Trends in Regulatory Enforcement in UK Financial Markets
2014/15 Mid-Year Report

By Robert Patton
In the two and a half years to 30 September 2014, the FCA and FSA imposed over £1 billion in fines, as compared to less than £320 million over the entire prior decade. This increase has been driven by large fines against firms, including LIBOR-related fines. By contrast, fines against individuals have fallen steeply.
NERA maintains a proprietary database of fines and other enforcement activity by the Financial Conduct Authority (FCA) and, previously, the Financial Services Authority (FSA), including data on fines back to 1 April 2002. We have classified fines by the type of underlying alleged misconduct and other criteria, to reveal a detailed portrait of recent enforcement activity and how it conforms to stated priorities. Our analysis reveals underlying trends not necessarily visible from a review of individual cases.

Introduction

Over the two and a half years from the start of the 2012/13 financial year, 1 April 2012, through to 30 September 2014, the FCA and its predecessor imposed more than £1 billion in fines. This compares to less than £320 million over the entire decade prior to 1 April 2012. More than £400 million in fines was handed down in each of the 2012/13 and 2013/14 financial years (See Table 1); moreover, fines are on pace to reach a record level in 2014/15, with a total of £221 million imposed as at 30 September 2014, the halfway point in the financial year. In contrast with the recent levels, in no year prior to 2012/13 did total fines exceed £100 million.

The recent leap to a new plateau in fine amounts has been driven to a large extent by a handful of very large fines imposed on banks and brokerages, including several fines in connection with alleged manipulation of LIBOR and other benchmark lending rates (see Figure 1). Indeed, nine of the 10 largest ever fines have been imposed since the beginning of the 2012/13 financial year, and five of these have been LIBOR fines. However, as Figure 2 shows, the upward trend has not been confined to the very largest fines: the median fine against firms in the first half of 2014/15 has exceeded £6 million, as compared to £1.4 million as recently as 2011/12. If fines against firms continue at their present pace, then they will have reached their highest annual total by the end of 2014/15.
Table 1. FCA\(^1\) Fines, 2011/12 to 2014/15 (First Half)

<table>
<thead>
<tr>
<th></th>
<th>Number of Fines(^2)</th>
<th>Aggregate Fines ((\text{£m}))(^3)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Individuals</strong></td>
<td>(1)</td>
<td>(2)</td>
</tr>
<tr>
<td><strong>Firms</strong></td>
<td>23</td>
<td>26</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>63</td>
<td>45</td>
</tr>
</tbody>
</table>

Notes and Sources:

1. On 1 April 2013, the Financial Services Act 2012 came into force, and the FCA superseded the FSA as financial enforcement regulator. In this paper, unless indicated otherwise, we use “FCA” or “the authority” to refer to the FSA and the FCA collectively.

2. The number of fines and aggregate fines shown in this figure differ slightly from statistics reported in FCA and FSA Annual Reports because, in the Annual Reports, beginning with the 2009/10 edition, each fine is assigned to a financial year based on the publication date of the press release announcing the fine, whereas NERA uses the date of the final notice.

3. Includes fines imposed from 1 April 2014 to 30 September 2014, the first half of the 2014/15 financial year.

On 1 April 2013, the Financial Services Act 2012 came into force, with the FCA taking over from the FSA in the enforcement sphere and receiving certain new powers (discussed below). In addition, an increasing proportion of fines have been assessed under the FCA’s new penalty framework, which applies to conduct occurring on or after 6 March 2010. Both developments may have contributed to the increase in the level of fines against firms. However, the first year in which fines against firms exceeded £400 million, 2012/13, preceded the launch of the FCA, and the majority of fines handed down in that year were not computed under the new penalty framework. Thus, these factors do not appear to have been decisive.

In contrast to the jump in fines against firms, fines against individuals have fallen substantially, both in number and aggregate amount, since reaching a peak in 2011/12 (see Table 1 and Figure 3). Few very large fines have been announced against individuals since that time, and the median fine against individuals fell by over 60 per cent from 2011/12 to 2013/14.

Fine amounts against individuals in the first half of 2014/15 have been different in composition from the previous several years. There have been no fines this year large enough to qualify for inclusion on the list of top 10 fines to date (the smallest on that list is nearly £1 million), but there have also been few very small fines. Indeed, five of the seven fines against individuals in the first half of 2014/15 exceeded £200,000. Thus, as Figure 3 shows, while 2014/15 individual fines are, in aggregate terms, on track to be lower than any of the prior four years, the median fine is at an all-time high. It remains to be seen whether this shift in composition represents an enduring trend or simply reflects the characteristics of the particular fines announced in the first half of this year.\(^6\)

The overall decline in fines against individuals over the past several years appears inconsistent with the FCA’s stated emphasis on increased enforcement against individuals. Several factors that may explain this decline are discussed below in this paper.
Our other key findings include the following:

- Five of the panel banks that set LIBOR and other interbank rates have been fined by the FCA in connection with allegations of manipulation of those rates, as have two brokerage firms, ICAP Europe Limited (ICAP) and Martin Brokers (UK) Ltd. LIBOR fines may be imposed on individuals in the near future.
• Consistent with the overall decline in fines against individuals, fines and fine amounts for Insider Dealing have declined recently. There have been a number of criminal indictments for Insider Dealing, but most of these have related to a single, large-scale investigation (Operation Tabernula), in which the first arrests were made in 2010. The most recent of the FCA’s periodic “market cleanliness” studies suggests that insider dealing in shares ahead of takeover announcements has declined. It may be that, consistent with these findings, earlier enforcement efforts have borne fruit in the form of lower levels of insider dealing, necessitating less enforcement at present. However, it also seems plausible that insider dealing increasingly is taking new forms – for example, trading in instruments other than equities – that would not be captured by the market cleanliness statistics.

• A growing number of cases are being decided under the Revised Penalty Framework. This attempts to make the process of determining fines more systematic. As discussed below, the application of the new framework may have contributed to the recent increase in aggregate fines against firms.

Figure 2. **Aggregate Annual FCA Fine Amounts and Annual Median Fine Amounts against Firms**

- Fines Excluding Top 10 Fines
- Top 10 Fines
- Projected
- Median Fine

<table>
<thead>
<tr>
<th>Financial Year</th>
<th>Aggregate Amount (£ millions)</th>
<th>Median Fine (£ millions)</th>
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<tbody>
<tr>
<td>2002/03 - 2007/08&lt;sup&gt;1&lt;/sup&gt;</td>
<td>0.3</td>
<td>13.0</td>
</tr>
<tr>
<td>2008/09</td>
<td>26.3</td>
<td>0.1</td>
</tr>
<tr>
<td>2009/10</td>
<td>0.8</td>
<td>30.9</td>
</tr>
<tr>
<td>2010/11</td>
<td>90.0</td>
<td>56.6</td>
</tr>
<tr>
<td>2011/12</td>
<td>33.3</td>
<td>0.6</td>
</tr>
<tr>
<td>2012/13</td>
<td>1.4</td>
<td>58.9</td>
</tr>
<tr>
<td>2013/14</td>
<td>2.9</td>
<td>30.0</td>
</tr>
<tr>
<td>2014/15&lt;sup&gt;2&lt;/sup&gt;</td>
<td>422.2</td>
<td>416.9</td>
</tr>
</tbody>
</table>

Notes and Sources:
Dotted portion of bars represents LIBOR fines.
<sup>1</sup> Annual average.
<sup>2</sup> Figures for 2014/15 financial year cover the first half of the year, to 30 September 2014. The projected amount assumes aggregate fines in the second half of the 2014/15 financial year will equal aggregate fines in the first half.
Looking ahead, several emerging issues may affect trends in fines and in enforcement generally:

- Investigations of alleged foreign exchange manipulation could produce fines with magnitudes comparable to or even higher than those observed in relation to alleged manipulation of LIBOR and related benchmarks. It has been estimated that six major banks alone may pay a combined £1.5 billion in fines to the FCA in relation to manipulation of foreign exchange rates.

- The FCA reports that it has postponed certain civil actions against individuals for LIBOR-related conduct as the Serious Fraud Office (SFO) conducts parallel criminal investigations; however, FCA fines against individuals for LIBOR-related violations may be in the pipeline. Indeed, one current investigation for benchmark rate manipulation has the potential to result in the largest ever FCA fine against an individual.⁷

- The FCA’s investigation into interest rate hedging products, in connection with which banks have already paid out nearly £2 billion in redress, may result in fines on banks in future.

- Some observers have speculated that the drop-off in enforcement activity against individuals may be due in part to a diversion of FCA resources into LIBOR and currency manipulation-related cases.⁸ If so, enforcement against individuals might be expected to pick up as LIBOR and foreign exchange cases work their way through the enforcement process. However, this may take several years.

Figure 3. Aggregate Annual FCA Fine Amounts and Annual Median Fine Amounts against Individuals

Notes and Sources:

1 Annual average.

2 Figures for 2014/15 financial year cover the first half of the year, to 30 September 2014. Projected amount assumes aggregate fines in the second half of the 2014/15 financial year will equal aggregate fines in the first half.
- The FCA’s use of attestation requests, which may make it easier to hold a manager liable if the firm’s controls are found deficient, along with related legal changes, may also help reverse the downward trend in fines against individuals.

- The FCA is to be given new powers to bring criminal sanctions over abuse of additional benchmarks, expected late 2014, and the authority to enforce competition law in financial services, as of 1 April 2015, which will increase the range of tools at the authority’s disposal.

- In May 2014, HM Treasury launched a review of the FCA’s enforcement process to evaluate its fairness, transparency, speed, and efficiency. Issues to be addressed include appropriateness of early settlement discounts, the transparency and efficiency of the enforcement process, and how the FCA compares to its counterparts in other countries. A committee plans to submit findings and propose recommendations late in 2014. What conclusions will be reached and what changes will result from the review are unclear, but given its remit to revisit basic aspects of the FCA’s enforcement process, this review has the potential to lead to fundamental changes in how the FCA approaches enforcement.

These and related issues are discussed in more detail in the sections below.

**Background: The Role of Financial Penalties in Enforcement**

According to the FCA, the principal purpose of imposing a financial penalty is: “to promote high standards of regulatory and/or market conduct by deterring persons who have committed breaches from committing further breaches, helping to deter other persons from committing similar breaches, and demonstrating generally the benefits of compliant behaviour.”

Fines are one of a number of enforcement tools at the FCA’s disposal, which include the power to:

- withdraw a firm’s authorisation;
- prohibit an individual from operating in the financial services industry;
- prevent an individual from undertaking specific regulated activities;
- suspend a firm for up to 12 months from undertaking specific regulated activities;
- suspend an individual for up to two years from undertaking specific controlled functions;
- censure firms and individuals through public statements;
- seek injunctions;
- apply to court to freeze assets;
- seek restitution orders;
- prosecute firms and individuals who undertake regulated activities without authorisation; and
- impose financial penalties.

This paper focuses primarily on fines, which consist of any amount ordered to be disgorged plus any penalty. We also examine trends in appeals of fines to the Upper Tribunal and in criminal prosecutions by the FCA. Our analysis of fines is based primarily on the information contained in the final notices published by the FCA upon resolution of civil enforcement actions.
Background: Recent Developments in Enforcement Policy

Our analysis of FCA fines provides a basis for assessing how observed enforcement outcomes measure up to stated policy objectives. To provide context for this assessment we first set out an overview of recent enforcement policy and review several key developments.

Since at least 2008/09, the FSA and FCA have pursued a stated objective of using fines, prohibition, and criminal prosecution to achieve “credible deterrence.” Around that time, Margaret Cole, then Director of Enforcement at the FSA, stated that credible deterrence meant “making people realise that they can suffer meaningful consequences if they break the law and if they don’t improve their standards of behaviour”.

FSA and FCA officials have stated that credible deterrence includes an emphasis on fines against individuals, including senior management. For example, Tracey McDermott, the FCA’s Director of Enforcement and Financial Crime, has said that, “responsibility for the overall culture of firms sits at the top. We need leaders and senior managers within the industry to set the tone for how their staff behave. It is therefore imperative that those individuals are held to account where they share responsibility for conduct failings.”

As at 1 April 2013, the FSA’s responsibilities for enforcement passed to the FCA, while responsibility for prudential regulation (promoting the soundness of financial firms and monitoring systemic risk) transferred to the Prudential Regulatory Authority (PRA) and the Financial Policy Committee of the Bank of England.

The FCA has also been granted certain new powers. These include the ability to ban or restrict, without consultation, sales of financial products that the regulator considers too risky or unsuitable for certain consumers. Moreover, the FCA has the right to ban financial advertising and promotions that lack detailed information and hence might confuse or mislead customers. In theory, these powers should allow the regulator to prevent some misconduct happening in the first place rather than punishing it ex post through enforcement. Clive Adamson, the FCA’s Director of Supervision, predicted shortly before the launch of the FCA that the new regulator would “move away from a primarily reactive style to be a more forward-looking regulator”.

The official remit of the FCA is to protect consumers and ensure that the UK financial services industry remains stable and competitive. According to the regulator, this is to be achieved through the following types of activity:

• regulating the prudential standards of firms that do not fall under the PRA’s supervision;
• protecting customers by closely supervising the activities of the financial services industry and making sure that the firms comply with regulatory standards and relevant laws;
• serving as a “champion” of customers to help ensure that the financial services firms act in customers’ interest;
• promoting effective competition in financial services; and
• enforcing laws and regulations by adhering to the existing policy of credible deterrence.
While the FCA’s stated policy priorities in part drive the focus of its enforcement efforts, in practice the choice of where to deploy enforcement resources is also driven by issues that arise externally and to which the regulator must respond. Below is a discussion of several recent areas of focus, including the alleged rigging of LIBOR and other benchmarks, interest rate swaps mis-selling, manipulation of foreign exchange markets, and moves to restrict promotion or sale of potentially unsuitable financial products.

**Sanctions Relating to Alleged LIBOR Manipulation**

Five banks and two brokerage firms have now been sanctioned in connection with alleged LIBOR manipulation. The FCA’s fines have been imposed in the context of cross-border investigations involving the FCA, US Commodity Futures Trading Commission (CFTC), US Department of Justice (DOJ), the Swiss Financial Markets Authority (FINMA), the Public Prosecution Service of the Netherlands (PPS), and the European Commission (EC). These fines are among the largest the FCA has imposed. However, as is underscored by Figure 4 below, the fines assessed by the FCA are often smaller than those imposed by other regulators, especially ones based in the US. For example, the £160 million fine against UBS AG (UBS) for alleged LIBOR manipulation is the largest ever imposed by the FCA or FSA, but represents less than one-fifth of total LIBOR-related fines against UBS, which total close to £1 billion. In the case of several banks fined by the European Commission in connection with this issue, including Deutsche Bank AG (Deutsche Bank), Société Générale S.A. (Société Générale), JP Morgan Chase & Co (JP Morgan), and Citigroup Inc. (Citigroup), the FCA has not as of yet imposed any fine.

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**Figure 4. Fines Imposed in Connection with the Alleged Manipulation of LIBOR and Other Benchmark Rates (By Regulator)**

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Notes and Sources:
Original fines amounts by regulators outside the UK were converted to GBP using exchange rates obtained from Bloomberg, L.P. as of the fine dates.
While the FCA has filed a series of warning notices against individuals, it has not yet fined any individuals, owing in part to parallel criminal investigations conducted by the SFO, during which FCA civil action has been stayed.\textsuperscript{22}

**Interest Rate Hedging Products**

An investigation of major banks by the FSA in 2012 found widespread mis-selling of interest rate hedging products (IRHPs) to small businesses and other potentially less sophisticated customers. The investigation found “a range of poor sales practices” including poor disclosure of exit costs, failure to ensure that customers properly understood risks, failure to ensure that swaps matched the underlying loans they were intended to hedge, and the presence of incentives for bank employees that may have encouraged mis-selling.\textsuperscript{23}

In June 2012, Barclays plc (Barclays), HSBC Bank plc (HSBC), The Royal Bank of Scotland plc (RBS), and Lloyds Bank plc (Lloyds) agreed to undertake reviews of IRHPs sold since 1 December 2001 and to make redress payments where appropriate.\textsuperscript{24} Shortly thereafter, the FSA announced that a number of smaller banks had also agreed to review their sales of IRHPs.\textsuperscript{25} As at May 2014, those banks had set aside roughly £3.75 billion in provisions for redress payments in connection with the issue,\textsuperscript{26} of which approximately £1.2 billion has been paid out to nearly 8,000 customers.

No fines have yet been imposed by the FCA in connection with interest rate swap mis-selling but the regulator has stated that it will consider imposing fines on banks in connection with the issue after the reviews have been completed.\textsuperscript{27}

**Alleged Foreign Exchange Market Manipulation**

In October 2013, following an informal probe, the FCA opened a formal investigation into alleged manipulation of the $5.3 trillion-a-day foreign exchange (FX) market, joining other regulators worldwide, including the DOJ in the US and FINMA in Switzerland.\textsuperscript{28,29} The FCA is investigating a number of benchmark rates operating in London and is primarily focussing on the World Markets/Reuters rates, which are provided hourly for 160 currencies and twice an hour for the 21 “trade currencies”.\textsuperscript{30,31} The SFO also opened a criminal investigation into the foreign exchange fixing allegations in July 2014.\textsuperscript{32}

As part of the investigation, expected to be completed in 2015, at least 15 banks have been asked to submit information to regulatory agencies.\textsuperscript{33} More than 25 FX traders at major banks have been terminated, suspended, or put on leave.\textsuperscript{34}

Although no fines have yet been imposed, FCA Chief Executive Martin Wheatley has called the allegations “every bit as bad as they have been with LIBOR”,\textsuperscript{35} and some bank executives have expressed concern that the magnitude of fines and litigation resulting from the FX probe will be comparable to that following the LIBOR scandal.\textsuperscript{36} In September 2014, six banks entered settlement talks with the FCA: Barclays, Citigroup, HSBC, JPMorgan, RBS, and UBS are conducting coordinated negotiations with the regulator; it is estimated that these banks may pay a combined £1.5 billion in fines (assuming a 30 per cent settlement discount for early settlement).\textsuperscript{37} According to recent news reports, the FCA’s focus is on fines for Failure to Prevent Misconduct rather than fines that directly sanction manipulation.\textsuperscript{38}
**Product Intervention**

In August 2014, the FCA announced temporary product intervention rules that impose restrictions in relation to the sale of contingent convertible securities (CoCos) to retail investors, pointing to the "complex and highly risky" nature of the products. The FCA’s new product intervention powers, which allow the regulator to temporarily regulate product features, restrict promotional activities, or ban product sales to certain types of customers for up to one year without consultation.

While temporary product intervention, without consultation, represents a new power introduced with the cutover to the FCA, product bans of up to one year were possible under the FSA, though only after consultation. For example, the June 2013 ban on the promotion to retail investors of Unregulated Collective Investment Schemes (UCIS), and close substitutes, was the culmination of a consultation launched by the FSA under its powers.

The FCA’s stated goal is to reduce the need for enforcement activity for mis-selling by pre-empting the sale of unsuitable products to investors. Recently, such fines have actually been rising. In NERA’s classification scheme, fines for mis-selling fall within the Unsuitable Investments & Mis-Selling category. In 2012/13, the regulator issued 10 fines within this category, rising to 15 in 2013/14. Nine fines for Unsuitable Investments & Mis-Selling were imposed in the first half of 2014/15, an annualised rate of 18 per year.

However, considering the lag between misconduct and the imposition of a fine, any decline in fine amounts attributable to the introduction of product intervention will likely be observed only several years in the future.

**NERA’s Analysis of FCA Fines**

NERA maintains a database of FCA enforcement actions involving fines in order to track and analyse trends in such activity. The database includes all enforcement actions that have resulted in fines announced since 1 April 2002.

We have classified each fine according to the principal type of underlying misconduct alleged. Our conduct-based classification system reveals the types of activity sanctioned most frequently and fined most heavily, no matter under which principle or rule sanctions were imposed. This provides an objective and empirical view of the types of conduct subject to FCA enforcement. The number of fines and criminal sanctions allocated to each of our thirteen conduct types, over the past two and a half financial years, is depicted in Figure 5.
Our classification scheme first makes a distinction between cases alleging violations of market integrity – i.e., behaviour that distorts or otherwise negatively affects financial markets – and other types of cases. Our “Market Integrity Violations” category is somewhat more expansive than the concept of “market abuse” specifically authorised under the Financial Services and Markets Act in that it includes cases alleging the failure of firms or individuals to disclose information they were obliged to disclose in accordance with the Listing Rules. Alleged misconduct that does not directly affect securities markets is included in one of three other overarching categories: Customer Protection Failures, Compliance Failures, and Fraud or Other Deliberate Misconduct.

Moreover, NERA classifies LIBOR fines as relating to market manipulation, which falls within the Market Integrity Violations category, based on the specific reference in the allegations to parties’ alleged manipulation with the intent to distort rates for personal benefit.

**Trends in Fines against Firms**

Fines against firms over the past two and a half years have been unprecedented in magnitude. For example, fines for LIBOR manipulation and the fine imposed against JP Morgan for the “London Whale” comprise six of the top 10 largest fines ever imposed against firms. However, as noted above, fines imposed by UK regulators are in some cases exceeded by the size of fines handed out in other jurisdictions.
Number and Mix of Fines against Firms

The number of fines against firms has been fairly stable over the past few years, as has the breakdown by category. There were 26 fines imposed in 2012/13, 27 in 2013/14, and 12 in the first half of 2014/15, on pace for 24 by the end of the financial year (see Figure 6). With regard to the mix of cases by category, the most notable shifts during 2013/14 and 2014/15 have been an increase in the number of fines for Unsuitable Investments & Mis-Selling (part of Customer Protection Failures) and a decline in fines for Compliance Failures. This decline has been driven by a reduction in the number of fines for Transaction Reporting, Record-Keeping, & Pricing Failures.

An exception to this trend is the recent £4.7 million fine imposed against Deutsche Bank on 21 August 2014 for failing to report particular swap transactions correctly. In its final notice for that fine, the FCA emphasised that it relies upon transaction data to monitor insider dealing and other forms of market abuse.

Figure 6. Annual Number of FCA Fines against Firms

![Graph of annual number of FCA fines against firms]

Notes and Sources:
1 Annual average.
2 Figures for 2014/15 financial year cover the first half of the year, to 30 September 2014. Projected amount assumes the number of fines in the second half of the 2014/15 financial year will equal the number of fines in the first half.
A decline in fines for Compliance Failures since 2012/13 has been offset by a recovery in the fines for Customer Protection Failures. After Customer Protection Failures fines fell to 14 in 2012/13, there were 22 such fines in 2013/14 and eight in the first half of the current year. Four of the fines in 2013/14 and one so far in 2014/15 have been for Mistreatment of Customers & Mishandling of Complaints; the largest of these, for £22.9 million, was against State Street Bank Europe Limited and State Street Global Markets International Limited (State Street). State Street was fined relating to allegations that its UK business unit developed and executed a “deliberate and targeted strategy” to charge unwarranted mark-ups on certain transactions, which the FCA found prioritised revenue generation over the interests of customers. The higher level of Customer Protection fines is consistent with the FCA’s stated emphasis on safeguarding the interests of financial consumers.

### Aggregate Fines against Firms

While the number and mix of cases has not changed markedly, the average size and aggregate amount of fines has been substantially larger over the past two and a half years than previously (see Figure 7). This is in substantial part attributable to LIBOR fines. For example, the three LIBOR fines imposed in 2012/13 alone were for a combined £307 million, larger than the combined sum of all fines against firms in all prior years. However, fines against firms would have achieved a new peak even absent those fines.

In 2013/14, aggregate fines against firms were £297.9 million even excluding the two fines in connection with the LIBOR rate-rigging scandal (imposed on Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A. (Rabobank) and ICAP, and totalling £119 million of the £416.9 million total). The “London Whale” fine against JP Morgan contributed an additional £137.6 million. In the first half of 2014/15, fines against firms totalled £219.4 million, and are thus on pace to slightly exceed the record level set in 2012/13.

### Figure 7. Aggregate Annual FCA Fine Amounts against Firms

![Graph showing aggregate annual FCA fine amounts against firms.](image)

Notes and Sources:
1 Annual average.
2 Figures for 2014/15 financial year cover the first half of the year, to 30 September 2014. Projected amount assumes aggregate fines in the second half of the 2014/15 financial year will equal aggregate fines in the first half.
Top 10 Fines against Firms

Consistent with the recent surge in fine amounts against firms, all but one of the top 10 fines against firms has been imposed since 1 April 2012, including all of the top five. Aside from the second largest fine, against JP Morgan relating to the “London Whale” trades, the five LIBOR fines imposed on banks constitute the largest in the regulator’s history (see Table 2). The magnitude of these fines ranges from £59.5 million against Barclays, to three fines in excess of £100 million. As discussed in Section 3.1, the LIBOR fines imposed by the FCA, though large relative to other FCA fines, have often been smaller than LIBOR fines imposed by other regulators, especially in the US.

Table 2. Top 10 Fines against Firms, 2002/03 – 2014/15 (First Half)

<table>
<thead>
<tr>
<th>Fine Rank</th>
<th>Firm</th>
<th>Financial Year</th>
<th>Total Fine (£)</th>
<th>Category of Misconduct</th>
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<tbody>
<tr>
<td>(1)</td>
<td>UBS</td>
<td>2012/13</td>
<td>160,000</td>
<td>Market Manipulation (LIBOR)</td>
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<td>(2)</td>
<td>JP Morgan</td>
<td>2013/14</td>
<td>137,610</td>
<td>Transaction Reporting, Record Keeping, &amp; Pricing Failures</td>
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<tr>
<td>(3)</td>
<td>Rabobank</td>
<td>2013/14</td>
<td>105,000</td>
<td>Market Manipulation (LIBOR)</td>
</tr>
<tr>
<td>(4)</td>
<td>Lloyds and Bank of Scotland</td>
<td>2014/15</td>
<td>105,000</td>
<td>Market Manipulation (LIBOR)</td>
</tr>
<tr>
<td>(5)</td>
<td>RBS</td>
<td>2012/13</td>
<td>87,500</td>
<td>Market Manipulation (LIBOR)</td>
</tr>
<tr>
<td>(6)</td>
<td>Barclays</td>
<td>2012/13</td>
<td>59,500</td>
<td>Market Manipulation (LIBOR)</td>
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<tr>
<td>(7)</td>
<td>Barclays</td>
<td>2014/15</td>
<td>37,745</td>
<td>Mishandling Client Assets</td>
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<td>(8)</td>
<td>JP Morgan</td>
<td>2010/11</td>
<td>33,320</td>
<td>Mishandling Client Assets</td>
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<tr>
<td>(9)</td>
<td>HomeServe</td>
<td>2013/14</td>
<td>30,647</td>
<td>Unsuitable Investments &amp; Mis-Selling</td>
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<td>(10)</td>
<td>Prudential</td>
<td>2012/13</td>
<td>30,000</td>
<td>Miscellaneous Regulatory Failings</td>
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Notes and Sources:
Fine amounts are in thousands of GBP.
Fines labelled “LIBOR” relate to fines in relation to the alleged manipulation of LIBOR and other benchmark rates.

In July 2014, Lloyds and Bank of Scotland plc were fined £105 million for alleged manipulation of both the Repo Rate and LIBOR. In contrast to other entities upon which the FCA has imposed LIBOR fines, Lloyds and Bank of Scotland were alleged to have manipulated rates both before and after the financial crisis. Following the crisis, the manipulation of the Repo Rate and the LIBOR markets is alleged to have been aimed at reducing the fees charged by the Bank of England for participating in the Special Liquidity Scheme, introduced during the financial crisis to improve banks’ liquidity positions.

The most recent fine included in the top 10 list was announced on 23 September 2014: Barclays was fined £37.7 million for mishandling client assets. According to the final notice issued by the FCA, the investment banking division of Barclays failed to adequately organise and protect £16.5 billion of client assets. While the bank notified the authorities of the issue promptly upon its discovery, and no assets were lost, the risk to client assets if the bank were to have become insolvent would have been significant. The FCA noted that the fine was higher than it otherwise would have been due to previous fines imposed on Barclays. This fine is consistent with the FCA’s stated emphasis on consumer protection and is the largest ever for Mishandling Client Assets, eclipsing a £33.3 million fine imposed on JP Morgan in 2010/11 (number eight in Table 2).
HomeServe Membership Limited (HomeServe), an insurance intermediary, was assessed the largest ever fine for Unsuitable Investments & Mis-Selling in February 2014: £30.6 million, for mis-selling insurance policies and failing to adequately investigate complaints. Moreover, the board was deemed to have neglected compliance duties and senior management to have ignored risks to customers. In short, the FCA alleged that HomeServe “incentivised staff to increase the volume of products sold, irrespective of the customer’s need for the product”.

Prudential plc (Prudential), the insurer, was fined £30 million in March 2013 for failing to properly notify the FSA of its intention to bid for AIA Group Limited (AIA), an Asian arm of American International Group, Inc. (AIG). While Prudential ultimately did not purchase AIA, the FSA censured Prudential for not alerting the regulating body of its bidding interest and for not being fully open and cooperative with the FSA throughout the bidding process. The fine, which comprised separate £16 million and £14 million penalties against The Prudential Assurance Company and Prudential plc, respectively, is the largest for compliance-related failings ever imposed by the FCA or FSA.

Impact of the Revised Penalty Framework
The FCA’s Revised Penalty Framework, which applies to fines sanctioning conduct that occurred wholly or mostly subsequent to 6 March 2010, has been used to determine fine amounts in a growing proportion of cases. While less than 10 per cent of fines in 2011/12 were determined under the revised framework, 31 of 49 fines in 2013/14 were computed using the new framework to establish at least part of the fine amount, and 13 of 19 have been in 2014/15. The Revised Penalty Framework determines fine amounts using a five-step process. While the framework is applicable to both individuals and firms, some evidence, discussed below, suggests it may have had a particular effect on recent fines against firms, potentially contributing to the recent increase in the sizes of such fines.

The details differ for firms and individuals (and depending on whether market abuse is alleged), but expressed generically the steps are as follows:

- **Step 1**: the removal of any financial benefit derived directly from the breach;
- **Step 2**: the determination of a figure which reflects the seriousness of the breach;
- **Step 3**: an adjustment made to the Step 2 figure to take account of any aggravating and mitigating circumstances;
- **Step 4**: an upward adjustment that may be made to the amount arrived at after Steps 2 and 3, where appropriate, to ensure that the penalty has an appropriate deterrent effect; and
- **Step 5**: a settlement discount to be applied if applicable. This discount does not apply to disgorgement of any financial benefit derived directly from the breach.

A number of recent fines for conduct that straddled 6 March 2010 have consisted of a component issued under the Revised Penalty Framework and a component under the previous framework. For example, the overall fine of £137.6 million against JP Morgan for risk-management failings relating to the “London Whale” trades included £123.6 million for misconduct after 6 March 2010 (assessed under the new framework), while the remainder, £14 million, corresponded to breaches of principles prior to 6 March 2010 and was computed under the old framework.
Figure 8 shows the aggregate fines issued under the previous regime and under the Revised Penalty Framework, for 2011/12 (the first financial year in which fines were assessed under the new framework), 2012/13, 2013/14, and the first half of 2014/15.

In 2013/14, the fines issued under the Revised Penalty Framework exceeded those under the old framework for the first time, by approximately £100 million. In 2014/15 a greater amount was imposed under the old framework but that is largely driven by the LIBOR fine imposed upon Lloyds and Bank of Scotland.

In Step 3, which reflects aggravating and mitigating factors, the FCA takes into account previous fines or other enforcement actions against the same individual or firm, even if it was for conduct unrelated to the fine at issue. In assessing the September 2014 fine against Barclays (classified under Mishandling Client Assets), for example, the FCA cited a 2011 fine against Barclays Capital Securities Limited for failing to segregate client assets, but also several previous fines against Barclays in respect of different conduct. The FCA discussed a previous fine for transaction reporting and a LIBOR fine, amongst others. After also taking into account mitigating factors, the September 2014 fine against Barclays was increased by 20 per cent in Step 3.
Similarly, in the final notice for a fine imposed against RBS in August 2014, relating to failures in the bank’s mortgage advisory business, the FCA cited previous actions as far back as 2002 as aggravating factors. In Step 3 the fine was increased by 30 per cent (after also accounting for mitigating factors). The previous actions related to alleged breach of anti-money laundering rules, failure to report transactions, and LIBOR manipulation.

Consideration of past fines as an aggregating factor is likely to continue to increase aggregate fine amounts, especially for large, diversified financial institutions, which often have at least one prior enforcement action by the FCA or FSA. Looking ahead to potential fines for alleged FX manipulation, which (based on provisions taken) may be for large amounts and are likely to target at least some major leading financial institutions, the uplift applied in Step 3 may result in these fines being larger still.

**Trends in Fines against Individuals**

Despite the emphasis placed by the FCA on enforcement against individuals, the number and aggregate amount of fines against individuals has been at a low ebb for several years. Since the end of the 2011/12 financial year, fines have been low both for Market Integrity violations – such as Insider Dealing and Market Manipulation – and also in the Compliance Failures category. Compliance-related fines might be expected to have risen, given the FCA’s initiative to hold senior management to account for misconduct within firms, but instead they have fallen. Consistent with the decline in fines against individuals, few fines large enough for inclusion in the top 10 to date were announced over the past two and a half years.

**Number and Mix of Fines against Individuals**

As discussed in Section 3 above, the FCA has emphasised enforcement against individuals as part of its credible deterrence strategy. Nonetheless, the pace of fines against individuals fell substantially in 2012/13, remained low in 2013/14, and has further slowed in the first half of the current financial year. While 48 fines were imposed on individuals in 2010/11 and 40 in 2011/12, just 19 were imposed in 2012/13, 22 in 2013/14, and seven in the first half of 2014/15 (see Figure 9). Fines against individuals are thus on track to total 14 by the end of the financial year, which would be lower than in any year since 2007/08 (which saw four fines against individuals).
Over the four years prior to 2012/13, the FCA fined an average of four individuals per year for Insider Dealing. However, over the past two and a half years (2012/13, 2013/14, and the first half of 2014/15) there have been only two fines imposed in this category (one more would have been fined but for a determination of financial hardship). One of the two was in the high-profile Ian Hannam case, and would have been imposed somewhat earlier had the case not been appealed to the Upper Tribunal.

In 2008, Mr Hannam, who was Chairman of Capital Markets at JP Morgan Cazenove, sent emails to the Minister for Oil in the Kurdish Regional Government, disclosing information about a potential third-party bid for Mr Hannam’s client, Heritage Oil (Heritage), and about developments in Heritage’s oil exploration. According to Mr Hannam, the information was provided to generate interest in an acquisition of Heritage. In February 2012, the FCA decided to impose a fine of £450,000.

Mr Hannam appealed to the Upper Tribunal, arguing that he was merely acting in the interests of his client and that the information was not material. In May 2014, the Upper Tribunal found against Mr Hannam, and in July 2014 the £450,000 fine was reinstated.
The other Insider Dealing fine over this period, of £30,000, was imposed on Jay Alan Rutland in July 2012. Mr Rutland, a broker, was fined for disclosing inside information in order to generate sales by his team. According to the Final Notice in the case, Mr Rutland would have been fined £160,000 but for the financial hardship.

Rahul Shah also would have been fined for providing investment advice based on inside information; however, due to financial hardship the assessed fine of £125,000 was reduced to zero.\(^52\)

In a July 2014 paper,\(^53\) the FCA has provided an update on its “market cleanliness” analysis, which seeks to detect suspicious movements in equity prices shortly before important corporate announcements such as takeover announcements. The FCA finds that the level of such suspicious activity has declined since 2009, around the time that the former FSA began to emphasize its credible deterrence strategy. It is possible that the recent decline in Insider Dealing enforcement is due to a lower level of insider dealing.

However, the FCA study focusses on equities trading surrounding takeover announcements. Increasingly, alleged insider dealing has departed from the type of activity likely to be captured by the market cleanliness statistics, for example dealing in securities other than equities.

The number of fines imposed on individuals for Compliance Failures has also fallen substantially. The FCA imposed an average of eight such fines per year from 2009/10 to 2011/12, but only one individual, Mitsui Sumitomo Insurance Company Ltd.’s executive chairman, Yohichi Kukagai, was fined for Compliance Failures in 2012/13. In 2013/14, two individuals were fined for Failure to Prevent Misconduct and one for Approved Person Regulation Failures. No fines in the Compliance Failures category have been announced this year.

Within Compliance Failures, fines classed as Failure to Prevent Misconduct are particularly likely to capture the FCA’s focus on holding high-profile individuals to account, so it is noteworthy that fines in this category have fallen as well. While fines for Failure to Prevent Misconduct were imposed on nine individuals in eight cases\(^54\) over 2010/11 and 2011/12, only two (in a single case) were fined\(^55\) for Failure to Prevent Misconduct in 2013/14 (see Figure 10).
The reduction in fines against individuals also reflects a slowdown in the pace of mortgage fraud fines, which are included in the Fraud or Other Deliberate Misconduct category. From July 2008 through the financial year 2011/2012, the FCA fined 22 individuals for Mortgage Fraud; however, no such fines were imposed in 2012/13 and only two individuals were fined in 2013/14. There has been one mortgage fraud-related citation in 2014/15, although no fine was imposed due to financial hardship.

**Aggregate Fines against Individuals**

Since their peak in 2011/12, aggregate fine amounts against individuals have fallen even more steeply than the number of fines. In that year, total fines against individuals were nearly £20 million, of which fines for Market Integrity violations comprised £15 million.
In 2012/13, Market Integrity fines amounted to just £2 million of £5 million total, nearly all of which was comprised of the Market Manipulation fines against hedge fund manager Stefan Chaligné (discussed below, in the context of the top 10 fines against individuals) and the salesman with whom he placed orders, Patrick Sejean.

The downward trend in Market Integrity fines continued in 2013/14, as aggregate fines in this category returned to approximately the level of 2009/10, totalling £1.3 million. The figure was primarily accounted for by Market Manipulation fines against two traders: Michael Coscia, who was fined for “layering“, and Mark Stevenson, who engaged in a series of transactions that were alleged to have artificially increased the price of a bond he was attempting to sell. Market Integrity fines are on track to total just over £1 million in 2014/15, which would represent a decline of approximately 93 per cent from the £15 million observed in 2011/12.

Aggregate non-Market Integrity fines have also fallen, from £4.9 million in 2011/12 to £2.6 million in 2013/14 and are on track to slightly exceed £2 million in 2014/15. The drop was primarily driven by the decrease in the number of Compliance Failures and Fraud or Other Deliberate Misconduct cases, discussed above. This reflects a slowdown of fines for mortgage fraud since 2011/12, which are classified in the Fraud or Other Deliberate Misconduct category. Offsetting the decline in non-Market Integrity fines to some degree, the average value of a non-Market Integrity fine continued to rise in 2012/13 and has reached an all-time high to date in 2014/15, approaching £300,000.
Top 10 Fines against Individuals

Unsurprisingly given the peak in fines against individuals observed in 2011/12, four of the five largest fines the FCA has imposed on individuals to date were issued in that year. However, consistent with the subsequent decline in enforcement against individuals, only three top 10 fines against individuals have been issued since (see Table 3).

Table 3. Top 10 Fines against Individuals, 2002/03 – 2014/15 (First Half)

<table>
<thead>
<tr>
<th>Fine Rank</th>
<th>Individual</th>
<th>Financial Year</th>
<th>Penalty (£)</th>
<th>Disgorgement (£)</th>
<th>Total Fine (£)</th>
<th>Category of Misconduct</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Rameshkumar Goenka</td>
<td>2011/12</td>
<td>4,138</td>
<td>1,971</td>
<td>6,109</td>
<td>Market Manipulation</td>
</tr>
<tr>
<td>2</td>
<td>David Einhorn</td>
<td>2011/12</td>
<td>3,000</td>
<td>638</td>
<td>3,638</td>
<td>Insider Dealing</td>
</tr>
<tr>
<td>3</td>
<td>Ravi Sinha</td>
<td>2011/12</td>
<td>1,500</td>
<td>1,367</td>
<td>2,867</td>
<td>Fraud or Other Deliberate Misconduct</td>
</tr>
<tr>
<td>4</td>
<td>Simon Eagle</td>
<td>2010/11</td>
<td>1,500</td>
<td>1,300</td>
<td>2,800</td>
<td>Market Manipulation</td>
</tr>
<tr>
<td>5</td>
<td>Michiel Wieger Visser</td>
<td>2011/12</td>
<td>2,000</td>
<td>0</td>
<td>2,000</td>
<td>Market Manipulation</td>
</tr>
<tr>
<td>6</td>
<td>Stefan Chaligné</td>
<td>2012/13</td>
<td>900</td>
<td>363</td>
<td>1,263</td>
<td>Market Manipulation</td>
</tr>
<tr>
<td>7</td>
<td>Sachin Karpe</td>
<td>2012/13</td>
<td>1,250</td>
<td>0</td>
<td>1,250</td>
<td>Mishandling Client Assets</td>
</tr>
<tr>
<td>8</td>
<td>Samuel Nathan Kahn</td>
<td>2011/12</td>
<td>884</td>
<td>211</td>
<td>1,095</td>
<td>Market Manipulation</td>
</tr>
<tr>
<td>9</td>
<td>Mehmet Sepil</td>
<td>2009/10</td>
<td>700</td>
<td>267</td>
<td>967</td>
<td>Insider Dealing</td>
</tr>
<tr>
<td>10</td>
<td>Gurpreet Singh Chadda</td>
<td>2013/14</td>
<td>250</td>
<td>695</td>
<td>945</td>
<td>Fraud or Other Deliberate Misconduct</td>
</tr>
</tbody>
</table>

Notes and Sources:
Fine amounts are in thousands of GBP.

The sole top 10 fine imposed in 2013/14 was for £945,000, on Gurpreet Singh Chadda, for fraudulent conduct regarding sale-and-rent-back agreements for residential property. The largest fine imposed on an individual in 2012/13 was the approximately £1.3 million sanction against French hedge fund manager Stefan Chaligné. Sachin Karpe received the next-largest fine, and the largest penalty, in 2012/13. He was fined £1.3 million for his actions as a “rogue trader” while working as a UBS desk head from 2006 to 2008. The regulator found that, in addition to making unauthorized transactions, Mr Karpe transferred funds between client accounts in an effort to conceal losses he incurred. UBS also paid $42.4 million (approximately £27 million) in redress to a customer to compensate for losses resulting from Karpe’s actions.

Decomposing the Decline in Fines against Individuals

While fines have declined from 2011/12, that year stands out as having unusually high aggregate fines against individuals. An alternative is to compare the two and a half years since then (from 1 April 2012 to 30 September 2014, encompassing 2012/13, 2013/14, and the first half of 2014/15), to the period of equivalent length immediately preceding it, i.e. the two and a half years from 1 October 2009 to 30 March 2012. This comparison still evidences a decline in aggregate fine amount of approximately two thirds, from £30.5 million in total (an average of £12.1 million per year), to £10.5 million (or £4.2 million per year on average) in the more recent period.
Figure 12, which is expressed in terms of annual averages, seeks to gain insight on this decline by decomposing it into several factors: It shows, first, that a large part of the decline is explained by focusing on the very largest fines – those in the top 10 ever imposed on individuals. Such fines accounted for an annualised average of £7.8 million in the earlier period, falling to an average of just £1.4 million in the most recent two and a half financial years.

Notes and Sources:
1  Annual average.
2  This shows the effect of the decline in the number of non-top 10 fines. It is calculated as the difference between (a) the number of non-top 10 fines over the earlier period and (b) the number of non-top 10 fines over the later period times the average size of non-top 10 fines over the earlier period.
3  This shows the incremental effect of the change in the mix of cases. For each fine type, the number of fines over the later period is multiplied by the average fine size within that fine type over the earlier period. This figure is summed across all fine types and subtracted from item (b) in footnote 2 above.
4  This shows the incremental effect of the change in fine amounts within fine categories. For each fine type, we calculate the change in average fine amount from the earlier period to average fine amount over the later period, and multiply it by number of fines within that fine type over the later period. This figure is summed across all fine types.
5  Annual average.
Excluding these very largest cases still leaves a drop of 35 per cent in more typical fines, from an average of £4.3 million in the earlier period to an average of £2.8 million in the more recent period. That decline can be decomposed into three sources: a change in the number of fines (holding average fine amounts constant), a change in the mix of fine types, and a change in the average fine size within each type.

First, relative to the earlier two and a half years, the number of fines (outside the top 10) fell by just above 50 per cent in the more recent period. Indeed, this more than fully explains the decline. A shift in the mix of fine types, from types of conduct with higher average fines (like Insider Dealing) to types of conduct with a lower average, had a relatively small effect, and was more than offset by an increase in average fine amounts within fine types.

In short, the key factors driving the decline in aggregate fines against individuals between these periods appear to have been (a) a recent decline in very large fines and (b) a decline in the number of more typical (i.e., non-top 10) fines. Changes in the mix of fines have played a small role, and (outside top 10 fines) average fine amounts within fine types have actually grown modestly.

Reason for the Decline in Fines against Individuals, and Outlook for the Future
It is unclear exactly why fines against individuals have declined recently. Below, several explanations are considered, and the outlook for future fines is discussed.

Some commentators have suggested that the large-scale enforcement actions against firms relating to alleged manipulation of LIBOR and other benchmark rates, and, more recently, to alleged FX manipulation, have consumed sufficient FCA time and personnel such that few resources are left to pursue cases against individuals in other areas. Moreover, the SFO has asked the FCA to stay civil action relating to LIBOR against certain individuals while it pursues criminal actions. According to news reports, the SFO has charged 12 individuals relating to LIBOR.

If the FCA has not pursued enforcement against individuals because of constraints on resources from large investigations, then enforcement activity against individuals might be expected to increase once the LIBOR and related cases, as well as FX manipulation cases, work their way through the enforcement pipeline (barring additional large-scale investigations of firms in future). As the FCA’s investigations and enforcement process in respect of FX manipulation are in a relatively early stage, however, it is unclear precisely when this will happen.

Depending on how the SFO’s criminal actions proceed, the FCA may ultimately be free to pursue enforcement actions against certain individuals relating to LIBOR manipulation. Some of these actions may yield large fines, as have the enforcement actions against firms in respect of interest rate benchmarks. Indeed, according to news reports, one current investigation has the potential to result in the largest ever fine against an individual. These news reports indicate that the FCA is currently investigating Christian Bittar, a former Deutsche Bank trader accused of Euribor manipulation, and considering a fine of around £10 million.

In addition, and as discussed above, the FCA’s ongoing FX manipulation probe, now in the early stages, ultimately has the potential to result in fines against individuals.
Certain changes to provisions in the Financial Services (Banking Reform) Act 2013 impose a new “Senior Managers” regime, which requires, amongst other things, that senior managers submit a statement of responsibilities regarding the functions or aspects of a business that the manager oversees. The Act also introduces a criminal offence for mismanagement of an institution that fails.

Other aspects of the legislation appear designed to further enhance the FCA’s ability to hold managers responsible for firm conduct breaches: certification of a regime requiring authorised persons to affirm that employees are suitable to conduct functions that have the potential to cause significant harm; new employee training requirements; and a reverse burden of proof for senior managers, requiring that, should a breach occur, managers must prove that they took reasonable steps to prevent it. The effect of these legal changes remains to be seen, but they may lay the groundwork for an upturn in enforcement against individuals over the next several years.

Thus, while substantial uncertainty remains, one can imagine a scenario in which fines imposed relating to LIBOR and FX manipulation allegations, plus those stemming from Upper Tribunal losses, reverse the present decline in fine activity against individuals, to which the FCA’s additional tools relating to enforcement against senior management may contribute.

While in general it is speculative to forecast fines, two fines against individuals, one quite substantial in size, may be described as reasonably likely to be imposed in the near future. That is because the two individuals in question have recently lost appeals to the Upper Tribunal, but the FCA has not yet issued final notices imposing a fine. These cases are discussed in the next section immediately below.

**Trends in Contested Fines**

The Upper Tribunal handed down four decisions relating to fines in cases with hearings in 2013/14; in all of these, the regulator prevailed. Of the four, three cases involved individuals: the case of Ian Hannam, who lost at the Upper Tribunal in May 2014 and was fined £450,000 in a final notice published July 2014, is discussed above.

The other two are Alberto Micalizzi and Amir Kahn. In Mr Khan’s case, the fine, for mortgage application fraud, is relatively small: £80,000. However, in Mr Micalizzi’s case the Tribunal has directed the FCA to impose a £2.7 million fine for alleged fraud related to the sale of “sham” convertible bonds (a 10 per cent reduction from the £3 million that the FCA intended to impose before Mr Micalizzi’s appeal).

The FCA has yet to issue final notices for either decision, but assuming it issues fines consistent with what the Upper Tribunal has directed, the fine against Mr Micalizzi will be the third largest imposed on an individual.
Most appeals to the Upper Tribunal are by individuals. However, in June 2011, Westwood Independent Financial Planners (Westwood) appealed a £100,000 fine that the FSA sought to impose for failure to ensure suitability and to communicate in a clear manner in selling of geared traded endowment policies. The hearing took place in May 2013 and in November 2013 the Tribunal affirmed the £100,000 penalty on Westwood, which the FCA imposed in a final notice in December 2013.

The four hearings on contested fines in 2013/14, and none to date in 2014/15, represent a decline in the number of fines contested compared to the period 2010/11-2012/13 over which the Upper Tribunal handed down six to seven decisions per year relating to contested fines (see Figure 13, which shows the names of the parties whose appeals succeeded in avoiding a fine). Tribunal hearings have typically lagged the FSA’s decision notices by one or two years, so the increase in contested cases observed in 2010/11 can be seen as aligning with the timing of the FCA’s stated shift in enforcement philosophy, and the decline in the past year and a half may stem from the decline in enforcement against individuals discussed above.

Figure 13. Decisions on Fines by the Upper Tribunal, by Year of Hearing

Notes and Sources:
1 Figure for 2014/15 financial year covers the first half of the year, to 30 September 2014.
Criminal Prosecution and Other Sanctions

NERA also tracks criminal indictments and convictions by the FCA, based upon FCA press releases and other public sources. As Table 4 shows, our review finds 25 arrests in the two and a half years up to 30 September 2014. Ten of these related to Insider Dealing; of these, however, nine related to a single investigation, “Operation Tabernula”, the largest ever Insider Dealing investigation by the FSA or FCA. The first arrests in connection with Operation Tabernula took place in 2010. The one remaining indictment in this period related to Insider Dealing involved Damian Clarke, who, following his arrest in January 2013 was charged with nine counts of Insider Dealing in June 2014. The allegations against Mr Clarke, who was an equity trader at Schroders plc, were related to trading shares and spread bets.

FCA criminal enforcement has also focused on Approved Person Regulation Failures and Land Banking cases: in Table 4, these are included in the “Miscellaneous” category. Of 15 indictments in the past two and a half years in the “Miscellaneous” category, eight relate to “Operation Cotton”, an investigation by the FCA into land banking firms accused of defrauding investors of over £5 million between 2008 and 2011 through sales of what were essentially worthless plots of land.

Table 4. FCA Criminal Indictments, 2002/03 – 2014/15 (First Half)

<table>
<thead>
<tr>
<th>Indictment Year¹</th>
<th>Prior to 2010/11</th>
<th>2010/11</th>
<th>2011/12</th>
<th>2012/13</th>
<th>2013/14</th>
<th>2014/15²</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) (2) (3) (4) (5) (6)</td>
<td>(7)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Indictment of Individuals</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Insider Dealing</td>
<td>12</td>
<td>7</td>
<td>3</td>
<td>6</td>
<td>2</td>
<td>2</td>
<td>32</td>
</tr>
<tr>
<td>Misleading Disclosures</td>
<td>4</td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>4</td>
</tr>
<tr>
<td>Miscellaneous³</td>
<td>0</td>
<td>1</td>
<td>0</td>
<td>3</td>
<td>11</td>
<td>1</td>
<td>16</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>16</td>
<td>8</td>
<td>3</td>
<td>9</td>
<td>13</td>
<td>3</td>
<td>52</td>
</tr>
</tbody>
</table>

Notes and Sources:
Data are from the FCA press release table, supplemented by a review of news articles. The table includes only named defendants.

¹ If indictment date is not reported in the FCA’s press releases, arrest date is used.
² Covers 1 April 2014 to 30 September 2014, the first half of the financial year.
³ Includes mis-selling, stealing, fraud, illegal deposit-taking, and failure to cooperate with the FCA.

The remaining seven indictments in this category are related to unauthorised investment schemes or unauthorised businesses.

The FCA also secured jail sentences in several cases that originated in prior years. Most of the convictions were related to Insider Dealing. For example, in 2012/13 the FCA secured sentences for six individuals as a part of “Operation Saturn”. The Operation Saturn defendants were charged with using price-sensitive information to place spread bets in advance of proposed or planned takeover bids. The FCA investigation lasted for over four years and included extensive use of forensic technology.
The first conviction in connection with Operation Tabernula was of former equities trader Paul Milsom, who in January 2013 was sentenced to two years in prison and was subject to a confiscation order for £245,000. Graeme Shelley, a former trader who pleaded guilty to trading based on tips provided by Mr Milsom, was given a two-year suspended sentence in March 2014.

Table 5. **FCA Criminal Convictions, 2002/03 – 2014/15 (First Half)**

<table>
<thead>
<tr>
<th>Conviction Year¹</th>
<th>2010/11</th>
<th>2011/12</th>
<th>2012/13</th>
<th>2013/14</th>
<th>2014/15²</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prior to 2010/11</td>
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<td>(2)</td>
<td>(3)</td>
<td>(4)</td>
<td>(5)</td>
<td>(6)</td>
</tr>
<tr>
<td>Indictment of Individuals</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Insider Dealing Convictions</td>
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<td>5</td>
<td>1</td>
<td>12</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Other Convictions</td>
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<td>4</td>
<td>1</td>
<td>2</td>
<td>0</td>
</tr>
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<td>Acquittals</td>
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<td>3</td>
<td>0</td>
<td>4</td>
<td>3</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
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<td>8</td>
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<td>17</td>
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Notes and Sources:
Data are from FCA press releases, news articles, and an FCA response to a Freedom of Information Act request (http://www.fca.org.uk/your-fca/documents/foi/foi3347-response).

1. If indictment date is not reported in the FCA’s press releases, arrest date is used.
2. Covers 1 April 2014 to 30 September 2014, the first half of the financial year.

In addition, the FCA sentenced to jail one individual involved in boiler room fraud in 2012/13 and two individuals charged for conducting unauthorised business and unauthorised investment schemes in 2013/14. Among the individuals convicted in 2013/14 was Benjamin Wilson, who was sentenced to seven years in connection with allegedly defrauding investors of over £21 million. Overall, the FCA has now secured 51 convictions, 24 of which relate to Insider Dealing cases.
Conclusion

With more than £400 million in fines imposed by the FCA in both 2012/13 and 2013/14, and £221 million imposed in the first half of 2014/15, the amount collected from firms in fines over the past two and a half years substantially exceeds total fines over the entire prior decade. A number of large fines, particularly related to LIBOR manipulation, account for a significant proportion of these fines. With ongoing investigations into FX manipulation and interest rate hedging products, and the increased use of the Revised Penalty Framework, fines against firms may remain at high levels.

Fines against individuals have declined in recent years, but this may change if and when the FCA begins to impose fines on individuals in respect of LIBOR and FX manipulation, particularly in light of enhanced regulatory and enforcement powers available through the Financial Services (Banking Reform) Act 2013.

Looking further ahead, HM Treasury’s review of the FCA’s enforcement processes has the potential to result in changes to the enforcement process. Finally, with the authority’s new powers to bring criminal sanctions over abuse of additional benchmarks, expected late 2014, and the authority to enforce competition law in financial services, as of 1 April 2015, the tools at the FCA’s disposal will be further enhanced.
Appendix: Classification of Fines by Type of Alleged Misconduct

Market Integrity Violations
Our classification scheme makes a basic distinction between cases alleging violations of market integrity – behaviour that distorts or otherwise negatively affects financial markets – and other types of cases. We classify four types of conduct as relating to market integrity:

• **Insider Dealing**: Unlawful trading based on non-public (inside) information and/or improper dissemination of such information.74

• **Market Manipulation**: Transactions made, orders placed, or other similar actions intended to manipulate the price of a financial instrument or otherwise create a false impression about the market for a financial instrument.75

• **Misleading Disclosures**: Dissemination of misleading information about an investment or issuer, or other actions taken to give a false impression about, and thus distort the market for, an investment.76

• **Failures to Disclose**: Delay or omissions by a publicly traded company in providing the market with information that is required to be disclosed, leading to a distortion in the market for the company’s securities.77

Customer Protection Failures
Fines related to customer protection failures involve the following types of misconduct:

• **Unsuitable Investments & Mis-Selling**: This category includes cases that allege investment advice given to, or investments made on behalf of, a client or clients, which are not suitable to client risk preferences or circumstances (or both). Often these cases involve a failure to obtain “know your customer” information necessary to assess the suitability of investment recommendations or decisions.78 This category also includes improper marketing cases including failure to provide sufficient and non-misleading information in promoting or selling a security,79 and some small capitalisation stock brokerage (“boiler room”) cases.80

• **Mistreatment of Customers & Mishandling of Complaints**: This includes cases where clients were not catered to in a manner deemed fit by the FCA. Common examples include overcharging of customer fees, using high-pressure sales tactics,81 poor treatment of customers facing mortgage arrears, or disadvantaging certain customers in any way.82 Failures to respond appropriately to client complaints are also included in this category.83

• **Mishandling of Client Assets**: This includes failure to segregate client assets from firm assets and other failures to safeguard, or misuse of, money managed on behalf of clients.84
• **Inadequate Security & Safeguards**: These include control failures relating to financial crime prevention – such as failing to screen customers against the Government’s “sanctions list”, failing to report or appropriately monitor suspicious behaviour (such as potential bribery), or allowing third parties inappropriate access to client funds, as well as cases where identity fraud risks were posed due to the granting of access to client funds or confidential information without the adequate verification of the identity of the party seeking such access or information.85

**Compliance Failures**

Fines related to failures in regulatory compliance involve the following types of misconduct:

• **Transaction Reporting, Record-Keeping, & Pricing Failures**: These are cases alleging inadequacies in maintaining accurate records and/or reporting such records in a timely and accurate manner. They often relate to failures to provide accurate and timely transaction reports or to mis-marking of securities.86

• **Approved Person Regulation Failures**: These relate to breaches of the FCA’s Approved Persons regulations, for example allowing an individual to hold a “significant influence function” (SIF) such as director or officer, without obtaining the FCA’s approval, or a failure to notify the FCA of a regulatory investigation in respect of an approved person in the UK.87

• **Failure to Prevent Misconduct**: These relate to cases in which the FCA sanctions managers (e.g., SIF holders) not directly involved in underlying misconduct but in a position to have prevented misconduct committed by others.88

• **Miscellaneous Regulatory Failures**: To date, these cases include fines for lying to the FCA, failing to adequately respond to FCA requests, operating without required FCA authorization, and tampering with documents sent to the FCA.89

**Fraud or Other Deliberate Misconduct**

In recent years these cases have consisted of fraud related to mortgage applications, insurance issuance, and of misleading clients or potential clients regarding status as an approved person.90 This category also includes theft from clients and misappropriation of client assets.
Notes

1 Mr Patton is an Associate Director at NERA. The author would like to thank Vinita Juneja, Erin McHugh, and Chris Brennan for valuable feedback on earlier drafts, and Marcin Pruski, Kaitlin Simpson, Sophia Khuntsaria, Zachary Slabotsky, and William Cole for research assistance.

2 On 1 April 2013, the Financial Services Act 2012 came into force, and the FCA superseded the FSA as financial enforcement regulator. In this paper, unless indicated otherwise, we use “FCA” or “the authority” to refer to the FSA and the FCA collectively.

Throughout this paper, unless otherwise indicated, information relating to fines is taken from NERA’s database of final notices obtained from the FCA (http://www.fca.org.uk/your-fca/list?ttypes=Final+Notice&search=) and the FSA (http://www.fsa.gov.uk/library/communication/notices/final).

3 The FCA’s financial year runs from 1 April through to 31 March, so, for example, the current financial year, 2014/15, began on 1 April 2014 and will end on 31 March 2015.

4 LIBOR stands for the London Interbank Offered Rate and is a series of benchmark rates that banks charge one another for short-term unsecured loans of various maturities. It serves as a reference rate for many financial products and contracts. It is set on a daily basis based on estimated borrowing rates submitted by major banks.

5 Hereinafter, for conciseness, we sometimes refer to alleged manipulation of LIBOR and other benchmark rates as “LIBOR manipulation” and to fines for such conduct as “LIBOR fines”.

6 Two fines imposed on individuals, subsequent to 30 September but shortly before this paper went to press, were considerably below the median for the first half of 2014/15. The FCA issued fines of £14,000 against David Welsby and £10,500 against David Gillespie, both employees of Pritchard Stockbrokers Limited, related to Mishandling of Client Assets.

7 As discussed below, news reports indicate that the FCA is currently investigating Christian Bittar, a former Deutsche Bank trader accused of Euribor manipulation, and considering a fine of around £10 million. See “UK financial watchdog seeks to fine ex-Deutsche Bank trader”, Reuters, 6 June 2014.

Euribor is the European Interbank Offered Rate. It is a series of benchmark rates at which large European banks make short-term unsecured loans in euro to one another. It is set on a daily basis based on estimated borrowing rates submitted by major European banks.

8 See, for example, “Inside-Trading Arrests Vanish as FX, Libor Top FCA Agenda”, Bloomberg, 16 September 2014.

9 Subject to consultation. “UK financial regulators to police 7 more benchmarks”, Financial Times, 25 September 2014.


13 Decision Procedure and Penalties Manual (DEPP), Section 6.1.2G, FCA. According to the FCA, this statement of purpose also applied to a public censure.


15 The FCA also publishes data on other sanctions and disciplinary enforcement activity in its annual report and performance account.


19 “FCA confirms approach to using temporary product intervention rules that will be used by the FCA”, FCA Press Release, 25 March, 2013.


22 “FCA seeks to fine former Deutsche trader”, Financial Times, 6 June 2014.

24 Ibid.

25 These include Allied Irish Bank (UK), Bank of Ireland, Clydesdale and Yorkshire banks, Co-operative Bank, the Irish Bank Resolution Corporation (Anglo Irish Bank), Northern Bank, and Santander UK. See “Interest Rate Hedging Products Pilot Findings”, FSA, March 2013.

26 “Regulator pays only one fifth of swaps mis-selling funds”, Reuters, 8 May 2014.


28 "UK opens formal probe as FX investigation goes global", Reuters, 16 October 2013.


34 "Forex manipulation allegations ‘as bad as Libor’, says FCA", Financial Times, 4 February 2014.


40 The issue must go to the FCA board, which will determine if the proposed measure is appropriate. See “The FCA’s use of temporary product intervention rules”, FSA Policy Statement 13/3, p. 32, March 2013.

41 The ban includes schemes deemed “close substitutes”, giving a category of “Non-Mainstream Pooled Investments”. See “FCA to ban the promotion of UCIS and certain close substitutes to ordinary retail investors”, FCA Press Release, 4 June 2013.


43 NERA’s classification scheme is described in more detail in the appendix to this paper.

44 1 April 2002 is the date from which fines data are published.

45 See the appendix to this paper for NERA’s classification scheme. Our classifications rely on the descriptions in the FCA and FSA fines tables and in Final Notices. In cases involving multiple types of misconduct, the FCA’s characterisation of the principal offense in the case was used to classify the fine, except that cases involving market integrity violations are always classified within the relevant market integrity category.

46 Anjam Ahmad is the only individual who has been subject to both a fine and a criminal indictment. Mr Ahmad was fined for accepting gifts in return for giving preferential treatment to a broker; in our classification this fine is classed as “Fraud or Other Deliberate Misconduct”. The FSA also indicted Mr Ahmad for Insider Dealing, to which he pleaded guilty.

47 The FCA has codified market abuse in the Code of Market Conduct as consisting of insider dealing, market manipulation, and certain misleading disclosures. Failure to disclose, by contrast, is a breach of Listing Rules but not of the Code of Market Conduct, and is therefore not officially classified as market abuse. (See FCA Handbook, Market Conduct and Listing Rules.) Given the equivalent economic effects of misstatements and failures to disclose, in that both distort the market, we treat both as violations of market integrity. We classify cases as violations of market integrity where accounting or other misstatements were made, and the FCA has expressed concern about the effect of the misstatements on the market for publicly traded securities even when the misstatements were not a breach of the Code of Market Conduct (i.e., are not legally considered Market Abuse). As a result, the cases we classify as involving alleged misleading disclosures include three fines over the last three years that the FCA does not classify as involving Market Abuse.

48 A repurchase agreement, or “repo”, is a short-term loan whereby the seller of a security agrees to buy the security back at a specified price and time. The seller pays an interest rate, the repo rate, when buying back the security.

The first penalty computed under the Revised Penalty Framework was imposed on 24 May 2011, against Samuel Kahn for abusive trading activity in connection with a boiler room scheme. “FSA fines individual £1m and secures first final High Court injunction to prevent market abuse”, FSA/PN/044/2011, 24 May 2011. In certain cases, the relevant conduct occurred both before and after 6 March 2010, but because most of the conduct occurred before, the FCA has not calculated the penalty under the new framework.

See the Financial Conduct Authority Handbook.

Mr Shah was prohibited from performing any function in relation to any regulated activities. Because the FCA decided to impose a fine, it is included in the counts of fines presented in this paper. However, because Mr Shah did not ultimately pay any amount, no fine amount is included in the aggregate fine amounts presented.

“Why has the FCAs market cleanliness statistic for takeover announcements decreased since 2009?”, Occasional Paper No. 4, FCA, July 2014.

In some cases, multiple individuals were fined in relation to the same misconduct.

“Layering” involves placing and rapidly cancelling large orders in order to create a false impression of trading volume.

Mr Chaligné was fined for manipulating security prices in an effort to artificially inflate the value of hiron, the Swiss-based hedge fund he managed. According to the final notice, on the last day of consecutive months, Mr Chaligné placed orders with Patrick Sejean, a Cantor Fitzgerald senior salesman, which boosted the monthly closing prices of several securities in which his fund was invested. Mr Chaligné’s fine consisted of a £900,000 punitive element and a £360,000 disgorgement of performance and management fees that resulted from the illicit behaviour. Mr Sejean was also fined £650,000 for his role in the scheme because the FSA determined that he was knowingly involved in the misconduct (the 15th largest fine against an individual to date). The two men contested the decision notices they received in 2010 at the Upper Tribunal. The Tribunal upheld their fines, though it dismissed a related £100,000 fine against a junior trader at Cantor Fitzgerald on the grounds of serious financial hardship.

The original redress amount of $42.4 was converted using the closing exchange rate (exchange rate data obtained from Bloomberg, L.P.) as of the date of the final notice, 25 November 2012.


See, for example, “RBS Libor probe to drag on to next year”, Financial Times, 10 August 2014.

Ibid.

“UK financial watchdog seeks to fine ex-Deutsche Bank trader”, Reuters, 6 June 2014.

Financial Services (Banking Reform) Act 2013.

Financial Services (Banking Reform) Act 2013, p. 32.

Financial Services (Banking Reform) Act 2013, p. 49.

Financial Services (Banking Reform) Act 2013, p. 40.


The Upper Tribunal decision against Mr Khan was handed down on 8 April 2014.

The Upper Tribunal decision against Mr Micalizzi was handed down on 30 July 2014.


Damian Clarke was one of five individuals arrested in January 2013. The case against the others arrested in this matter has been dropped.

The case was temporarily halted in spring 2014 due to cuts in legal aid that left the defendants without proper representation. The case resumed in June 2014. See “FCA land bank battle resumes after legal aid negotiations”, City Wire, 23 June 2014.


These cases typically are described by the FCA as breaching sections 1.3 (“Insider Dealing”), 1.4 (“Improper Disclosure”), and/or 1.5 (“Misuse of Information”) of its Code of Market Conduct (MAR).
Market manipulation cases typically allege breaches of sections 1.6 ("Manipulating Transactions"), 1.7 ("Manipulating Devices"), and/or 1.9 ("Misleading Behaviour & Distortion") of the FCA’s Code of Market Conduct (MAR).

Misleading disclosure cases typically correspond to breaches of section 1.8 ("Dissemination") of the FCA’s Code of Market Conduct (MAR), and often cite breaches of the FSA’s Listing Rules (LR).

These are typically described as breaching the FCA’s “Listing Rules” (LR), but not its Code of Market Conduct (MAR).

These typically allege a breach of Principle 9 ("Customers: relationships of trust") of the FCA’s Principles for Businesses (PRIN).

These typically allege a breach of Principle 7 ("Communications with clients") of the FCA’s Principles for Businesses (PRIN).

In some other cases “boiler room” activities may amount to market abuse.

This category includes the 2008 fine against Square Mile for both using high-pressure sales tactics and providing misleading information to investors.

These cases typically allege breaches of Principles 6 ("Customers' interests") or 8 ("Conflicts of interest") of the FCA’s Principles for Businesses (PRIN).

These typically allege breaches of Principles 6 ("Customers' interests") of the FCA’s Principles for Businesses (PRIN).

These cases typically allege breaches of the FCA’s Client Money Rules or Principle 10 ("Clients’ Assets") of the FCA’s Principles for Business (PRIN).

Cases involving control failures relating to financial crime often cite breaches of Principles 2 ("Skill, care and diligence") and 3 ("Management and control") of the FCA’s Principles for Businesses (PRIN). Cases involving identity fraud risks typically allege breach of the “Money Laundering Rules” (ML), as the potential identity fraud could have been used in money laundering schemes.

These cases typically cite breaches of Principle 2 ("Skill, care and diligence"), Principle 3 ("Management and control") of the FCA’s Principles for Businesses (PRIN), and may also cite breaches of the FCA’s “Statement of Principles for Approved Persons” (APER).

Most recently, these cases cite breaches of Principle 1 ("Integrity") and Principle 11 ("Relations with Regulators") of the FCA’s “Principles for Businesses” (PRIN), and breaches of Principle 6 (skill, care, and diligence) of the FCA’s “Statements of Principles for Approved Persons” (APER).

These cases often cite breaches of Principles 2 ("Skill, care and diligence") and 3 ("Management and control") of the FCA’s Principles for Businesses (PRIN) and often additionally cite breaches of the FCA’s “Statement of Principles for Approved Persons” (APER). These cases include failures to prevent market abuse.

These cases have included breaches of the Listing Rules and the FCA’s “Principles for Businesses” (PRIN), including Principle 2 ("Skill, Care and Diligence"), Principle 3 ("Management and control"), Principle 5 ("Market conduct"), and Principle 7 ("Communications with clients").

These cases typically include breaches of the FCA’s Principles for Businesses and often additionally cite breaches of the FCA’s “Statement of Principles for Approved Persons” (APER).
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