Association of Foreign Banks – Written evidence (EGC0017)

The Association of Foreign Banks (AFB) represents non-UK headquartered banks operating in the UK. With around 170 members from across the world, we represent 80% of the UK's foreign banking market. Our members (operating via branches and subsidiaries) employ over 110,000 people across the UK.

AFB appreciates the opportunity to respond to the House of Lords Financial Services Regulation Committee's Call for Evidence with a summary of our views on the proposals contained in the FCA's Consultation Paper (CP)24/2. We note the Committee's exchange of correspondence with the FCA on this topic.

AFB submitted a response to CP24/2 to the FCA, focussing on the concerns of international banks operating in the UK. In particular, we highlighted the detrimental impact the FCA's proposals would have on the UK's international competitiveness in financial services. In our view, the proposals do not support the FCA's primary objective and contradict the FCA's secondary competitiveness and growth objective introduced last year.

AFB key points/concerns

AFB is concerned that the publication of the name of an institution at the opening of an enforcement investigation will risk firms suffering significant reputational and prudential damage, even where no misconduct is found to have occurred.

We understand that one of the Executive Directors of Enforcement at the FCA has stated that two out of three investigations within the FCA's current case load would satisfy the proposed public interest test. Further, the FCA has said that it closed 67% of cases without further action in 2023/24. Therefore, if the proposals are adopted, we can expect that a material proportion of the firms named by the FCA in the future would in fact have committed no wrongdoing.

However, consumers and market participants will likely believe that the FCA has named the subject of an investigation because the subject is guilty of significant wrongdoing. This could lead to consumers and counterparties taking action to reduce their exposure to the firm under investigation, for example by withdrawing funds.

As the Committee will be aware, in the FCA's letter, dated 25 April 2024, to Lord Forsyth of Drumlean on CP24/2, it noted that in 2023/24 investigations took an average of 43 months. If the proposals are adopted, the subject of an investigation would be required to wait almost four years after being named, before a decision as to their innocence or guilt is announced. This would be too late to rectify any damage.

The FCA also lacks a reliable dataset to assess how its proposed approach would likely impact the share prices of firms named. The evidence base for disclosures 'not' impacting share prices, as mentioned in the FCA letter, does not include incidents in which the FCA made public disclosures of the type which they are now proposing.

In our view, the FCA's proposals would therefore not enhance its deterrence or enforcement practices for the firms which do commit wrongdoing, but would simply penalise and risk the reputation, and even survival, of innocent firms caught by a broadened scope for disclosure.

Beyond the impact on individual firms, AFB is concerned for the proposals' potential to harm the international competitiveness and growth of the UK's financial services sector, and the stability of its financial markets.

In its letter, the FCA noted the reasons why it has made the proposals, including the aim of enhancing public confidence. However, the publication of an investigation into a firm that has in fact not committed wrongdoing would not further this aim. The public would likely lose trust in that particular firm, as well as the UK market if/when a firm fails. Given this risk to financial stability, AFB was surprised that the FCA did not consider it appropriate for the PRA to have a role in considering the impact a public announcement may have on a bank's liquidity, share prices, and the market, or grant the PRA a veto power over early publication.

On the UK's international competitiveness, the risk of damage as a result of the proposals, adds to existing concerns regarding the attractiveness of the UK for non-UK headquartered firms. AFB members commented that all the factors mentioned above would be considered by their Head Offices when their global strategies are being assessed and would likely result in parent entities deciding not to expand their UK business and the diversion of investment away from the UK.

AFB is also concerned that the proposals are likely to deter overseas talent from accepting senior UK roles, further harming the UK's strength as a financial centre. Staff may not commence employment, or may leave their role, if the FCA announces an investigation into that firm, as there is a risk of being publicly linked to the investigation, unlike in other jurisdictions. This risk would be greater for small firms with fewer senior managers, as individual staff could be more easily identified.

Comparison with other regulatory bodies

If the FCA were to proceed with its proposals in the current form, the UK would be a regulatory outlier; in no other G7 country do the regulators publish details of their enforcement investigations before they are concluded. Multiple overseas regulators do not publicise the opening of enforcement investigations such as the United States Commodity Futures Trading Commission, the French Autorité des Marchés Financiers and the Canadian Office of the Superintendent of Financial Institutions.

We note that the FCA states that the Monetary Authority of Singapore (MAS) has a similar approach to the proposals. However, although MAS does have a "Communications Policy" with a public interest framework, it only publicises the opening of its enforcement investigations infrequently, and generally where the subject matter is already in the public domain.

Additionally, the FCA includes in its letter examples of UK regulatory bodies which have the power to disclose in other sectors, and states that it is not aware of any significant evidence where their approaches harmed the competitiveness of these sectors. AFB believes these are not strong cases for comparison, as the nature of financial markets is notably more international and the secondary objective of the FCA, unlike other bodies, should require it also to consider the impact on the UK's international competitiveness.

We also note that other UK bodies, such as the Office of Financial Sanctions Implementation (OFSI), do not generally name firms under investigation. OFSI does now have the power to make disclosures, but only to highlight compliance lessons for industry. OFSI has clear procedural requirements, set out in primary legislation, as well as an evidential test. In comparison, the FCA's proposals do not include an evidential threshold for naming a firm under investigation. We note that the statutory threshold for the FCA opening investigations is extremely low, and that the proposals do not include a list of objective criteria to be considered before an announcement.

Additional concerns (relationship between FCA and industry)

AFB would also like to highlight to the Committee the unexpectedness of the FCA's proposals, and the lack of usual process followed. For example, the consultation paper was not indicated to industry via the Regulatory Initiatives Grid. This lack of engagement with industry prior to the consultation paper has led to the FCA misjudging the extent of the negative impact on firms, international competitiveness and the markets.

Further, in the Committee's letter dated 18 April 2024 to Nikhil Rathi on CP24/2, the impact of the FCA's proposal on the relationship between regulators and the industry was queried. AFB's view is that the adoption of proposals would negatively affect the relationship between the FCA and industry. Most firms have an ongoing dialogue with their supervisory teams that goes beyond mandatory notifications and disclosures, deriving from a sense of trust and an expectation of fair treatment. This more informal dialogue is crucial for firms to better understand the regulators' evolving expectations, and for regulators to supervise more effectively. However, we consider that the proposals would result in firms being more cautious in their dialogue with the FCA and less willing to engage beyond mandatory requirements, due to the fear of being 'named and shamed'.

We also note that, as a result of the criticism of the proposals from many stakeholders, the FCA is reconsidering its approach (see here).

Specifically, it has stated that the public interest test will include 'consideration of the potential impact [of publication] on the firm and the market'. We will engage with the FCA in this additional period of consultation and reiterate the recommendations set out below.

AFB recommendations: how the FCA could achieve its aims

The FCA's 25 April 2024 letter to Lord Forsyth of Drumlean on CP24/2 sets out the circumstances in which an investigation may be made public under the current framework. This includes a disclosure in exceptional circumstances by the FCA, a disclosure to Parliament which Parliament may decide to publish, or a firm announcing the investigation. AFB would reiterate that the current framework therefore provides the opportunity to name the subject of an investigation in circumstances where a publication is genuinely needed. In our view there is no reason why the discretion to disclose should be broadened.

In this letter, the FCA firstly states that it aims to conduct fewer investigations at a faster pace and make firms aware of critical issues at a much earlier stage. However, naming the subject of an investigation would have no beneficial impact towards achieving these goals. Instead, AFB recommends that the FCA should set itself a 12-month deadline for completing investigations. This would achieve the FCA's aim of greater transparency by progressing more quickly with its investigations. It would also help notify firms of issues at an earlier stage, as the details of wrongdoing would be publicised more contemporaneously with the alleged wrongdoing.

Secondly, the FCA stated in the letter that it will improve triage across the authorisations, supervision and enforcement teams to ensure it deploys all tools available. In our view the use of its current tools (such as Dear CEO letters, supervisory intervention, and thematic reviews) would be more effective in achieving the FCA's aims than public disclosure. Additionally, we would note that the letter states the FCA aims to make firms aware at a much earlier stage of important issues. An 'Enforcement Watch' publication (similar to the existing 'Market Watch') would be more effective than the FCA's proposals in CP24/2. In this document, the FCA would publicise the opening of investigations on an anonymised basis, containing the type of firm under investigation and the relevant product/service. This approach, especially if released in a timely manner, would be useful in helping firms improve their practices and standards. It would also achieve the FCA's aims, by providing insight to consumers and industry, and increasing awareness and education in the areas of concern.

Thirdly, in the letter the FCA states that it aims to encourage confidence in whistleblowing. We believe that that confidence would be better achieved through quicker investigations, so that the whistleblower is reassured that their concerns are being/have been investigated.

Conclusion

In light of the comments made above, we would encourage the Committee to urge the FCA to revisit its proposals and consider the recommendations we have put forward.

If the Committee would be interested in reading AFB's response to CP24/2 (as submitted to the FCA), please contact us.

10 October 2024