Policy briefing

April 2016

FCA Business Plan 2016

FCA Business Plan – key areas for coming year:

- **Firms' culture and governance:** strong culture and governance which helps competition and consumers alike;
- **Pensions:** fair treatment for consumers, stronger competition and a market that meets consumer needs;
- **Financial advice:** affordable, professional advice to meet consumers' changing and complex needs;
- **Innovation and technology:** resilient systems and new sources of competition;
- **Treatment of existing customers:** effective competition, a fair deal and greater transparency for long-standing customers;
- **Financial crime and Anti-Money Laundering:** better proportionate and more efficient AML controls and consumers who are better able to avoid scams;
- **Wholesale financial markets:** strong controls to ensure clean, efficient and effective markets.

Particular areas of note to the CII and its members:

- **Delivering the Financial Advice Market Review:** the FCA will work on implementing the recommendations throughout the year, as well as developing clear policies to support the development of the advice market. The FSCS Funding Review will also commence in April 2016.
- **Adviser professionalism:** FCA supervisory focus will continue to be on supporting increased financial advice professionalism, and will increase communications with the sector and continue to assess advice suitability
- **Senior Managers and Certification Regime:** developing a policy to extend this to all FSMA firms.

Overview

The Financial Conduct Authority (FCA) published on 5 April 2016 its annual business plan for the year 2016-17.
http://www.fca.org.uk/news/our-business-plan-2016-17

This included a summary of the organisation's role, an overall risk outlook (setting out socio-economic, regulatory/political risks, technology and culture), a list of seven areas of particular interest, plus a list of additional key workstreams and its ongoing activities.

Chief Executive's Introduction

Tracey McDermott, Acting Chief Executive of the FCA said: "Our overall priority is to ensure an effective and proportionate regulatory approach which tackles the problems of the past without inhibiting the developments of the future. Key to this is delivering a sustainable model of regulation which allows us to focus our resources on the biggest risks to our objectives in a flexible and tailored way.

Over the course of this year we will continue to embed sustainability in everything we do. We will impose new requirements where they are needed, encourage industry-led initiatives where appropriate and remove or adapt regulation where the benefits do not justify the costs. This year, we will review whether aspects of our rules may be outdated or no longer effective in advancing our statutory objectives, and consider which may need to be removed or redrafted to better do so. We will have a particular focus on how technology can be used to make compliance easier and more effective."

Overall risks

Macro/socio-economic

- The 'slow but stable' forecast may motivate firms to diversify or seek returns elsewhere. However, others may become complacent to review business models to reflect new growth patterns and changed consumer needs.
- Firms might sell lower volumes, and may respond by reducing costs, seeking efficiency gains, or trying to sell more products to existing customers.
- Debt as percentage is projected to rise again, exposing consumers to liquidity risks.
- Market volatility has the potential to create capital losses, some of which may be unforeseen by investors who may not have understood the inherent risk of often very complex products. While such volatility cannot be controlled by the FCA, their role of maintaining market integrity requires an understanding of developments that could potentially damage market confidence and access.

Policy and regulation

In response to the financial crisis, global-level regulatory initiatives G20 finance ministers and the Financial Stability Board prioritised new market and prudential standards. A new financial regulatory framework has been created, with many new regulations, such as CRD IV and Solvency II, now in force and the rest being implemented over the next three years.

- **EU referendum:** the FCA are considering the issues that could have the potential to impact its objectives, including considering the immediate and short-term consequences of an exit vote, such as the potential for increased market volatility.

Technology

The use of smart data and advanced analytics within financial institutions has created large volumes of data, which firms can filter and use in marketing and product development, driving risk-based pricing and more personalised products, such as telematics in cars and more health and lifestyle-based insurance. Two areas were particularly singled out:

- **Blockchain technology** represents an alternative approach to the safe storage of information of value such as trade execution, clearing and settlement and custody. While this new alternative approach has many advantages, it also presents new challenges related to data privacy, defect corrections, and trust in decentralised financial servicing.
- **Cloud technology** this could allow businesses to establish computing estates quickly via specialist firms that provide the computing hardware and associated services quickly and cost-efficiently, allowing them to scale their business without large up-front investments, reducing barriers for new market entrants and improving competition.

Conduct and Culture

Conflicts of interest are still driving risk: this is particularly susceptible in firms playing multiple roles with multiple clients. In investment management, conflicts of interest may occur where market participants do not prioritise consumers' interests, and controls over how client money is spent may be lacking. The risk is heightened by limited consumer oversight and challenge.

Transfer of risk

In some areas, such as pensions, Government policies are shifting responsibility for financial planning to individual consumers, which brings risks as well as opportunities. One risk is the adequacy of long-term financial planning, hence a greater need for financial support and advice so they can assess and meet their needs.

FCA priority areas

The FCA have identified seven areas of primary focus for their discretionary work over the year ahead:

- **Firms' culture and governance:** strong culture and governance which helps competition and consumers alike;
- **Pensions:** fair treatment for consumers, stronger competition and a market that meets consumer needs;
- **Financial advice:** affordable, professional advice to meet consumers' changing and complex needs;
- **Innovation and technology:** resilient systems and new sources of competition;
- **Treatment of existing customers:** effective competition, a fair deal and greater transparency for long-standing customers;
- **Financial crime and Anti-Money Laundering:** better proportionate and more efficient AML controls and consumers who are better able to avoid scams;
- **Wholesale financial markets:** strong controls to ensure clean, efficient and effective markets.

These priorities do not represent the totality of the FCA work, but will be used to drive their decisions about thematic projects and market studies and also inform the areas for particular attention in the course of their core activities.

Firms' culture and governance

The Business Plan includes substantial content on what the regulator sees as a critical area of work over the next year. It wants to see:

- firms managed in a way that promotes appropriate culture and behaviours;
- firms' governance and culture contributing to good outcomes for customers and market integrity, and to promote effective competition in the interest of consumers; and
- firms having effective governance arrangements in place to identify the risks they run in their business models and operations, and a strategy to manage and mitigate these risks to deliver fair outcomes to customers, clients and market integrity.

Governance

While the specific design of governance arrangements provides an infrastructure for how firms are run, the regulator's focus is on their effectiveness. Senior managers have a crucial role in demonstrating that they are accountable and responsible for their part in delivering effective governance, including taking responsibility and being accountable for the decisions they make and exercising rigorous oversight of the business areas they lead.

Culture

The regulator sees culture as a set of shared values and norms that characterise a particular organisation – the mind-sets that drive behaviours in firms:

- Firms need to own and manage their cultures at all levels and understand the drivers that will help or hinder them to achieve the cultures they aspire to; and
- Firms must understand the importance the FCA attaches to delivering culture change, where it is relevant to statutory objectives, and evidence it by outcomes, with clear indicators that the drivers of culture are measured, monitored and managed.

Specific risks

- **Poor cultures** in firms drive behaviours that result in poor outcomes for consumers and markets.
- **Firms' strategies, business models and governance arrangements** are not aligned with firms' values and good conduct.
- **Incentive structures and performance management** do not reward behaviours that act in the long-term interests of customers and market integrity.
- **Weak governance and lack of accountability** create poor oversight of risks to customer and market integrity risks in how firms are run.

Planned activities

Accountability and governance

The key aims of the Senior Managers & Certification Regime (SM&CR) are to enhance senior level individual accountability in deposit takers and PRA-designated investment firms, and enhance conduct standards at all levels.

The regulator's revised framework for insurers is another part of a drive to raise standards of individual conduct across financial services. Different requirements exist to ensure proportionate requirements on firms, depending on whether they fall under Solvency II. The FCA will:

- continue to embed the new regime into its supervisory approach and processes, and focus on how SM&CR is integrated in the way deposit takers and PRA-designated firms are run.
- begin extending the accountability regime to all FSMA firms, including further developing the regime for insurers.

Culture

The FCA will focus on what it sees as the most significant drivers of good or poor mindsets and behaviours, such as incentives and remuneration, and the steps firms take which address associated risks, with particular interest in the direction of travel of firms' cultures and if indicators show progress. The FCA will:

- continue to demand high standards of conduct, backed by supervision and enforcement action if necessary so that appropriate culture remains a top priority for firms' management;
- continue to support and drive culture change as the conduct regulator; and
- promote constructive discussions with various stakeholders, including industry and consumer groups, to gain a better understanding of how to achieve long-lasting cultural change across markets.

Pensions and retirement

This is a priority sector given the fundamental recent changes to the market, and the regulator will look across the sector to ensure its policies support fair treatment of customers and encourage competition. The FCA will also aim to raise consumer awareness, disrupt scams and take enforcement action against unauthorised businesses.

Specific risks

- **Policy changes and demographics:** will have major impacts on the pension sector over the longer term, with those aged 85-plus already the fastest growing segment of the UK population. Consumer choices throughout retirement are becoming both more complex and more significant.
- **Pension products with high costs/uncapped fees:** can disproportionately reduce fund values, with a significant cumulative impact on consumers' funds.
- **Alternative investments** will be attractive to more customers, and carry unique risk and advice implications.
- **Access or attractiveness of pension choices:** and many struggle to contribute to a pension. This puts them at risk of an underfunded retirement.

Planned activities

Retirement Outcomes Review: the regulator expects to launch this in 2016/17 to consider the impact of the pension reforms on competition and switching in the market. Research and data analysis has found that many people are using the pension freedoms to either release their pension pot as cash or to choose drawdown products, all impacting the selecting of an annuity. The FCA will work to further understand how consumers react to 'wake-up packs', which encourage them to take action, and how they use and respond to the various annuity comparison tools.

Early exit charges cap: a Treasury consultation in February 2016 concluded that early exit charges constitute a key barrier to accessing the freedoms. Parliament then called upon the FCA to develop and consult on proposals for cap on early exit charges.

Pension reforms – changes to rules and guidance: the FCA will publish a policy statement in Q2 this year, which will summarise responses to the earlier consultation, and publish the final rules and guidance.

Annuities Sales Practices: the FCA continues its review of firms' disclosures to existing customers about enhanced annuities through their non-advised sales processes. The FCA has asked several firms to carry out a more extensive sample review of their past annuity sales, and will assess the results of this work to decide next steps.

Annuities secondary market: to create a consumer protection model for the secondary annuities market which is scheduled for April 2017. The FCA will issue a consultation paper.

Accumulation: – effectiveness of Independent Governance Committees: the regulator will undertake a review of the effectiveness of Independent Governance Committees (IGCs). The review will assess how effective IGCs are in helping pension providers deliver value for money for workplace pension policyholders.

Financial advice

Specific risks

- **Consumers need more support:** as consumers' needs, finances and financial literacy become more varied and complex, the need for appropriate, accessible advice and products is growing.
- **Advisers may not always give consumers:** the most suitable investment advice, may offer a limited range of products or have staff reward schemes that motivate sales over suitability.
- **Consumers may reject paid-for financial advice:** because of the potential cost. They may choose non-advised sales, even when support is better for their needs.
- **Complex charging structures:** and poor transparency make it harder for consumers to compare products.

Planned activities

Delivering the Financial Advice Market Review

The FAMR final report set out a series of recommendations aimed at stimulating the development of a market that provides affordable and accessible financial advice and guidance for everyone, at all stages of their lives. These included recommendations for the FCA to:

- Simplify and clarify the regulation of financial guidance.
- Support firms offering 'streamlined advice' on a limited range of consumer needs.
- Create a specialist Advice Unit operating in a similar way to the FCA's Project Innovate to give regulatory support to new automated advice models.
- Clarify certain rules relating to financial advisers including on cross subsidisation, training and fact finds.
- Consider introducing risk based levies or wider funding classes as part of the FSCS Funding Review.

- The review also contained recommendations for the FCA, Government, and industry designed to increase consumer engagement with financial advice, including through the provision of workplace advice.

The FCA will work on implementing the recommendations throughout the year, as well as developing clear policies to support the development of the advice market. The FSCS Funding Review will also commence in April 2016.

The FCA and the Treasury will report jointly to the Economic Secretary and FCA Board in 2017 on the progress made towards implementation. In 2019, both organisations will conduct a review of the outcomes from FAMR.

Professionalism and the suitability of advice

The FCA supervisory focus will continue to be on supporting increased financial advice professionalism, and will increase communications with the sector and continue to assess how suitable advice is. It will also monitor any changes that result from implementing FAMR proposals.

Innovation and technology

Specific risks

- **Widespread adoption of technology limited by vulnerabilities** in the design and management of systems and infrastructure.
- **Reliance on complex IT infrastructures** which can complicate the maintenance of key services such as payments. Ring-fencing of retail banks can exacerbate such risks.
- **Security of process outsourcing:** firms looking to tighten margins but they have little or no control over the security or functionality.
- **Cyber-attacks are increasing and pose risks to consumers and markets**: some attacks are likely to be successful and firms may not have adequate defences or effective plans to identify and respond to them.
- **Rigid regulation** stifling innovation in financial services.

Planned activities

Encouraging innovation, competition and new entrants to the market

The FCA will increase both awareness and the capacity of Project Innovate to provide advice and support for innovative developments which increase competition in the interests of consumers:

- increase signposting of firms to regulators in other jurisdictions to encourage UK-based firms to grow internationally, and support non-UK investors entering the UK market.
- launching the Regulatory Sandbox: creating a safe place for businesses to test new ideas to ensure they meet regulatory requirements. This will accelerate the development and testing of genuinely novel products which benefit consumers and provide a leading example to regulators in other countries.

Operational resilience

The FCA work will include communicating its expectations in effective IT and operational resilience, and working with firms to understand their capabilities in this area, such as

- identifying, managing and protecting key assets;
- threat and attack detection, response and recovery; and
- appropriate governance to manage risks and learn lessons.

Reactive work will also be undertaken when outages occur to understand their impact on consumers and markets and how firms respond to them.

Keeping pace with developments in Big Data

The Call for Input on Big Data Use in the General Insurance Sector will be used to better understand how this area affects customers and whether it fosters competition. The regulator will also analyse how its regulatory framework affects Big Data developments to determine whether we will conduct a market study or take a different approach.

Automated advice

The regulator will be implementing the FAMR's recommendation to create an 'Advice Unit' to support firms with automated advice models with the potential to deliver affordable and accessible financial advice to consumers.

Treatment of existing customers

Specific risks

- **Tougher economic conditions** may lead to firms seeking to 'manage' back book customers into more expensive/default products.
- **A growing number of over-indebted mortgage holders** and those with limited access to credit. A future rise in interest rates may make it harder for borrowers, including those already in payment difficulties, to repay. If credit conditions tighten this can leave higher risk consumers with limited options.
- **Firms may restructure products, bundling together add-on services** to make comparison difficult or lock borrowers into higher rates.
- **Firms may apply unjustified exit or switching fees** which reduce competition.
- **Consumers' weak bargaining position could give Investment Management firms** little incentive to compete on value for money.

Planned activities

Competition in retail banking

Following concerns that essential parts of the UK retail banking sector do not compete effectively and fail to meet the needs of personal consumers or small and medium-sized enterprises (SMEs), the Competition and Markets Authority (CMA) launched its retail banking investigation.

The FCA has worked with the CMA to produce a package of proposed remedies aimed at:

- increasing customer awareness of the potential benefits of switching and prompt shopping around.
- supporting customers' ability to make comparisons between providers.
- making Business Current Account opening easier.
- improving the switching process.
- reducing the advantages banks have from incumbency (existing customers' reluctance to switch).

Cash savings market study follow-up

The FCA study found that the market was not working well for many consumers. In particular, many providers hold significant amounts of consumers' savings balances in accounts opened more than five years ago. As a result, the regulator is developing package of remedies to deliver improved customer awareness about the interest rates on their accounts, their providers' strategies to long-standing customers and to encourage more shopping around.

In 2015, following consultation, the FCA published final rules for various disclosure remedies. This year, following completion of real-life trials, it will consult on a second package of remedies to improve transparency and increase shopping around and switching.

Fair treatment of long-standing customers in the life insurance sector

In March 2016 the FCA published the findings from the thematic review of the fair treatment of long-standing customers in life insurance. It reported a mixed picture in the firms we reviewed, demonstrating good practice in one or more areas and poor practice in other areas. The regulator will be undertaking further work:

- consulting on non-Handbook guidance which will provide firms with extra detail on the actions they should be taking in order to treat their closed-book customers fairly in the future.
- convening an industry-wide discussion with a view to industry reaching a voluntary solution to capping or removing exit and/or paid-up charges on investments of the type that were the subject of the thematic review.
- working with the firms caught by the review to address the specific findings identified through our ongoing supervisory work.
- consider whether some of those firms have failed to meet standards and, if so, whether remedial and/or disciplinary action is necessary in relation to these firms or others across the market.

Current and planned thematic work and market studies

	Work begins	Completion or Reporting
Pensions and retirement income		
Retirement Outcomes review	Q2 2016	Complete Q3 2016
Annuities sales practices		Complete Q4 2016
Review of effectiveness of Information Governance Committees	Q2/3 2016	Complete Q4 2017
General insurance and protection		
Big Data review		Report Q3 2016
GI brokers' PII review		Complete Q2 2016
Appointed Representatives review	End Q3 2015	Complete Q2 2016
Retail investments		
Inducements and conflicts of interest		Complete Q2 2016
Other		
Mortgages: Embedding the MMR – Responsible Lending review		Complete Q4 2016
Financially Vulnerable Customers review		Complete in Q3 2016

CII Group Policy & Public Affairs
7 April 2016

Appendix A

Other key elements of the FCA's 2016-2017 workstream

Sustainable regulation

We are committed to ensuring that the UK has robust, respected regulation. We will be tough when required but we also recognise that regulation must be able to adapt and evolve to the changing market place.

We will review whether aspects of our rules are outdated or are no longer an effective way of advancing our statutory objectives. Following this, we will consider whether any rules can be removed or redrafted to better achieve our statutory objectives.

The Enterprise Bill, currently being debated in Parliament, may also apply to the FCA. Under the legislation, regulators are required to have the cost of any changes in relevant regulations verified by the Regulatory Policy Committee. This builds upon existing requirements within FSMA, which require us to conduct cost-benefit-analyses when we consult on new policy.

Payment Protection Insurance (PPI)

The current complaints framework and our supporting supervisory work has so far resulted in over £22.2 billion redress being paid to over 12 million customers.

At the end of 2015, we published a consultation paper which proposed to set a deadline for making PPI complaints and to run a high-profile communications campaign telling consumers about it and signposting how to complain. Our consultation also proposed new rules and guidance for firms on handling PPI complaints after the Supreme Court's decision in the Plevin case.[20]

In 2016/17, we will consider the responses to the consultation, decide our final approach and, if appropriate, publish a Policy Statement. We will also continue to monitor and challenge firms to ensure that they continue to deal fairly and promptly with PPI complaints.

20 The Court ruled that the lender's failure to disclose the large commissions payable out of the consumer's PPI premium made their relationship unfair under s140A of the Consumer Credit Act.

Prudential regulation

This year, our prudential work will focus on the continued implementation of the Capital Requirements Directive IV (CRD IV). We will be implementing changes to our Supervisory Review and Evaluation Process (SREP) to meet the European Banking Authority's (EBA) new guidelines that come into effect in 2016.

Other areas of focus will include implementing the Recovery and Resolution Directive (RRD) and helping firms to improve their wind-down planning in the event of a firm failing.

We will continue to ensure firms have appropriate mechanisms to protect client assets to ensure consumers are protected in the event of failure.

Ring-fencing

After the financial crisis, the Government decided to ring-fence core banking activities from other activities. This is to make it easier and less expensive to resolve banks which get into financial difficulty, and reduce the likelihood of disruption to key services provided by the largest retail banks.

The PRA is the lead regulator for implementing ring-fencing. We have key responsibilities for implementing the regime effectively and we will continue to work with firms as they finalise their plans for ring-fencing.

We will monitor and manage any potential negative impacts of ring-fencing on consumers, market integrity and competition.

Appendix B

Updated organization chart