

"It is amazing what you can accomplish if you do not care who gets the credit". Harry S Truman

Unlike Mr Truman the Financial Conduct Authority ('FCA') does care who gets Credit and how firms are regulated under the Consumer Credit Act. Many Firms are now going through the process of seeking FCA authorisation since they took over the regulatory baton from the Office of Fair trading and this month there was a speech from the FCA regarding the way they will look to regulate the industry.

Already a major payday lender has entered into a voluntary agreement with the FCA.

Consumer credit Speech

Linda Woodall, Director of Mortgage and Consumer Lending of the FCA, has given a speech this month regarding consumer credit.

She detailed how the FCA's strategic objective for consumer credit is to ensure that the market functions well for consumers, leading to the three operational objectives to:

- secure an appropriate degree of protection for consumers
- protect and enhance market integrity
- promote effective competition in the interests of consumers

The FCA seeks a change in the approach the industry takes:

- in advertising and financial promotions
- in product terms and conditions
- at the application stage
- in customer service during the life of the product
- post-sale problems, including debt recovery, debt management and complaints handling

The FCA requires firms to put the interest of its consumers at the heart of its business.

FCA Approach to regulation – Firm reviews due.

The FCA supervise firms using its three pillar approach. We understand that they are putting together a pilot review for tier four firms with the aim of reviewing all Tier 4 firms by the end of 2017. The 3 Pillars are:

Pillar 1: The Firm Systematic Framework aims to make forward-looking assessments of firms, and the risks they pose to the FCA objectives. It is designed to answer the key question of 'are the interests of customers and market integrity at the heart of how this firm is run?'

Pillar 2: The second supervisory pillar is based on dealing with issues that are emerging or those that have happened, and are unforeseen in their nature, 'event driven work'. It includes issues such as whistleblowing allegations; spikes in reported complaints and investigating reports of mis-selling. The FCA will use this for intelligence to drive such reviews.

Pillar 3: 'issues and products' and is commonly known as thematic work. This will identify and determine the

extent of any cross-firm or product issues, and provide a wider basis for the FCA to investigate and, if needed, mitigate.

A current example of such reviews is the ongoing thematic review into the forbearance practices of high-cost short-term credit providers. FMConsult has posted many articles on LinkedIn and Twitter recently regarding FCA enforcement on the back of this thematic review.

Another thematic review is also underway to look at the quality of advice provided by debt management companies. Evidence suggests that consumers with multiple debts approach debt management providers when these debts become unmanageable. It is vital that when they do so, the advice they receive is appropriate and not driven solely by firms' own incentive structures.

Pay Day Lender enters into voluntary agreement with the FCA

The FCA discovered when it took over consumer credit regulation that the firm had failed to assess whether customers had the ability to meet repayments in a sustainable manner.

The FCA has agreed an approach with the firm for remedial redress for those customers who were affected by inadequate affordability assessments:

- Approximately 330,000 customers who are currently in excess of 30 days in arrears, will have the balance of their loan written off and will owe the firm nothing
- This equates to a total impact in the company's profit and loss sheet of £220 million.
- Approximately 45,000 customers who are between 0 and 29 days in arrears will be asked to repay their debt without interest and charges and will be given an option of paying off their debt over an extended period of four months.

Clive Adamson, Director of Supervision, said "We are determined to drive up standards in the consumer credit market and it is disappointing that some firms still have a way to go to meet our expectations. This should put the rest of the industry on notice – they need to lend affordably and responsibly."

Achieving the correct consumer outcome and having appropriate client take on processes are high on the FCA's agenda. FMConsult can assist firms in reviewing their arrangements in regards to client take on processes by providing expert analysis of whether the firms systems and controls are adequate to meet FCA requirements.

FCA Innovation Hub.

The FCA has launched the Innovation Hub, part of its 'Project Innovate', which has been set in motion to help support innovators.

As in May's Newsletter, FCA chief executive Martin Wheatley announced the desire to remove uncertainty over compliance when in relation to developing products that could improve financial services for consumers.

The goal of Innovation Hub is provide direct support from a team of dedicated FCA staff to both regulated and non-regulated innovators.

Businesses will need to show that their innovation could bring benefits to the end consumer, either an individual or business, in order to seek the regulator's guidance.

The Innovation Hub will provide to businesses, who qualify, with access to the following:

- a dedicated contact providing individual guidance as appropriate
- additional support for up to a year after authorisation
- help to understand the regulatory framework and how it applies
- identify areas where the regulatory regime needs to adapt to facilitate innovation

Client Assets Money Changes ('CASS')

Firms are reminded that the latest changes to the CASS rules take effect on 1 December 2014.

These include changes to:

1. the way unclaimed assets and money can be treated;
2. the use of the Delivery v Payment (DvP) exemption
3. transfer of client money to 3rd party
4. custody asset agreements
5. CASS7 acknowledgement letters
6. The alternative approach to client money segregation

Further changes are effective from 1 June 2015.

FCA looks to permanently restrict Coco sales to retail investors

The FCA is consulting on permanently restricting the sale of contingent convertible securities (CoCos) to retail investors. CoCos are convertible bonds that absorb losses when the capital of the insurer falls below a certain level. The likelihood of converting to equity is contingent on a specific event.

The FCA said "*We are proposing to make permanent the approach taken in the temporary rules. These rules prevent firms from distributing CoCos in the retail market without first checking that the prospective client meets certain criteria. In effect, firms should not distribute these instruments to ordinary retail investors.*"

CoCos can yield around 6% or 7%, and have proved attractive to investors due to the low interest rate environment. However, their terms and conditions vary widely, and so they could easily be misunderstood by retail investors who are unaware of the details.

The FCA has proposed that firms selling these investments need to ensure the investor has read specified risk warnings and committed not to invest more than 5% of their net assets.

Christopher Woolard, director of policy, risk and research at the FCA, said "[These rules] will make sure that there are appropriate safeguards in place so these complex instruments are offered only to investors who are able to make informed decisions about them."

The regulator is also proposing new requirements also be imposed on mutual society shares, including core capital deferred shares (CCDS).

FCA application to vary a firm's proportionality level with regard to remuneration

Firms or groups that may fall into a lower proportionality level with regard to remuneration may apply for individual guidance from the FCA to vary their proportionality levels.

Applications must be supported by sound reasoning and be justified, with reference to the proportionality principle. For a firm to decide whether to apply to vary its proportionality level, it should identify the firms within its group that the Remuneration Code applies to directly and determine which proportionality level they fall into, by reference to the:

- general guidance on proportionality: The Remuneration Code SYSC 19A; or
- general guidance on proportionality: The Remuneration Code BIPRU firms (SYSC 19C).

Once the FCA has received this information it will determine whether to give the individual guidance. In order to have a consistent decision-making process and to assist firms in understanding the type of information the FCA may require when making its decision, the FCA has published three separate application templates:

- Template A - groups only. Application to move an IFPRU [Prudential sourcebook for investment firms] limited licence or limited activity firm engaging in asset management activities, or a BIPRU [Prudential sourcebook for banks, building societies and investment firms] firm, from the group proportionality level in paragraph 2 to proportionality level 3;
- Template B - groups only. General application to move a firm from the group level into a lower level (excluding IFPRU limited licence asset management firms, or BIPRU firms); and
- Template C - general level change application. For stand-alone firms or a firm that is the only firm directly caught by the Code in the group.

FCA Enforcement cases

FCA fine building society £4m

The FCA has fined a Building Society £4,135,600 for failings when dealing with its mortgage customers experiencing payment difficulties.

Between October 2011 and July 2012, call handlers at the bank, dealing with customers in payment difficulties, failed to deal properly with these customers. They were unable to identify promptly the cause of their problems and their future financial prospects. Leading to customers incurring increased fees and associated interest

According to the FCA, these failures led to significant delays in determining the most appropriate payment solutions.

The redress scheme is currently underway and approximately 33,900 customers will be repaid a total of £8.4 million.

Tracey McDermott said "Customers in financial difficulty need to be treated fairly and sensitively. Firms must ensure that they are taking into account the particular circumstances affecting customers who find themselves in difficulty. Firms need to be dealing with these customers proactively, without delays, in order to ensure they are not losing out."

FCA publishes Decision Notice against former financier

The Decision Notice, states that the FCA has decided to fine the former Financier £290,344 and ban him from performing any function in relation to any regulated activities on the basis that he is not fit and proper because he lacks integrity.

The individual was deemed to have:

- recklessly recommended high risk investment products to eight retail clients, when he knew that he could not justify their suitability;
- was knowingly involved in the falsification of the signatures of two clients on sophisticated investor certificates to suggest that the investment could be legitimately promoted;
- deliberately made investments on behalf of two clients without their knowledge or authorisation;
- deliberately produced inflated valuations of clients' investments in an attempt to mislead them and conceal the poor performance of the investments he had recommended;
- deliberately submitted loan facility and investment applications, on behalf of a number of his clients, which contained inflated incomes and other false and misleading information; and
- deliberately attempted to mislead the FCA by retrospectively creating various documents and misrepresenting that they were contemporaneous.

Two former directors have been fined and banned by the FCA for recklessly failing to protect client money

The enforcement has been issued for recklessly failing to protect client money and committing a number of specific breaches of the FCA's client money (CASS) rules.

Tracey McDermott, FCA Director of the Enforcement and Financial Crime Division said:

"Ensuring that client money is properly protected is a basic, but fundamental, regulatory requirement. [the individuals] conduct fell far short of our standards. Their recklessness contributed to a shortfall of £3 million of client money and resulted in significant consumer detriment.

Under the FCA's CASS rules, client money should be held in a segregated client bank account. The rules are intended to protect client money if a firm becomes

insolvent. [the company and the individuals failed] to protect client monies for which they were responsible."

They were found to have reckless failings:

- client money was wrongly used to pay business expenses;
- failed routinely to pay sufficient funds into its client bank account to cover shortfalls in client money;
- placed reliance upon the offshore facility as a client money resource despite the fact that such a facility was not permitted to be included; and
- The FCA was not informed when a shortfall in client money occurred.

Irish News

Guidelines on Preparing for Solvency II: Forward Looking Assessment of Own Risks (FLAOR)

The Guidelines on Preparing for Solvency II have now been in place for nine months. Undertakings should be making good progress on the System of Governance and Submission of Information guidelines. All undertakings are reminded to submit a FLAOR report before 31 December 2014, using the Central Bank's Online Reporting System (ONR). Firms should use ONR to submit the FLAOR, whether using the FLAOR tool (Low and Medium Low impact undertakings) or submitting an unstructured report (High and Medium High undertakings). It is important that undertakings submit the FLAOR using ONR for the following reasons:

- For "full" Solvency II, in relation to the ORSA submission, ONR will be the mechanism by which the Central Bank will collect ORSA reports. Therefore, during the preparatory phase, it is beneficial that undertakings use ONR to test the end to end submission and reporting process;
- From an audit perspective, it is important that the Central Bank has a record on ONR of the FLAOR submission; and
- If the FLAOR is submitted to the Central Bank through another channel, for example, via email, the undertaking will continue to receive automated reminders from ONR that a FLAOR has not been submitted.

Full instructions on how to submit the FLAOR using ONR are available on the reporting requirements section of the Central Bank website

Consultation on National Specific Templates

As referred to in the May edition of this newsletter, the Solvency II Directive provides for the submission of information necessary to cover national legal requirements or local market specificities. The Central Bank has defined a list of national specific templates (NSTs) and plans to consult on these in November 2014. These national specific templates will be applicable for "full" Solvency II only; there is no intention to require the submission of NSTs during the preparatory phase. The consultation on the national specific templates will be posted on the consultation papers section of the Central Bank website Consultation Papers.

Early Approvals Under Solvency II

The Solvency II Directive sets out that from 1 April 2015 Member States shall ensure that the supervisory authority has the power to decide on a number of "early approvals" under Solvency II.

These include, but are not limited to, ancillary own funds, undertaking specific parameters, matching adjustment and volatility adjustment. The Central Bank plans to survey undertakings in November 2014 to determine undertakings' intention to apply for and use these mechanisms

FMConsult News

FMConsult is currently recruiting highly experienced Compliance executives for roles in its UK and Irish Offices.

All offices provide clients with:

- Compliance monitoring services
- Company and consumer credit authorisation services
- Fund authorisation services
- Outsourced MLRO services
- Outsourced compliance solutions
- Regulatory project assistance (e.g. Investment Restrictions, Money Laundering, Client Money, ICAAPs)

UK and Ireland also provide:

- Investment & Operational Risk management services
- Fund restructuring services
- Internal Capital Adequacy Assessment Process (ICAAP) review and development;
- ACD / Management Company structuring and governance review
- Fund and firm re-domiciliation advice
- AIFM Authorisation
- AIFM monitoring (including risk services)

Dublin also provides Fund UCITS IV Reporting, MLRO and Company Secretarial Services.

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