with financial penalties against individuals in other contexts.

Also of note is the FSA decision to impose a public censure on BDO,[119] the accountancy and advisory firm, for failing to act with due care and skill in relation to a sponsor service to Shore Capital in its takeover of Puma and for failing to deal with the FSA in an open and cooperative way. The FSA found that although Shore Capital was an experienced listed firm, it is the responsibility of the sponsor to take an objective view of transactions and to advise clients in line with the requirements of the Listing Rules.

Notes

1 See art.1(4) of the Regulation establishing ESMA (the "ESMA Reg").

2 See Annex II for a list of Member States' voting powers, based on qualified majority voting. The largest four Member States (Germany, France, Italy and the United Kingdom, each have 8.4 per cent of the votes).

3 See "The Importance of Wholesale Financial Services to the EU Economy 2009", at page 38 (London Economics analysis, 2008, based on Eurostat data) available at http://217.154.230.218/NR/rdonlyres/DF649F73-2F5D-4C3E-AA24-E491A280A9B5/0/BC_RS_ImportanceofWholesaleFStoEUEconomy09.pdf

4 See art.6a(5) of the ESMA Reg.

5 See art.9(6) of the ESMA Reg.

6 An emergency situation is defined (under art.10(1) of the ESMA Reg) as: "adverse developments which may seriously jeopardise the orderly functioning and integrity of financial markets, or the stability of the whole or part of the financial system in the EU". However, no definition of "adverse developments" exists, and "there are no indications of how the ESAs would use the emergency powers, or to what end".

7 Proposal for a regulation of the European Parliament and of the Council on OTC derivative transactions, central counterparties and trade repositories—Presidency Compromise, August 29, 2011 (the "Draft EMIR Regulation").

8 See art.4b of the Draft EMIR Regulation.

9 See art.4 of the Draft EMIR Regulation.

10 See art.3 of the Draft EMIR Regulation.

11 See art.5 of the Draft EMIR Regulation.

12 See art.7 of the Draft EMIR Regulation.

13 See art.6 of the Draft EMIR Regulation.

14 See Proposal for a Directive of the European Parliament and of the Council on markets in financial instruments repealing Directive 2004/39/EC, October 20, 2011 (the "MiFID II Directive") and the Proposal for a Regulation of the European Parliament and of the Council on markets in financial instruments and amending Regulation on OTC derivatives, central counterparties and trade repositories, October 20, 2011 (the "MiFID II Regulation").

15 See art.9 of MiFID II Directive.

16 See art.17 of MiFID II Directive.

17 See art.51 of MiFID II Directive.

18 See art.51 of MiFID II Directive.

19 See art.24 of MiFID II Directive.

20 See art.27 of MiFID II Directive.

21 See arts.41–44 of MiFID II Directive.

22 See Proposal for a Regulation of the European Parliament and of the Council on insider dealing and market manipulation (market abuse).

23 See art.6 of the MAD II Regulation.

24 Proposal for a Directive of the European Parliament and of the Council on criminal sanctions for insider dealing and market manipulation, October 20, 2010.

25 Bank of England Act 1998, s.9B.

26 FSMA, s.2A.

27 FSMA, s.3H.

28 FSMA, ss.1C–1E.

29 FSMA, s.1A.

30 FSMA, s.3H.

31 Bank of England Act 1998, ss.9G–9P.

32 FSMA, s.137C.

33 FSMA, s.137P.

34 FSMA, s.3B.

35 FSMA, s.3D.

36 FSMA, s.3E.

37 FSMA, s.138N, as set out in the Bill.

38 FSMA, s.137P, as set out in the Bill.

39 FSMA, ss.40–55, as set out in the Bill.

40 FSMA, para.5A of Sch 6, as set out in the Bill.

41 FSMA, s.55H, as set out in the Bill.

42 FSMA, s.55I(1) and (2), as set out in the Bill.

43 FSMA, s.55I(3), as set out in the Bill.

44 FSMA s.55J, as set out in the Bill.

45 FSMA, s.64, as set out in the Bill.

46 FSMA, s.64(2), as set out in the Bill.

47 FSMA, s.65 as set out in the Bill.

48 FSMA, s.387 and 393 as set out in the Bill.

49 FSMA, s.391 as set out in the Bill.

50 Section 133(5) as set out in the Bill.

51 FSMA, s.395 as set out in the Bill.

52 Policy Statement 10/12, "The Assessment and Redress of Payment Protection Insurance Complaints", August 10, 2010.

53 See, for example, "PPI: What the High Court Ruling Means for Your Mis-Selling Claim", The *Daily Telegraph*, April 20, 2011, and "Banks Braced for Deluge of PPI Complaints", *Financial Times*, April 20, 2011.

54 Speech by John Tiner, FSA, April 23, 2007.

55 FSA press release FSA/PN/109/2006, "FSA publishes radical proposals for move to principles based regulation", 2006.

56 FSA, "Principles Based Regulation: Focusing on the Outcomes that Matter", 2007.

57 Ibid.

58 Ibid.

59 Ibid.

60 Ibid.

61 "Principles-Based Securities Regulation in the Wake of the Global Financial Crisis", Christie Ford, *McGill Law Journal,* 2010.

62 Speech by Hector Sants, "Delivering Intensive Supervision and Credible Deterrence", delivered to the Reuters Newsmakers Event, March 12, 2009.

63 The action was supported by Nemo Personal Finance Ltd, which sold over 15,000 PPI policies directly and through brokers between 2005 and 2009.

64 The BBA's first ground of challenge was that by designating the Principles as not forming the basis for any cause of action for damages under s.150 of the FSMA, the FSA prevented the application of the Principles by the FOS and the FSA when requiring firms to handle complaints fairly (i.e. the BBA argued that the Principles were incapable of giving rise to obligations owed by firms to customers). Rather, the obligations created by the Principles applied between firm and regulator only (the BBA's submissions can be found at paras 55–70 of the judgment). The court rejected this argument, holding that "actionable" did not mean "capable of giving rise to obligations or compensation" (see paras 71–94 of the judgment). The effect of s.150(2) was limited to removing a cause of action for breach of statutory duty, and no more. A breach of the Principles could therefore still give rise to obligations to provide redress to consumers under the complaints-handling regime. The third ground of challenge concerned root-cause analysis and was advanced by Nemo Personal Finance

Limited and adopted by the BBA. It was argued that s.404 of the FSMA, in the form it was in at the time the FSA published PS 10/12, allowed the FSA to ask HM Treasury to make an order for a scheme to compensate customers for widespread failures in relation to a particular activity. The wording of s.404 meant that such a scheme would not have been capable of compensating customers for breaches of the Principles. The creation of a scheme was also prevented by a number of safeguards. Relying on case law, it was argued that, since Parliament had provided a power to remedy widespread market failures, once the ability to use the scheme power was triggered, the FSA could not circumvent the safeguards and limitations of that power by using another, more general power to achieve the same end (Nemo's submissions can be found at paras 210–227 of the judgment). The court rejected the argument on several grounds. Ultimately, looking at the purpose, nature and effect of what the FSA measures set out in PS 10/12 sought to achieve (particularly with regard to root-cause analysis) as against the s.404 scheme, the court agreed with the FSA that they were not one and the same (see paras 228–263 of the judgment).

65 ICOB was replaced by the Insurance Conduct of Business Sourcebook ("ICOBS") in January 2008. The judgment, however, refers to ICOB.

66 The BBA's second ground, that the Principles cannot conflict with or augment specific rules, is set out in the judgment from para.95 onwards.

67 See para.98 of the judgment. Note that the BBA accepted that this did not apply to Principle 1 (Integrity). If Principle 1 was breached, the FSA could enforce that since the specific rules in ICOB were not intended to supplement that Principle.

68 Para.99 of the judgment.

69 Paras 130 and 131 of the judgment.

70 Ibid.

71 Para.131 of the judgment.

72 The court's conclusions are at paras 161–188 of the judgment.

73 See para.161 of the judgment.

74 See para.162 of the judgment.

75 See para.166 of the judgment.

76 See para.162 of the judgment.

77 See para.161 of the judgment.

78 Ibid.

79 Ibid.

80 Paper accompanying the FSA's Turner Review, "A Regulatory Response to the Global Banking Crisis", Discussion Paper 09/2, 2009.

81 FSA press release, "Investment banker, his wife and family friend sentenced for insider dealing", February 2, 2011.

82 Final Notice for Christopher William Gower, January 12, 2011.

83 Final Notice for Samuel Khan, May 24, 2011.

84 Final Notice for Barnett Michael Alexander, June 14, 2011.

85 Fixing the market in certain shares.

86 Decision Notice for 7722656 Canada Inc formerly carrying on business as Swift Trade Inc, May 6, 2011. Following an amendment to s.391(4) of the FSMA in 2010, the FSA has the power to publish Decision Notices, as it did in this case.

87 Final Notice for David Massey, February 2, 2011.

88 Final Notice for Graham Betton, August 26, 2011.

89 Final Notice for Oluwole Fagbulu, September 20, 2011.

90 See also the Tribunal's more recent decision in the case of David Bedford, where Mr Bedford's financial penalty was reduced by half. Final Notice for David Bedford, October 3, 2011.

91 Final Notice for Michiel Visser, September 20, 2011.

92 Final Notice for Jason Geddis, September 2, 2011.

93 FSA Press Release, "FSA secures first criminal conviction for boiler room fraud", June 14, 2011. In a related action, the FSA fined approved person David Sinclair of Axiom Capital £68,000 and prohibited him from holding any significant-influence function in the future. Sinclair unwittingly allowed Mason to use a bank account under his control to dissipate investor money to Mason and boiler room fraudsters (Final Notice for David Sinclair, December 20, 2010).

94 FSA Press Release, "Three sentenced to jail for operating £2.75 million boiler room scam", August 22, 2011.

95 FSA Press Release, "FSA winds up one unauthorised land bank and secures a world-wide injunction against another", June 8, 2011.

96 FSA Press Release, "FSA continues its crackdown on land banking with another high court decision protecting consumers", June 29, 2011.

97 Final Notice for Willis Ltd, July 21, 2011.

98 Final Notice for Aon Ltd, January 6, 2009.

99 Final Notice for Royal Bank of Scotland and NatWest, January 11, 2011.

100 Final Notice for Bank of Scotland, May 23, 2011.

101 Final Notice for Barclays Bank Plc, January 14, 2011.

102 Final Notice for Norwich & Peterborough, April 15, 2011.

103 Final Notice for Credit Suisse (UK) Ltd, October 25, 2011.

104 Final Notices for: Wheatcroft Fox & Co (June 29, 2011) and Peter Fox (June 29, 2011) and Gary Hexley (June 13, 2011) (investment advice); Alexander Brincat (June 28, 2011) and Andrew James Porter (insurance advice, June 22, 2011); The Matrix Model Group (UK) Limited (geared traded endowment policies, March 31, 2011); and David Bedford (October 3, 2011).

105 FSA, "Unregulated Collective Investment Schemes: Project Findings; FSA Unregulated Collective Investment Schemes; Good and Poor Practice Report"; July 2010.

106 Final Notices for: Clark Rees LLP, Paul Clark and Ceri Rees (November 25, 2010); Specialist Solutions Plc and Ian Jones (April 14, 2011); Rockingham Independent Ltd, Jonathan Edwards, Gary Forster and Stephen Hunt (August 15, 2011); and Paul Banfield and Anthony Moss (July 20, 2011).

107 Final Notice for Barclays Capital Securities Ltd, January 24, 2011.

108 See also the Final Notice for David McGrath, the CF10 responsible for compliance oversight at ActiveTrades. McGrath was fined £3,000 for failing to take reasonable steps to ensure that ActivTrades complied with the relevant requirements and standards of the regulatory system, May 23, 2011.

109 Final Notice for Towry Investment Management Ltd, September 29, 2011.

110 FSA "Dear CEO" letter, January 19, 2010; FSA "Client Money & Asset Report", January 2010.

111 Final Notice for JJB Sports Plc, January 25, 2011.

112 Final Notice for City Index Ltd, January 20, 2011.

113 Final Notice for Sir Ken Morrison, August 16, 2011.

114 Final Notice for Swift 1st Ltd, September 8, 2011.

115 Final Notices for: Mark Thorogood trading as Property Park Mortgages; Darren Button, formerly of Property Park Mortgages; Daniel Djaba trading as DPD Consultancy Services; Adeolu Adeosun, formerly of DPD Consultancy Services, and Waheed Hanif trading as The Broker Group (December 7, 2010); Joseph Chinedu Nwosu of Gemmini (April 11, 2011) Mortgages; Jageet Kaur of Gemmini Mortgages (April 11, 2011); Alaba Adewale Adebajo of Whitehouse Estates (January 31, 2011); Selvavinayakam Vigneswaren; Michael Joseph James Lewis t/a Lewis Partnership.

116 Final Notices for Alistair Curren and B-Assured Financial Services (April 14, 2011) and Nazia Bi and Qadeem Mohammed (October 26, 2011).

117 Final Notice for Daniel Hassell, February 7, 2011.

118 Final Notice for Vantage Capital Markets LLP, June 17, 2010.

119 Final Notice for BDO LLP, May 26, 2011.

ISSUE 93 – MARKET ABUSE UPDATE

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The EU Market Abuse Directive 2003/6 ("MAD") left Member States with considerable discretion to design and develop their market abuse regimes. In the United Kingdom, the civil market abuse offences in the Financial Services and Markets Act 2000 are complemented by criminal offences in the Criminal Justice Act 1993. The next issue of the Bulletin provides a brief outline of the current legal framework and an update on recent case law.

However, much of this is bound to change as in October 2011 the European Commission published legislative proposals on a Regulation of the European Parliament and of the Council on insider dealing and market manipulation and a Directive of the European Parliament and of the Council on criminal sanctions for insider dealing and market manipulation. The next issue of the Bulletin also gives an overview of the legislative proposals and explores their practical implications, with a focus on the United Kingdom.

COMPLIANCE OFFICER BULLETIN

The regulatory environment in which financial institutions operate has been one of constant change and evolution in recent years, not only as a result of the FSA's own regulatory initiatives, such as the move to more principles-based regulation, but also as a direct consequence of the need to implement European directives within the United Kingdom, and domestic and international responses to the credit crisis.

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