



FCA: Our FSF Approach for Flexible Portfolio Firms

Presentation to AFM Conference

Bob Martin
Manager
LTS&P – LID - Retail Life Team

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The Financial Conduct Authority (FCA)

Strategic objective

- ensuring the relevant markets function well

Operational objectives

- promoting effective competition in the interests of consumers;
- securing an appropriate degree of protection for consumers; and,
- protecting and enhancing the integrity of the UK financial system



Overview of the firms we supervise

- When the FCA came into being on 2 April 2013 we supervised some 25,000 entities – 23,000 of which we are both prudential and conduct regulator for (*solo regulated firms*) and some 2,000 for which we are the conduct regulator and another regulator, generally but not always the PRA, is the prudential regulator (*dual regulated firms*)
- We conduct categorise our **firms** C1 to C4 (C1 and C2 are fixed portfolio, with C3 and C4 firms labelled flexible portfolio) and prudentially categorise firms P1 to P3
- On 1 April 2014 we took over the supervision of some 40,000 firms in regard to consumer credit
- Besides our competition objective we have also initiated other activities such as that we have currently embarked on in regard to vulnerable consumers

Recap of your obligations to the FCA

- Underpinning all the requirements is the obligation to meet the Threshold Conditions at all times

N.B. TC4 sets out Non-financial Threshold Conditions as well as the Financial Threshold Conditions.

- When did you last question whether your firm met the requirements?

- When did you last go on-line to look at the FCA (and PRA) Handbooks?

- You will know, and we will now recap, individuals as well as the firm have obligations to the FCA, and we can take enforcement action against either, or both

Principles for Businesses (PRIN) *from FCA Handbook*

Ref.	Principle	Detail
1	Integrity	A firm must conduct its business with integrity.
2	Skill, care and diligence	A firm must conduct its business with due skill, care and diligence.
3	Management and Control	A firm must take responsible care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
4	Financial prudence	A firm must maintain adequate financial resources.
5	Market conduct	A firm must observe proper standards of market conduct.
6	Customers' interests	A firm must pay due regard to the interests of its customers and treat them fairly.
7	Communications with clients	A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.
8	Conflicts of interest	A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client.
9	Customers: Relationships of trust	A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgement.
10	Client's assets	A firm must arrange adequate protection for client's assets when it is responsible for them.
11	Relationships with regulators	A firm must deal with its regulators in an open and co-operative way, and must disclose to the appropriate regulator anything relating to the firm of which that regulator would reasonably expect notice.

Greater emphasis on individual Accountability - Controlled Functions

Type	CF	Description of controlled function
Governing functions*	1	Director function
	2	Non-executive director function
	3	Chief executive function
	4	Partner function
	5	Director of unincorporated association function
	6	Small friendly society function
Required functions*	8	Apportionment and oversight function
	10	Compliance oversight function
	11	Money laundering function
	12	Actuarial function
	12A	With-profits actuary function
	12B	Lloyd's actuary function
Systems and controls function*	28	Systems and controls function
Significant management functions*	29	Significant management function
Customer functions	30	Customer function

***Significant Influence Functions (SIF)**

Note: FSA CP 10/3 - Effective corporate governance (Significant influence controlled functions and the Walker review)

Code of Practice for Approved Persons (APER 4)

4.1= An approved person must act with integrity in carrying out his accountable functions

4.2=An approved person must act with due skill, care and diligence in carrying out his accountable functions

4.3=An approved person must observe proper standards of market conduct in carry out his accountable functions

4.4= An approved person must deal with the FCA, the PRA and other regulators in an open and cooperative way and must disclose appropriately any information of which the FCA or the PRA would reasonably expect notice

4.5= An approved person performing an accountable significant-influence function must take reasonable steps to ensure that the business of the firm for which he is responsible in his accountable function is organised so that it can be controlled effectively

4.6= An approved person performing an accountable significant-influence function must exercise due skill, care and diligence in managing the business of the firm for which he is responsible in his accountable function

4.7= An approved person performing an accountable significant-influence function must take reasonable steps to ensure that the business of the firm for which he is responsible in his accountable function complies with the relevant requirements and standards of the regulatory system

The FCA Approach

Our approach is based on 10 Principles:

- More forward-looking and pre-emptive;
- Focused on judgement, not process;
- Greater focus on business models and culture of firms;
- Focused on big issues and root causes of problems, not just the symptoms;
- More consumer focused;
- Quicker resolution of event-driven work, as well as more robust when things go wrong;
- Orientated towards firms doing the right thing for their customers;
- Greater emphasis on individual accountability at firms;
- Externally focused, engaged and more transparent; and
- Joined-up approach internally.

How will we achieve our objectives?

Supervision of firms – Three Pillars – proportional approach C1 to C4

1. Firm Systematic Framework

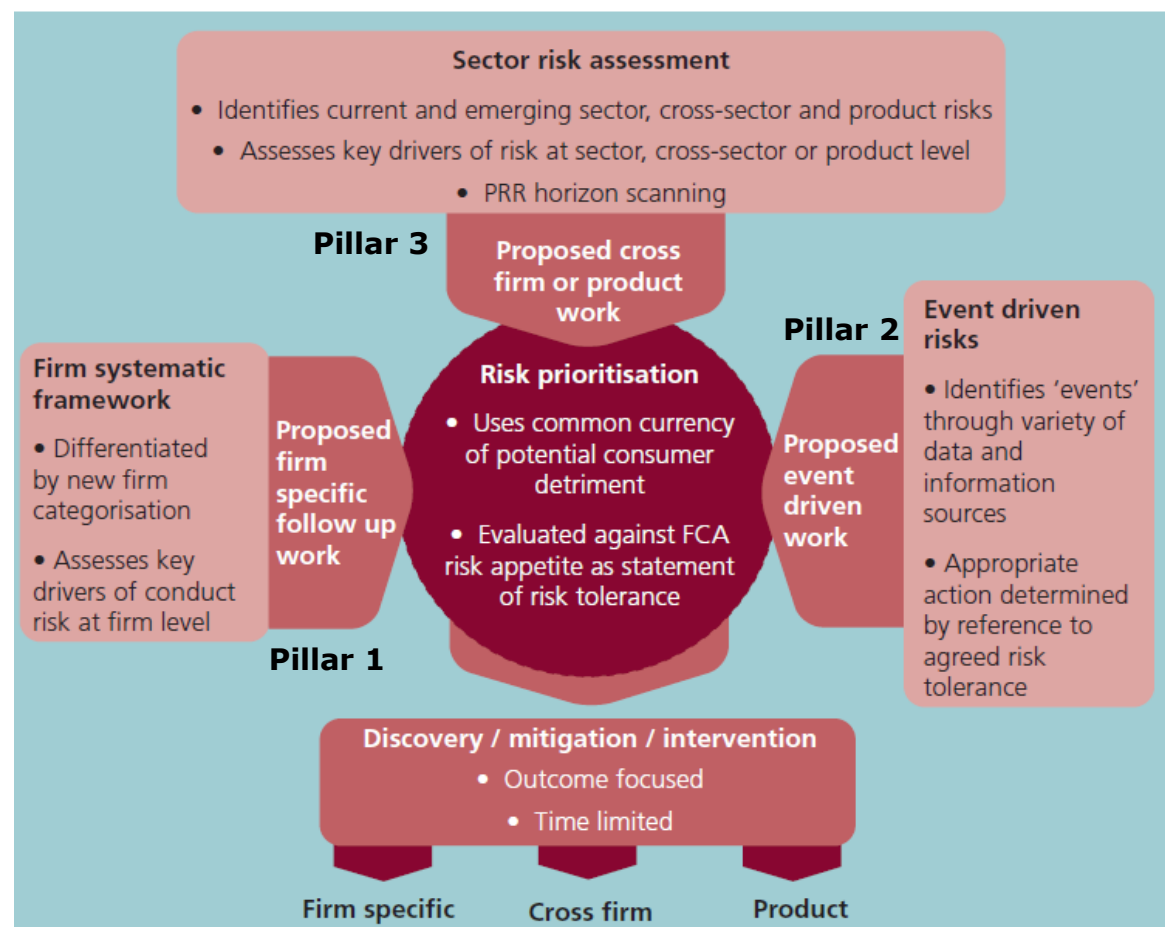
Forward looking preventative work through structured conduct assessments and regular engagement with firms to assess whether the firm is being run, currently and prospectively, in a way that results in the fair treatment of customers.

2. Event-Driven Supervision

Addressing the causes of potential or actual detriment that occur outside of Pillar 1, which have a direct impact on consumer protection or market, securing customer redress or other remedial work where necessary. This will cover issues that occur outside the firm assessment cycle, and will use better data monitoring and intelligence.

3. Issues and Products Supervision

Forward looking, fast, intensive campaigns on sectors of the market or products within a sector that are putting or may put consumers at risk.



FSF for Flexible Portfolio Firms (1 of 3)

- We have devised a self-assessment questionnaire
- We have field tested this questionnaire with 4 firms:
 - Reliance
 - Foresters Friendly
 - Cirencester
 - Bus Employees
- We will now roll this out to all C4s and wish to seek your views on how best to do this (see next slide)
- There is a minimum requirement will be for firms to complete this at least once in a 4-year cycle

FSF for Flexible Portfolio Firms (2 of 3)

- Although we only require the completed questionnaire to be sent to us (on request) once in a 4-year cycle, we believe there is merit in making the questionnaire available to all C4 mutuals now, in order that they can maintain it on an on-going basis (This would assist in evidencing considering of conduct risk as part of the ORSA process).
- We would suggest under Principle 11 firms voluntarily make an additional submission whenever there is a significant change that could impact conduct risk

FSF for Flexible Portfolio Firms (3 of 3)

- The questionnaire is structured into 5 Sections:
 - Background Details
 - Business Model
 - Management and Governance
 - Controls
 - Signature page
- It has some 150 questions, the vast majority of which are answered by a tick in a box
- No attachments are required for the submission and text boxes have deliberately been limited in size so that responses are kept short
- Let's hear from some of the firms that have already completed it

Bringing the FSF and APER together: *Sign off page from FSF Questionnaire*

Signature

I confirm that the information given on this questionnaire (and in any attached additional sheets) is correct and complete to the best of my knowledge and belief.

I also understand that it is a criminal offence to knowingly or recklessly give false or misleading information to the FCA under section 398 Financial Services and Markets Act 2000.

Signed

Date

Recap on what you can expect from us: The FCA aims to be a judgement based, forward-looking and pre-emptive regulator

The FCA's approach will emphasise 5 elements:

- be more **forward-looking** in assessment of potential problems – looking at how we can tackle issues before they start to go wrong;
- **intervene earlier** when we see problems and before they cause consumer detriment or damage to market integrity;
- **tackle underlying causes** of problems, not just the symptoms, as this will be more effective and efficient in the longer term for consumers and firms;
- **secure redress** for consumers if failures do occur; and
- **take meaningful action** against firms that fail to meet our standards through levels of fines that have a deterrent effect.

To do this, we were given additional powers at the time of our formation. These include the ability to:

- temporarily ban products or restrict sales for up to 12 months;
- stop misleading financial advertising;
- impose requirements on firms; and
- subject to consultation, tell the market earlier about enforcement action

How will we achieve our objectives?

Protecting the perimeter

The FCA's aim is to ensure that **the right firms, run by the right people, selling the right products to the right consumers, are approved to do business.**

To achieve this, the FCA will continue the FSA's conduct requirements but add some new elements to the authorisation process, including:

- new **business model threshold condition**, to ensure firms have a viable and sustainable business model appropriate for the nature and scale of business they intend to carry out;
- a risk-based approach to approving controlled functions; and,
- a streamlined process for dual-regulated firms.

We need firms to fully understand their responsibilities and not to have any misunderstanding that we are available for consultancy services.

How will we achieve our objectives?

Supervision of firms – Prudential Supervision

Although primarily a conduct regulator, the FCA is the solo regulator for firms not prudentially regulated by the PRA.

Approach	Key Features
<ul style="list-style-type: none"> Starting principle is that firms should be allowed to fail, therefore, our focus is on mitigating the impact on retail customers and market integrity of firms failing or under financial strain. Our approach is to ensure that any failure is orderly by ensuring that customers assets and money are protected. Prudential supervision is graduated according to prudential significance. On-going dialogue with PRA where we both have prudential responsibilities for a group. 	<p>Prudential Classification – based on the impact that the disorderly failure of a firm could cause in terms of market disruption and market failure.</p> <p>Setting Capital & Liquidity Financial Resource Requirements – assessing financial resources requirements for our most prudentially significant firms.</p> <p>Regulatory Return Monitoring – pro-actively reviewing returns for the most significant firms and acting on alerts for other firms.</p> <p>Thematic Work – cross-firm capital / liquidity work (including smaller firms)</p>

How will we achieve our objectives?

Approach to Competition

- Our competition mandate gives us an operational objective to promote effective competition in the interests of consumers, as well as a duty to do so when exercising general functions (making rules, guidance, codes and policies)
- We can use our existing regulatory toolkit to promote competition, including general rule-making powers and firm-specific orders, as well as being able to refer issues to the OFT
- We expect to use market studies as our main tool for examining competition issues in the markets we regulate, and completed our first market study into general insurance add-ons earlier this year

Summarising - what should firms expect from the FCA?

- Greater intensity and focus of conduct supervision;
- More focus on whether their business model delivers the right outcomes for consumers and behaviours in the markets they operate in;
- A greater expectation of a strategic approach to the conduct agenda and senior management and board engagement in it;
- Greater appetite for pre-emptive intervention;
- More purposeful engagement through systematic assessment and issues and product work delivered by a range of sector-skilled supervisors;
- More focus on causes of problems that we see;
- A greater expectation that firms demonstrate they have resolved issues promptly (not FCA devoting resources to monitoring this);
- More engagement of FCA senior management, especially for larger firms; and
- A predictable and committed regulator, which works with industry in a balanced way.

Thank you for your attention

Q&A session