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Global Enforcement Review

EXPLORING THE IMPACT OF REGULATORY ENFORCEMENT ON THE GLOBAL FINANCIAL SERVICES INDUSTRY

2018

About this report

Now in its fifth year, Duff & Phelps' Global Enforcement Review (GER) 2018 provides commentary and insights on global enforcement trends with a focus on the financial services industry. Combining both our regulatory experience with in-depth analysis of enforcement penalties issued by key regulators around the globe, our aim is to assist firms in understanding the key risks to inform strategic, governance, risk and compliance programmes. This year's report also includes contributions from Kroll, the global leader in complex investigation, security and cyber solutions which Duff & Phelps acquired earlier this year. Our combined organisation now has nearly 3,500 employees located in 28 countries around the world, which has extended our market reach, insights and capabilities.

In compiling this research and analysis, we have drawn on Corlytics' extensive RiskFusion Global Enforcement database for the period 1 January 2013 to 30 June 2018. Corlytics is a world leader in determining of regulatory risk impact. The firm prioritises and selects penalties for inclusion in the database based on the following criteria:

- Enforcement penalties from high priority financial services regulators (see Appendix for regulators included).
- Enforcement penalties greater than US$1 million or equivalent across all selected regulators.
- All enforcement penalties (including those below US$1 million) for financial services firms and associated individuals with assets greater than US$25 billion on the date of the enforcement.
- Enforcement penalties cover enforcement actions against both firms and individuals. For individuals, the US$1 million threshold does not apply, rather the scope includes penalties for those selected firms.

Please refer to the Appendix for a list of regulators included in this research, as well as the category descriptions for regulatory control failings.

Author
Julian Korek
Managing Director and Global Head of Compliance and Regulatory Consulting
Duff & Phelps
julian.korek@duffandphelps.com

Executive summary

The huge benchmark manipulation cases of recent years still cast a long shadow on financial services regulators' enforcement activity. A shadow from which some regulators are only now just emerging. However, the signs are that a new regulatory enforcement landscape is coming into view.

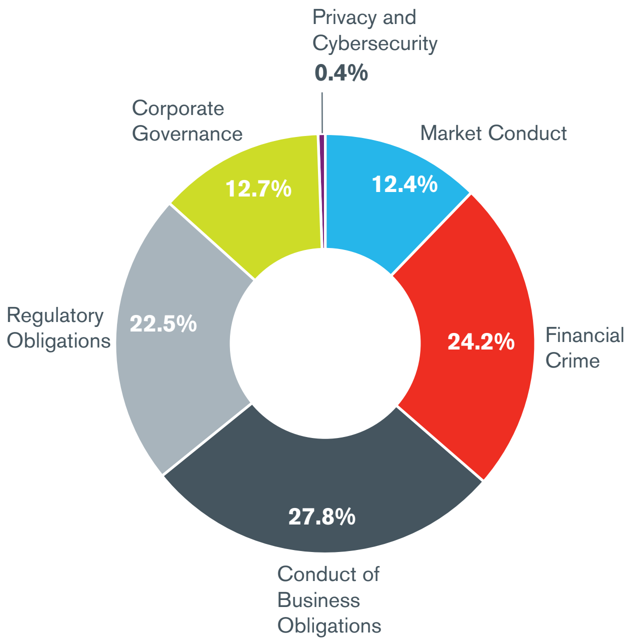
On one hand, many of the regulators' priorities are familiar and well worn. Corporate governance, disclosures to clients and markets, fraud, anti-money laundering (AML), and unlicensed activity remain key areas of focus and activity, with the number of enforcement cases in these areas consistently high across the last five years. On the other hand, a new determination to hold individuals to account and the new challenges presented by technology, are beginning to shape a new enforcement landscape.

Moreover, there has been no obvious dramatic change in enforcement activity when it comes to fines. After the surge in 2013 and 2014 comprising the bulk of the Libor and foreign exchange (FX) abuse cases, fine totals fell sharply. They have since edged up, rising to US$26.5 billion globally last year, from US$20.5 billion in 2015, under what looks like a new normal.

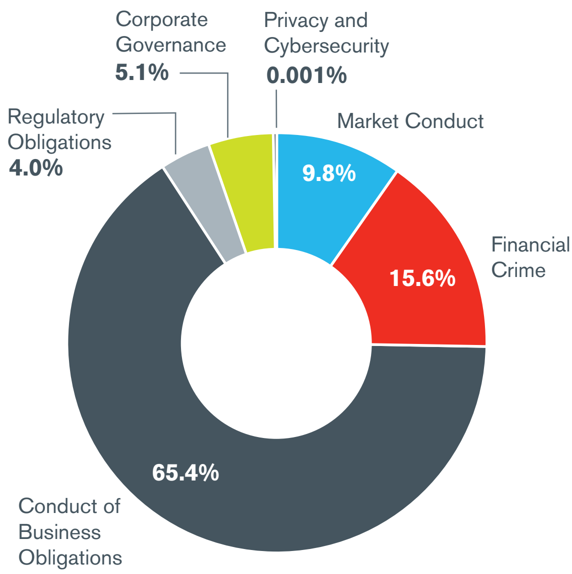
The U.S. regulators continue to account for most of these fines – 95% of the total global sum of fines against firms last year, and 96% of the sum since 2013. These large U.S. fines are also frequently levied against non-U.S. headquartered institutions. The perception that the U.S. is continuing to act as 'Globo-cop' in the industry may not be far wrong.

Look more closely, though, and while some things stay the same, the evolving financial services industry presents challenges in new areas.

FREQUENCY OF PENALTIES GLOBALLY BY REGULATORY CATEGORY 2013-17



GLOBAL FINE AMOUNTS BY REGULATORY CATEGORY 2013-17



NEW PRIORITIES; NEW PLAYERS

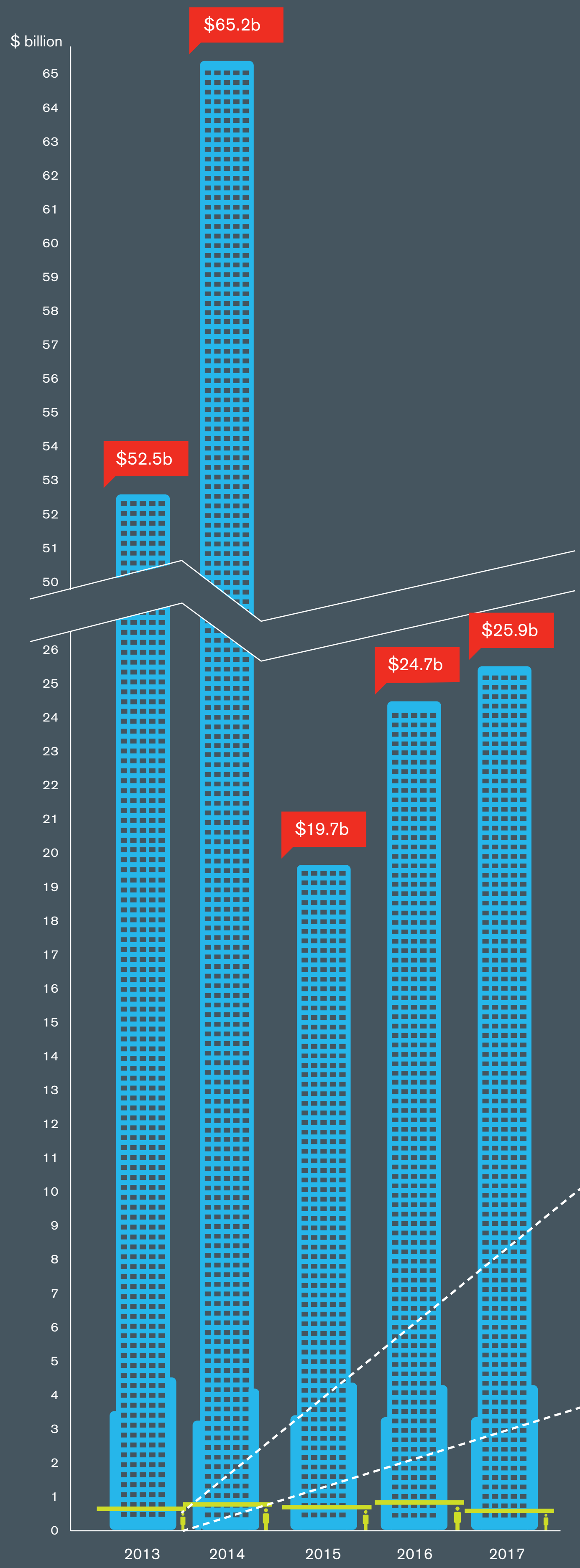
First, some other genuinely new regulatory priorities are emerging. Most obvious, is increasing concern from regulators globally around cybersecurity and data privacy. Firms must now contend with not only supervisory authorities such as the UK's Information Commissioner's Office (ICO), given increased powers through Europe's General Data Protection Regulation (GDPR), but also financial regulators focusing – and fining – on these issues.

Technological developments, such as those around cryptocurrencies (a priority for the U.S. Financial Industry Regulatory Authority (FINRA) and the UK's Financial Conduct Authority (FCA) among others), will also continue to present new challenges.

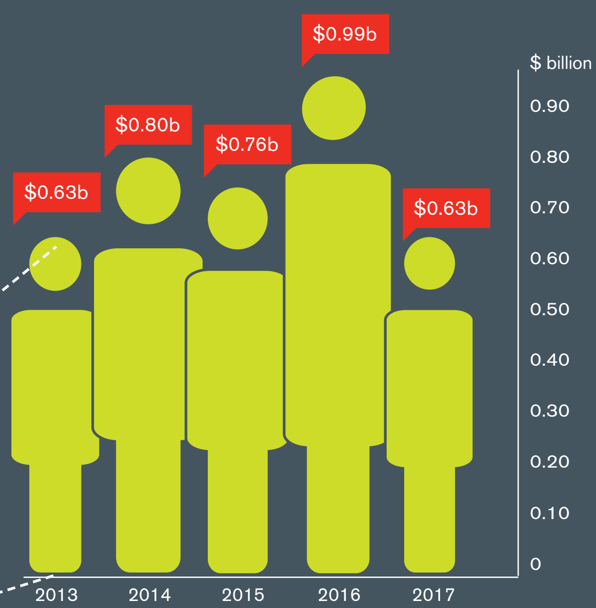
Priority is also being given globally to protecting retirement savings and investments, which will inevitably be an increasing area of enforcement focus for many regulators in the years ahead. Not surprisingly, this is most pronounced in those countries with well-developed private sector pensions such as the UK, U.S. and Australia. The FCA for instance has a goal to protect older savers from ill-advised transfers out of defined benefit pension schemes and other challenges arising from "pensions freedoms" introduced in recent years.

Second, the dominance of the U.S. at the top of the enforcement league table and a focus on fine amounts obscures a more complex picture. Some smaller but still significant activity can easily be missed, which shows the wider adoption of public enforcement action by regulators. We have seen, for example, an uptick in enforcement from certain regulators, like the Central Bank of Ireland and the two French regulators, the AMF and the PSRA, and action from more recent arrivals to the enforcement world, like ESMA.

PENALTY AMOUNT (US$) AGAINST FIRMS GLOBALLY 2013-17



PENALTY AMOUNT (US$) AGAINST INDIVIDUALS GLOBALLY 2013-17



Recent notable action can be lost in the totals, for example:

- The UK's FCA used its powers under Section 384 of the Financial Services and Markets Act for the first time to require Tesco, a listed non-financial services company, to pay compensation to investors for market abuse in relation to a trading update.[1]

- The U.S. Securities and Exchange Commission (SEC) charged businessman Maksim Zaslavskiy and two companies with defrauding investors in relation to initial coin offerings purportedly backed by investments in real estate and diamonds, the first action of its kind by the SEC.[2]

- France's AMF fined Natixis Asset Management €35 million[3] (its largest on record) for breaching its professional obligations in relation to the management of formula funds.

- ESMA's fine of €1.24 million against Moody's Corporation, a credit ratings agency, for[4] two breaches of the Credit Rating Agencies Regulation.

- Hong Kong's Securities and Futures Commission (SFC) in March 2018 intervened to halt an initial coin offering by Black Cell Technology, over concerns that the firm had engaged in unauthorised promotional activities and unlicensed regulated activities.[5]

Finally, penalty amounts only give part of the story. Even in the U.S., the figure is heavily skewed by a few big cases. Whilst, fine amounts tell us a fair amount about the size of organisations involved, and perhaps the gravity of the breaches, but they tell less about the overall level of activity of the regulators when it comes to enforcement.

In fact, the total number of larger fines issued against firms globally tells a different story. It actually rose in 2015 (while fine amounts fell) but has been falling since: between 2015 and 2017, the number of significant fines fell by 30%.

1. https://www.fca.org.uk/news/press-releases/tesco-pay-redress-market-abuse
2. https://www.sec.gov/news/press-release/2017-185-0
3. http://www.amf-france.org/en_US/Actualites/Communiques-de-presse/Comission-des-sanctions?docId=workspace%3A%2F%2FSpacesStore%2F8e8922df-a8c9-4717-9a45-c8a0daf8dd9d
4. https://www.esma.europa.eu/press-news/esma-news/esma-fines-moody%E2%80%99s-%E2%82%AC124-million-credit-ratings-breaches
5. https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=18PR29

Making it personal

The declining number of penalties and fine amounts compared with previous years arguably point to a weakening of regulators' faith in the ability of big fines alone to change behaviour, or at least a recognition of the importance of using other levers.

Those levers include, more creative methods to address failures, notably with an increased emphasis on restitution; and, perhaps more significantly, a focus on individual accountability: In fact, penalties against individuals accounts for almost a third (31%) of the total cases globally between 2013 and 2017. This has been rising steadily year on year apart from a drop of 13% in 2017.

That is only going to grow. At present there is still a relative dearth of large fines against individuals outside the U.S. Of the total US$627.9 million in large penalties imposed against individuals globally last year, US$621.3 million (99%) was by U.S. regulators. But change is coming.

New rules are bedding in with the UK Senior Managers and Certification Regime (SMCR) and Hong Kong's Managers in Charge (MIC) rules. Singapore looks likely to join them with recently proposed Guidelines on Individual Accountability and Conduct from the MAS. Elsewhere, regulators have also been clear that individuals are in the firing line, not just for breaches and abuse, but also for failures for which they may not be directly responsible, but that happen on their watch.

How soon that change is seen in the enforcement figures is uncertain: The regulatory pipeline is long and a change in direction from the regulators is often only felt – or at least becomes apparent in enforcement figures – approximately two or three years on average in most jurisdictions (and in some case more) down the line. But, with massive fines against firms no longer retaining the power to shock, regulators are increasingly looking to alternative, more impactful approaches such as business restrictions, prohibitions and criminal actions against individuals.

For those individuals concerned, it might be that, in the years ahead, 2017-18 comes to be seen as the calm before the storm.

2. Regulatory enforcement priorities

The end of the big benchmark manipulation cases, which were somewhat thrust upon regulators, and the freeing up of enforcement resources has allowed regulators to pursue more of their own priorities (at least until the next unexpected issue arises and demands their attention).

For firms, the good news is that these areas of focus are no secret. The trend is towards transparency, with many regulators now openly publishing their priorities, for instance: The FCA its business plan[6]; SEC[7] and FINRA[8] their examination priorities; the AMF in France its priorities; the Monetary Authority of Singapore (MAS) its regulatory agenda; and the China Banking and Insurance Regulatory Commission (CBIRC) its supervisory and regulatory objectives.

Firms can also look to regulators' reporting of enforcement actions, which indicate the extent and focus of their activity and sends strong messages to the market and consumers. What we see in this year's Global Enforcement Review research is that the same areas of focus keep recurring: corporate governance, disclosure to clients and fraud have all been top areas of enforcement activity in each of the last five years.

Unlicensed activity, too, remains a key source of cases. In addition to fraud, financial crime related activities such as AML, bribery and customer due diligence are areas with significant enforcement activity across most jurisdictions in recent years.

A mix of old and new

Looking at regulators' published priorities, meanwhile, we see these old favourites joined by new areas such as cybersecurity (FCA, SEC and MAS) and risks around crypto currencies (FINRA, MAS, FCA).

Unsurprisingly, the protection of retirement savings is most pronounced in those countries with significant and well-developed private sector pensions, and it is an explicitly stated priority for the SEC and the FCA. The UK regulator in particular has had a task in protecting older savers from ill-advised transfers out of defined benefit pension schemes and other challenges relating to "pensions freedoms" introduced in recent years.

Nevertheless, aging populations and an increasing emphasis on private provision for financing retirement are global trends. Retirement savings and investment are therefore likely to be an increasing area of focus for many financial regulators in the years ahead.

Individual accountability

As important as what the regulators focus on is how they do so, and it is clear that the emphasis is now on holding individuals to account.

Again, the number of enforcement cases provides only part of the story. Within the scope of this research, the number of enforcement actions against individuals globally increased by 7% from 2015 to 2016, only to decline slightly by 13% last year.

However, in their public pronouncements regulators are clear that they intend to hold individuals responsible wherever possible. And they have not only the intention, but the tools to do so: The SMCR in the UK, the MIC initiative from Hong Kong's SFC and, most recently, the proposed Guidelines on Individual Accountability and Conduct from Singapore's MAS are all making it easier for regulators to identify and take action against individuals responsible for regulatory breaches.

The regulatory framework increasingly presumes responsibility where failures occur on an individual's watch. As the new regimes bed in, this is likely to be reflected by an increase in the number of cases against individuals in the future.

Beware black swans

Finally, however, it is worth remembering that regulators are only partly masters of their own destiny. Just as discovery of Libor and FX benchmark manipulation absorbed significant regulatory resources in recent years, unexpected issues demanding their attention could well disrupt regulators' plans.

It is difficult to say what these may be, but it would not be surprising if they involved fast changing technology. The increasing emphasis given to cybersecurity is already as much necessity as choice; already the impact on savers and investors has made it clear financial regulators cannot ignore the issue. We are likely to see increasing action for failures in both protecting confidential information and in ensuring resilience of financial services.

New risks continue to emerge, though, and precise priorities around developments such as big data and crypto currencies remain somewhat vague. While regulators are still monitoring and assessing the impact and risks around these technologies, there is little focus on future risks with new developments regularly occurring. As always, regulators in these emerging areas, like generals, are destined to fight the last war, not the coming one. There is also a significant focus on protecting retirement savings.

6. https://www.fca.org.uk/publication/business-plans/business-plan-2018-19.pdf
7. http://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2018.pdf
8. http://www.finra.org/industry/2018-regulatory-and-examination-priorities-letter

Author
Nick Bayley
Managing Director, Duff & Phelps
nick.bayley@duffandphelps.com

Making good: New thinking on compensation for public market investors

Regulators are finding new ways to compensate those who lose out as a result of firms' failures, and it could have significant consequences for the costs of regulatory breaches.

Who pays the price? Regulators and policy makers have long contended with the question of whether enforcement fines are truly effective – if financial penalties really work. In jurisdictions such as the UK, despite the drive for individual accountability, fines against individuals remain relatively small. Those imposed on firms, meanwhile, are ultimately borne by their shareholders and the public, rarely by those actually responsible.

This year's Global Enforcement Review shows that in the market conduct arena, the massive fines associated with abuses of Libor and FX benchmarks are now largely behind us. Whether those cases have really changed behaviours – and cultures within those firms – remains an open question, however. In this light, the concept of genuine restitution to those who lost out is attractive: If regulators can't be confident they're really punishing the guilty parties, they can at least stop them benefiting and try to put things right for those who have lost out.

The idea is certainly not a new one. In the UK, disgorgement is one of the three principles underpinning the FCA's penalty regime (along with discipline and deterrence)[9] and disgorgement and restitution are significant elements of many of the sanctions imposed by the SEC, FINRA and CFTC in the U.S.[10] Interestingly, in SEC and FINRA cases firms actually paid out more in restitution and disgorgements in 2017 than they did in fines.

If the use of the restitution remedy is unusual in public market cases it is perhaps because of the difficulties determining exactly who has lost out and by how much as a result of the misconduct. In cases of mis-selling where investors have been matched with inappropriate financial products, it is often straight-forward to calculate their losses, and regulators frequently use this as a starting point for penalties. In other cases, such as misleading statements or market manipulation, the losses are often not so clear-cut.

Every little helps

Which is why the FCA decision against Tesco in March 2017 could prove significant. The FCA took action against the supermarket giant over its overstatement of profits in 2014.[11] For the first time the regulator used its powers under the Financial Services and Markets Act to require a listed company to pay compensation for market abuse to those affected: about 10,000 retail and institutional investors who purchased Tesco shares or bonds and held them during the period between the erroneous trading update and its correction about six weeks later. The compensation, totalling about £85 million, was calculated to reimburse these buying investors for the inflated price they paid as a result of Tesco's misstatement.

The FCA's thinking on penalties for misconduct by listed companies has evolved over the years and changed notably with its action against oil rig services company Lamprell in 2013.[12] In that case, when it penalised the company for listing rules breaches, rather than calculate the penalty according to relevant revenue as in the past, the FCA used market capitalisation as a better reflection of the impact and importance of the firm to the public market.

The Tesco case takes this much further. Importantly, it demonstrates the willingness of the regulator to think creatively about compensation and act to remedy actual losses for public market investors even where they may be difficult to quantify.

Compensating a large number of investors for manipulation of LIBOR and EURIBOR was impractical. What this may mean for the financial costs of a breach in the future will depend on the particulars of the cases in question and the methodology the regulator decides to employ. The focus, however, may increasingly be where it should be: on making investors whole again.

9. https://www.handbook.fca.org.uk/handbook/DEPP/6/5.html
10. https://www.finra.org/newsroom/statistics#key, https://www.cftc.gov/PressRoom/PressReleases/pr7650-17 and https://www.sec.gov/files/enforcement-annual-report-2017.pdf
11. https://www.fca.org.uk/news/press-releases/tesco-pay-redress-market-abuse
12. https://www.fca.org.uk/news/press-releases/lamprell-plc-fined-%C2%A32428300-systems-and-controls-failings

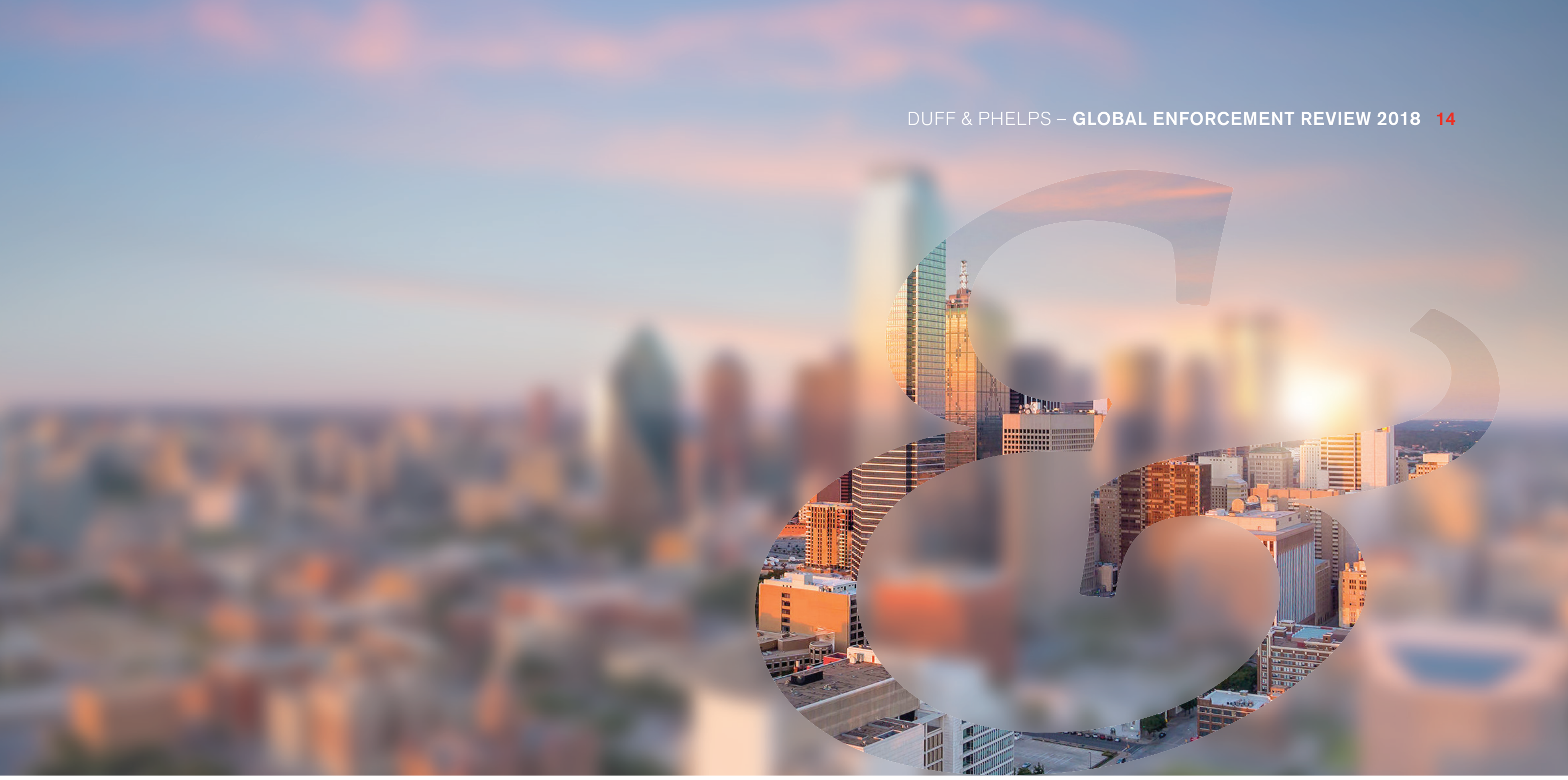
Author
Ken C. Joseph[13]
Managing Director, Duff & Phelps
ken.joseph@duffandphelps.com

Heightened examination and enforcement capabilities in the U.S.

Some industry pundits have pointed to objective year-to-date statistics on the number of white collar prosecutions, securities enforcement actions and related financial penalties as evidence of a deregulatory turn in the U.S. financial markets. Yet all is not what it seems.

Studies have shown that white collar prosecutions in the U.S. are projected to fall to their lowest level in 20 years.[14] This trend appears evident in the U.S. regulatory enforcement statistics as well:

- In FY 2017, the U.S. Securities and Exchange Commission (SEC) reported that it brought 754 enforcement actions, down approximately 13% from FY 2016. It also obtained judgments and orders totalling more than US$3.7 billion in disgorgement and penalties, a decline of approximately 7% from the previous year.[15]
- The Financial Industry Regulatory Authority (FINRA) has also reported declines with 1,369 new disciplinary actions filed in FY 2017, down from 1,434 in 2016, and fines of US$64.9 million in FY 2017, compared to US$173.8 million the previous year.[16]



SEC ENFORCEMENT RESULTS: FISCAL YEARS 2014 – 2017[17]

Fiscal Year	2014	2015	2016	2017
Standalone Enforcement Actions	413	507	548	446
Follow-On Administrative Proceedings	232	168	195	196
Delinquent Filings	110	132	125	112
Total Actions	755	807	868	754
Disgorgement and Penalties Ordered (US$)	$4.16b	$4.19b	$4.08b	$3.79b

While there is an evident downtrend in enforcement actions and related penalties, U.S. market participants may unduly be taking comfort and significantly misjudging the risks and costs of landing in the regulatory cross-hairs. There are two innovations employed by the U.S. regulators that either have, or will, sharpen and maintain the regulators' ability to identify and target actual or potential violations of the U.S. federal securities laws and related rules: Over approximately the past five years, the SEC has increased its reliance on both human sources and data analytics. This has been to inform its decisions on whether to allocate resources to examinations and investigations, to identify emerging risks, to scope areas for review, and to risk-rate or profile persons or entities who may be involved in misconduct.

Human Sources

Whistleblowers, incentivised in part by multimillion-dollar bounties for supplying data that help the SEC uncover and stop securities law violations, continue to flood the agency with valuable information. In its FY 2017, the SEC received 4,484 tips from whistleblowers — almost 33% more than it received five years earlier.[18] This figure does not include the thousands more in tips, complaints, or referrals the agency

13. The writer acknowledges the contributions of Gary Napadov and Basyah Klyman from Duff & Phelps
14. Trac.syr.edu. (2018). "White Collar Prosecutions Fall to Lowest in 20 Years." [online] Report date: 24 May 2018 (http://trac.syr.edu/tracreports/crim/514/?et=editorial&bu=National%20Law%20Journal&cn=20180530&src=EMC-Email&pt=Compliance%20Hot%20Spots)
15. SEC Division of Enforcement FY 2017 Annual Report (https://www.sec.gov/files/enforcement-annual-report-2017.pdf)
16. FINRA Statistics: Regulatory Actions and Corporate Financing Review 2013 – 2017 (https://www.finra.org/newsroom/statistics)
17. SEC Division of Enforcement FY 2017 Annual Report (https://www.sec.gov/files/enforcement-annual-report-2017.pdf); SEC Summary of Performance and Financial Information FY 2016 (https://www.sec.gov/files/2017-03/sec-summary-of-performance-and-financial-info-fy2016.pdf); SEC Press Release: SEC Announces Enforcement Results for FY 2016 (https://www.sec.gov/news/pressrelease/2016-212.html)
18. 2017 Annual Report to Congress: Whistleblower Program (https://www.sec.gov/files/sec-2017-annual-report-whistleblower-program.pdf)

received from federal and state law enforcement partners, SROs, and other market participants.

The quality and value of whistleblower information is evidenced by the fact that since approximately 2012, the SEC has imposed almost US$1.5 billion in monetary sanctions on alleged violators that could be traced, at least in part, to information provided by whistleblowers.[19] During the same timeframe, 53 whistleblowers collected more than US$262 million in bounty payments, including awards to three whistleblowers in early 2018 totalling US$83 million.[20]

In addition, the SEC's examination and investigative strategy and tactics are increasingly shaped by onboard industry experts, and by highly-trained legal, accounting, finance, and other professionals who now routinely collaborate across traditional organizational silos. In its FY 2017 Congressional Budget Justification, the SEC discussed the enhancements to its National Examination Program (NEP) and specifically highlighted the "internal collaboration [and recruitment of] more staff with specialized expertise and experience."[21] Similarly, the agency's Market Abuse Unit's Analysis and Detection Center within the Division of Enforcement utilised industry specialists with unique analytical, statistical, programming, or investigative skills.[22]

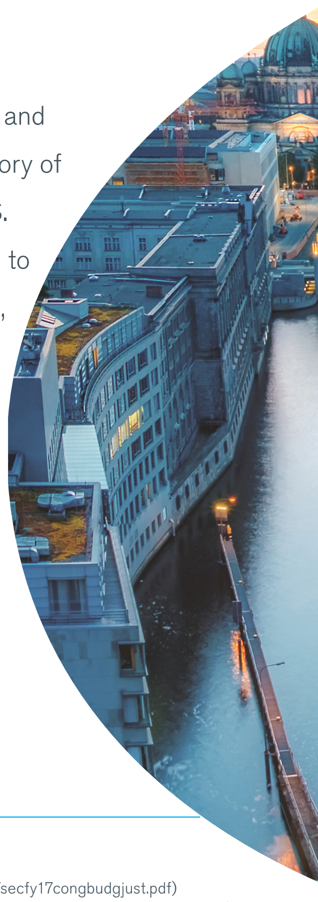
Big data and predictive analytics

The SEC has also made great strides in the adoption of sophisticated 'big data' analytical tools and techniques, coupled with predictive analytics and forms of machine learning to significantly increase its ability to detect and deter potential misconduct. The agency's commitment to compiling and mining the vast amount of public and confidential-filed data at its disposal has significantly increased the likelihood of a 'positive' outcome for the agency. For example, the agency's deployment of the National Exam Analytics Tool (NEAT) and the Advanced Relational Trading Enforcement Metrics Investigation System (ARTEMIS) has given the agency unprecedented ability to identify actual or potential violations relating to insider trading, market manipulation, illegal short sales, unauthorised transactions, inflated valuation, and misrepresentation of performance, to name a few.

In the same vein, the agency's Division of Economic and Risk Analysis (DERA), in conjunction with seasoned examiners and investigators, has developed and deployed sophisticated algorithms and machine learning tools to detect patterns and anomalies that bear the badges of fraudulent conduct. Not to be outdone, FINRA launched its Cross-Market Auction Ramping surveillance pattern whilst also noting that it is "working on incorporating machine learning techniques to aid in further detection of manipulative layering activity."[23]

The outlook

The declining amounts of monetary fines and enforcement actions do not tell the full story of the risk of detection and prosecution. U.S. regulators have innovated and responded to the realities imposed by strained budgets, dwindling resources, and an increasingly sophisticated marketplace. As such, U.S. market participants who fail to conduct their business in a legally compliant manner run the risk of exposure to the regulatory hammer.



19. SEC Press Release "SEC Awards Whistleblower More Than $2.1 Million." 12 April 2018 (https://www.sec.gov/news/press-release/2018-64)
20. SEC Press Release "SEC Announces Its Largest-Ever Whistleblower Awards." 19 March 2018 (https://www.sec.gov/news/press-release/2018-44)
21. SEC FY 2017 Congressional Budget Justification, FY 2017 Annual Performance Plan, and FY 2015 Annual Performance Report (https://www.sec.gov/about/reports/secfy17congbudgjust.pdf)
22. Ehret, Todd. "SEC's Advanced Data Analytics Helps Detect Even the Smallest Illicit Market Activity." Reuters. 30 June 2017 (https://www.reuters.com/article/bc-finreg-data-analytics-idUSKBN19L28C)
23. FINRA 2018 Annual Regulatory and Examination Priorities Letter (http://www.finra.org/industry/2018-regulatory-and-examination-priorities-letter)

Author
John Byrne
Chief Executive Officer, Corlytics
john.byrne@corlytics.com

Knowing the Rules

Data analytics could be the key to making sense of principles-based regulations.

Principles-based regulation was introduced in 1990 by the Financial Services Authority, the UK's financial services regulator at the time (since superseded by the FCA and PRA). The approach has since found widespread support among regulators elsewhere, adopted to varying degrees by those from the Hong Kong's SFC to France's AMF.

Even the U.S., home of rules-based regulation, is not immune. Many of the legislative rules in the country are, in practice, applied in a principles-based manner by the SEC and CFTC. Hence, instruments that act like derivatives or securities are regulated as such. (As they are with other regulators around the world as well.)

There are obvious benefits to the approach of preferring broadly stated principles to prescriptive, technical rules. It leaves less scope for legal loopholes to be exploited by the unscrupulous. It also provides greater flexibility to adapt to developments in the market such as new financial instruments, without the need for fresh regulation.

But it comes at a cost of clarity. As regulators move away from detailed rules to broad principles, the exact requirements become more difficult to determine. They can only truly be understood by examining the outcomes; and it is no coincidence that regulators such as the FCA and SFC also talk about an "outcomes-based" approach.[24]

Walking the walk

Examining outcomes means looking at the enforcement action taken and the regulatory impact. Financial penalties and other sanctions provide proof of regulatory priorities. Furthermore, regulators applying broadly drafted rules are often extremely detailed in the enforcement notices issued. They frequently specify their precise expectations for the controls, procedures and governance they want firms to put in place.

Modern analytical tools can help make sense of this data. They employ quantitative analysis to clarify enforcement priorities and the potential costs of non-compliance. Not just penalties, disgorgements and restitution levels, but investigation costs, too, which can be enormous. Textual analytics and natural language processing can then sift through enforcement notices to identify the actual requirements that are left unstated in the rules – how the regulator wants to see the principles applied in practice.

This analysis offers some comfort to firms. Back testing shows that most regulators are consistent in their approach. That makes such analytics and machine learning Artificial Intelligence a powerful suite of tools to manage current regulatory risks.

But it also has predictive power. We can also access future intent, by combing regulator business plans, speeches, regulatory notices and dear CEO letters. Similar analysis of regulatory notices and announcements shows the impact different types of output have on the regulatory risk. This shows that speeches have a very high impact. For example, if the head of enforcement or supervision highlights an issue in a speech, enforcement action usually follows in time.

Used intelligently, therefore, technology can help us not only clarify what regulators are looking for today, but to stay one step ahead of their demands for tomorrow. For this, however, we need to take them at their word.

24. https://www.fca.org.uk/business-plan-2016-17/1-our-role and http://www.sfc.hk/web/EN/regulatory-functions/intermediaries/supervision/supervisory-approach.html

3.

Jurisdictional enforcement trends

Any discussion of the regulatory landscape across the globe is complicated by the dominance of U.S. regulators in the statistics. Of the enforcement actions included in-scope of this research, the U.S. had accounted for 95% of the penalty amounts against firms and 80% against individuals. Equally, the U.S. dominated the number of penalties issued globally, with 73% against firms and 72% against individuals. Consequently, activity in the U.S. drives the global trends observed and can obscure less obvious changes taking place elsewhere.

One significant impact of this is that a slowdown in the activity of the U.S. regulators last year compared to 2016 and 2015 looks like a global trend. The number of U.S. penalties issued against both firms and individuals combined has fallen on average by 34% since 2015.

In some jurisdictions, that is a fair reflection of the reality. Notably, the UK – where the FCA is one of the most active of the regulators outside the U.S. – has seen the number of fines issued last year drop significantly from 2016. In fact, that number has fallen every year since 2013, although fine amounts have fluctuated, influenced heavily by the very large penalties imposed because of the benchmark manipulation cases. Market manipulation action also disappeared from the UK figures after 2015, with the largest FCA fine in 2017 imposed for AML failings.[25]

New players

However, looking across other jurisdictions tells a different story. In the rest of Europe, for instance, enforcement action has actually increased, particularly against individuals. In 2015 in Europe, there were two significant cases against individuals involving a fine; in 2017 there were 14.

Activity in Europe is bolstered by more active enforcement from regulators such as the Irish Central Bank and French AMF – particularly against asset managers in the case of the latter, including a €35 million fine, the largest on record.[26] It is also boosted by new entrants to enforcement, including ESMA, with action against a credit ratings agency;[27] and more cases from the EU Commission against big banks for operating a cartel with respect to euro interest rate derivatives.[28]

In Asia Pacific, meanwhile, regulators have largely maintained the pressure, including in Australia, where the Federal Court handed out the highest ever civil penalty in the country's corporate history last year.[29] Hong Kong is also busier than ever, with more enforcement outcomes there in 2017 than the UK.

One constant across regulators globally, however, is a relative dearth of large fines against individuals, where almost all the big cases come from the U.S. With an increased emphasis on individuals and new regulatory frameworks in jurisdictions such as the UK and Hong Kong, it will be interesting to see how this changes in the years ahead.

Luck or judgement?

While the level of activity varies, there's significant consistency in the area attracting the greatest number of fines. In the U.S., UK, Europe and Asia Pacific – as well as Canada, Australia and Hong Kong – corporate governance, and specifically, firm management is the issue to most frequently attract regulatory action.

Singapore is the exception, where it was financial crime, specifically AML and due diligence, that was the most active area. In fact AML and due diligence were both common priorities and top areas of enforcement activity across Europe, Hong Kong and Asia Pacific as a whole, as was disclosure to clients across the U.S., Australia and Asia Pacific. Outside of these traditional enforcement areas, however, there is less of a pattern: The wide variety ranges from frequent activity around market manipulation and regulatory reporting in Europe, to a focus on client order execution in Asia Pacific, particularly in Australia.

As ever, this variety reflects both genuinely different regulatory priorities and happenstance. Particularly for smaller regulators with fewer resources, issues that arise can quickly come to dominate the enforcement agenda; we are seeing that with the 1MDB scandal in Singapore, for instance.

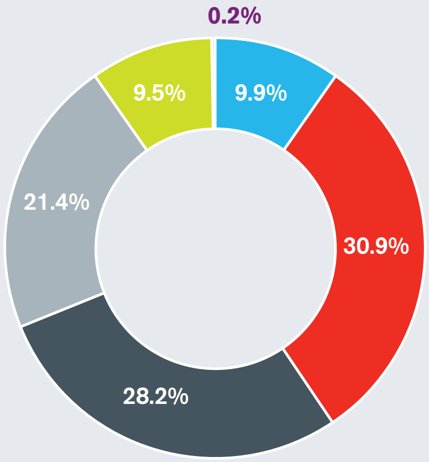
What is true across the globe, however, is that those jurisdictions that aspire to be key international financial centres must be able to demonstrate they have a credible enforcement regime. Notable in recent years, is the increased enforcement activity in emerging centres regulators with fewer resources, headline-grabbing issues that they seize upon can quickly come to dominate such as China,[30] as well as an uptick in enforcement activity in certain European countries outside the UK.

25. https://www.fca.org.uk/news/press-releases/fca-fines-deutsche-bank-163-million-anti-money-laundering-controls-failure
26. http://www.amf-france.org/en_US/Actualites/Communiques-de-presse/Comission-des-sanctions?docId=workspace%3A%2F%2FSpacesStore%2F8e8922df-a8c9-4717-9a45-c8a0daf8dd9d
27. https://www.esma.europa.eu/press-news/esma-news/esma-fines-moody%E2%80%99s-%E2%82%AC124-million-credit-ratings-breaches
28. http://europa.eu/rapid/press-release_IP-16-4304_en.htm
29. http://www.austrac.gov.au/media/media-releases/record-45-million-civil-penalty-ordered-against-tabcorp
30. Statistics on China are not included in this report

FREQUENCY OF PENALTIES GLOBALLY BY REGULATORY CATEGORY 2013-17

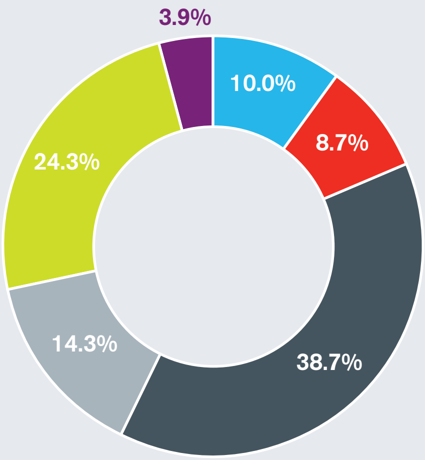
Market Conduct
Financial Crime
Conduct of Business Obligations
Regulatory Obligations
Corporate Governance
Privacy and Cybersecurity

US



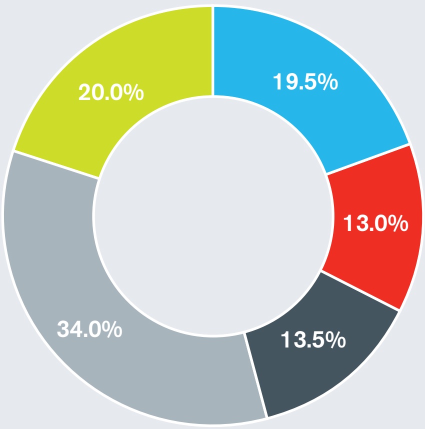
For the period of 2013-2017, the top five areas for the number of penalties by regulatory category failings regulatory in U.S. enforcement actions in scope of this research are: disclosures to clients (Conduct of Business); fraud (Financial Crime); firm management (Corporate Governance) particularly in relation to systems and controls, risk management and compliance; unlicensed activity (Regulatory Obligations); and regulatory reporting (Regulatory Obligations).

UK



For the period of 2013-2017, the top five areas for the number of penalties by regulatory category in UK enforcement actions in scope of this research are: firm management (Corporate Governance) particularly in relation to oversight, systems and controls and risk management; disclosures to clients (Conduct of Business Obligations); miss-selling and suitability (Conduct of Business Obligations); market manipulation (Market Conduct); and conflicts of interest (Conduct of Business Obligations).

EUROPE (EX.UK)

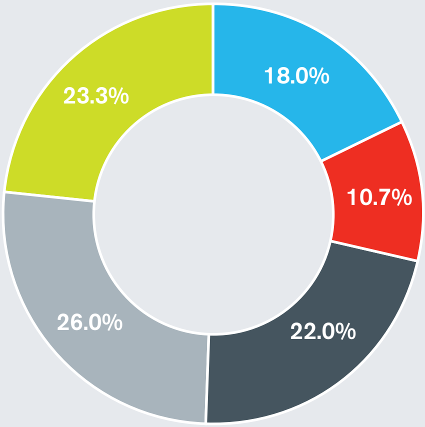


For the period of 2013-2017, the top five areas for the number of penalties by regulatory category in European enforcement actions in scope of this research are: firm management (Corporate Governance) particularly in relation to systems and controls, risk management and compliance; regulatory reporting (Regulatory Obligations); AML (Financial Crime); anti-competitive behaviour (Market Conduct); and disclosures to clients (Conduct of Business Obligations).

FREQUENCY OF PENALTIES GLOBALLY BY REGULATORY CATEGORY 2013-17

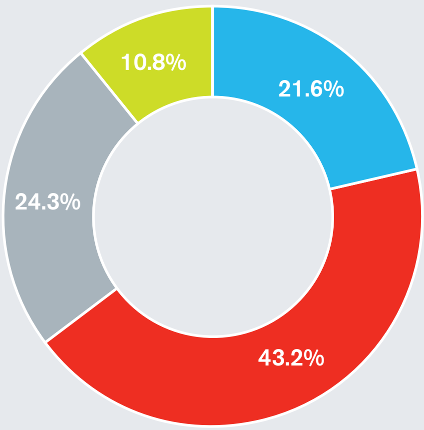
Market Conduct
Financial Crime
Conduct of Business Obligations
Regulatory Obligations
Corporate Governance
Privacy and Cybersecurity

HONG KONG



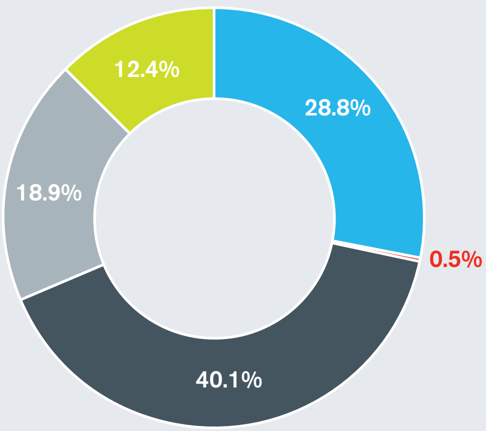
For the period of 2013-2017, the top five areas for the number of penalties by regulatory category in Hong Kong's enforcement actions in scope of this research are: firm management (Corporate Governance) particularly in relation to systems and controls, oversight, and supervision and delegation; regulatory reporting (Regulatory Obligations); record keeping (Regulatory Obligations); trading (Market Conduct); and disclosures to the market (Market Conduct).

SINGAPORE



For the period of 2013-2017, the top five areas for the number of penalties by regulatory category in Singapore's enforcement actions in scope of this research are: AML (Financial Crime); Customer Due Diligence (Financial Crime); disclosures to the market (Market Conduct); unlicensed activity (Regulatory Obligations); and firm management (Corporate Governance) particularly in relation to systems and controls.

AUSTRALIA



For the period of 2013-2017, the top five areas for the number of penalties by regulatory category in Australia's enforcement actions in scope of this research are: disclosures to clients (Conduct of Business Obligations); trading (Market Conduct); regulatory reporting (Regulatory Obligations); firm management (Corporate Governance) particularly in relation to systems and controls, supervision and delegation, and risk management; and disclosures to the market (Market Conduct).

Author
Monique Melis
Managing Director, Duff & Phelps
monique.melis@duffandphelps.com

Human Resources as the new Compliance function

Individual accountability won't transform organisational culture on its own, but firms could make greater use of a resource they already have.

In recent years, efforts to change the compliance culture in firms have been have been greatly impacted by the increased emphasis on individual accountability. Regulators such as the FCA have repeatedly – and rightly tried to encourage this change by stressing the importance and influence of the "tone from the top" in firms.[31]

However, without an organisational infrastructure to promote, coordinate and control efforts to change the culture, , these efforts are likely to fail.

One reason for this is that, in practice, the driving force behind individual accountability is the threat of sanctions on individuals for compliance failures for which they are held responsible. That threat is still relatively slight in jurisdictions such as the UK,– notwithstanding of course the introduction of the SMCR. FCA fines in 2017 totalled £229.5 million, but those issued against individuals amounted to just £435,000. The regulator has in 2018, despite their strong stance on individual accountability and conduct even shown reluctance to opt for harsher sanctions against individuals in at least one recent high-profile case against Barclay's Chief Executive Officer following his attempts to identify an internal whistleblower.[32]

Where the regulator's bark is seen to be worse than its bite when it comes to individual sanctions, the power of individual accountability to transform the organisation culture is ultimately diminished.

People power

It is unrealistic to expect regulatory initiatives, such as the SMCR to change culture in isolation without broader support. In other areas, such as tackling sexual harassment, bullying or discrimination there is no lack of consequences for an individual's failure to behave properly; nevertheless, it is still assumed the organisation will be the one to take responsibility for ensuring the rules are followed.

In both of these areas, it is the Human Resources department that takes a lead in both developing and enforcing policies and procedures, as well as handling complaints. Might it play a similar role in compliance?

There is a strong argument that it should. Of all the functions in the business – possibly including the leadership – Human Resources has arguably the greatest experience, expertise and role in determining the workplace culture. Monitoring and managing employees' behaviour against the firm's objectives, expectations and policies is its bread and butter. Human Resources usually has a hand on the key levers businesses have to influence staff behaviour, too: appraisal systems, feedback, goal setting, and of course bonuses and pay. Since compliance is ultimately about encouraging the right behaviours, this department could be a powerful force in steering organisational culture to where it needs to go.

For that vision to be realised, however, at least two things need to happen. First, the connection and communication between the Compliance function and Human Resources will need to improve. A collaboration between the two could amalgamate Human Resources' expertise in helping promote and influence employees' behaviours and Compliance's the in-depth understanding of the behaviours required into the perfect infrastructure to promote a better culture.

Second, Human Resources needs a higher profile within the organisation as well as the power to drive change through to the end. The function needs to be elevated to a greater role in setting businesses strategy so that it can ensure the cultural changes required are reflected in priorities for hiring, appraisals, and pay.

Human Resources therefore has massive potential in driving through the changes firms need to see. By establishing a collaborative infrastructure that integrates the Human Resources and Compliance functions, firms could become much more efficient and effective in their compliance responsibilities. As ever, though, this directive also needs to be lead from the top.

31. https://www.fca.org.uk/news/speeches/culture-conduct-extending-accountability-regime
32. https://www.fca.org.uk/news/press-releases/fca-and-pra-jointly-fine-mr-james-staley-announce-special-requirements

Author
Claire Simm
Managing Director, Duff & Phelps
claire.simm@duffandphelps.com

AML compliance firmly in focus

Regulation of AML is a high risk and continually changing area. Regulators across the world are also consistently taking decisive, public action against firms and individuals for AML failures, in an effort to combat financial crime.

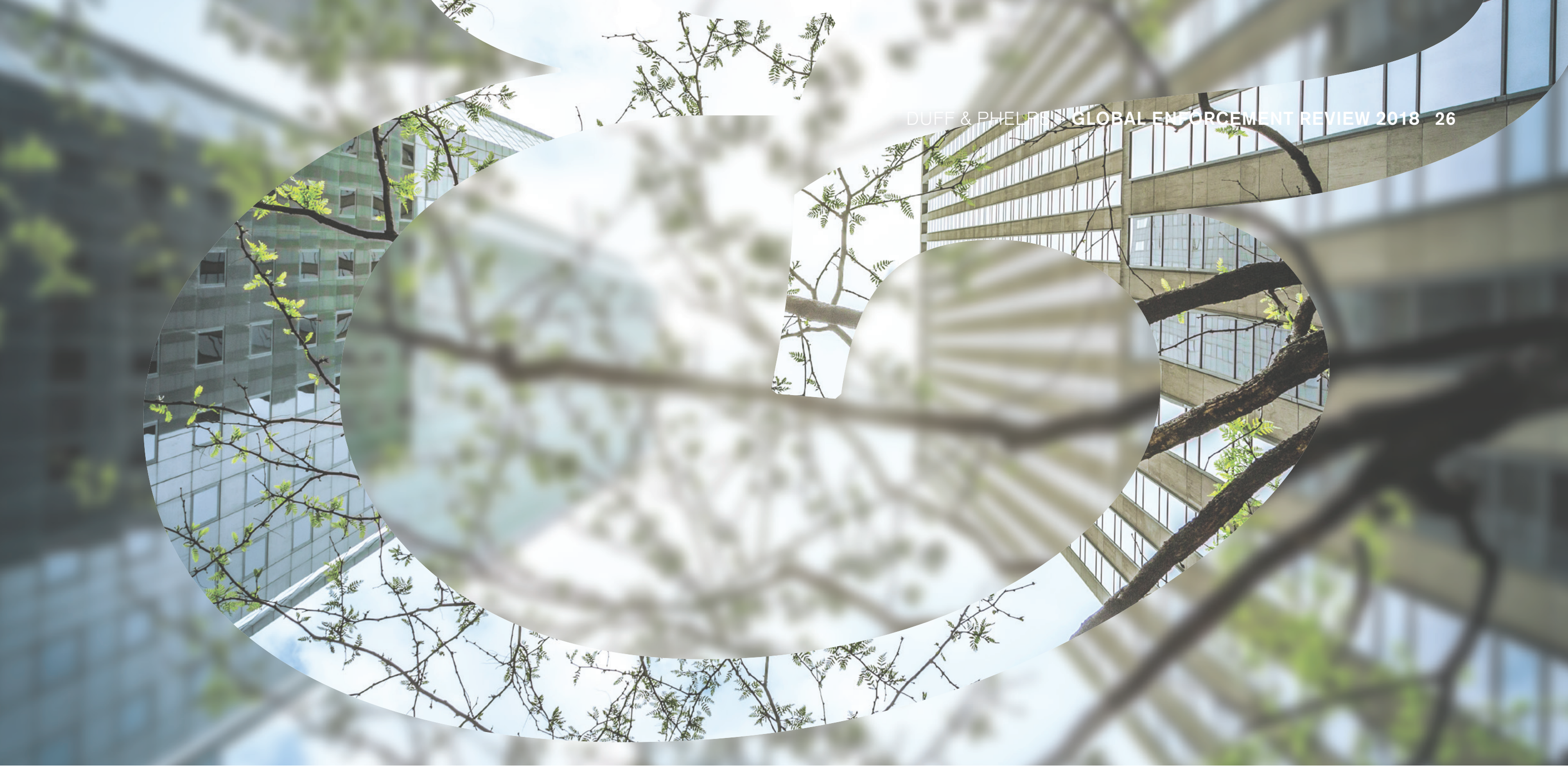
Numerous high-profile enforcement actions show that financial crime compliance remains a core priority for regulators and law enforcement agencies around the world. When we look globally at enforcement fine amounts over the past five years, financial crime is the second highest category behind conduct of business obligations.

Within the financial crime category from 2013 to 2017, the top five areas relate to sanctions breaches (US$10.1 billion), followed by bribery (US$5.6 billion), tax evasion (US$5.1 billion), fraud (US$4.4 billion) and AML (US$3.5 billion). This attention is not going to change soon, with both institutions and individuals firmly in regulators' focus.

The rise in AML enforcement

AML has particularly come to the fore in 2017 and 2018, with enforcement actions resulting in multi-million-dollar fines and some high-profile cases, including:

- ING reached a settlement agreement with the Dutch Public Prosecution Service to pay a fine of to pay a fine of €675 million and €100 million for disgorgement for shortcomings in the execution of customer due diligence policies to prevent financial economic crime at ING Netherlands.[33]
- Commonwealth Bank of Australia (AU$700 million) was issued the largest fine in Australian corporate history from AUSTRAC for breaches in AML and CFT financing laws.[34]



- Rabobank (National Association) agreed to pay over US$360 million for processing illicit funds and concealing AML deficiencies.[35]

- US Bancorp was fined approximately US$600 million by three U.S. agencies for failing to have an adequate AML programme.[36]

- UK and US regulators took strong action against Deutsche Bank, fining the firm approximately US$600 million for AML controls failings.[37]

- FinCEN secured its largest ever fine against an individual, a US$250,000 civil penalty against a chief compliance officer for failing to implement an effective AML program.[38]

This tough action reflects, at least in part, cases that involved the actual laundering of potentially criminal money, not just a failure of a firm's systems and controls. In such circumstances, it should be no surprise that the regulators have come down very hard.

But it's not only the large, headline grabbing cases that demand firms' attention. Smaller, though still significant, actions show that a wide range of financial services firms and individuals are being scrutinised. Offshore markets continue to strengthen their AML regulatory framework and enforcement regimes, with a number of recent enforcement actions imposed in jurisdictions such as Singapore,[39] Ireland,[40] Channel Islands[41] and Bermuda[42] among others. Moreover, unregulated corporate entities are also open to AML risk and broader financial crime risk through the enforcement of sanctions, corruption or other criminal laws.

A changing landscape

The push against money laundering that has been running since the late 1980s has undoubtedly made it

33. https://www.ing.com/Newsroom/All-news/Press-releases/ING-reaches-settlement-agreement-with-Dutch-authorities-on-regulatory-issues-in-the-ING-Netherlands-business.htm
34. hhttp://austrac.gov.au/media/media-releases/austrac-and-cba-agree-700m-penalty
35. https://www.justice.gov/opa/pr/rabobank-na-pleads-guilty-agrees-pay-over-360-million
36. https://www.justice.gov/usao-sdny/pr/manhattan-us-attorney-announces-criminal-charges-against-us-bancorp-violations-bank
37. https://www.fca.org.uk/news/press-releases/fca-fines-deutsche-bank-163-million-anti-money-laundering-controls-failure; https://www.dfs.ny.gov/about/press/pr1701301.htm
38. https://www.fincen.gov/news/news-releases/fincen-and-manhattan-us-attorney-announce-settlement-former-moneygram-executive
39. http://www.mas.gov.sg/News-and-Publications/Media-Releases/2018/MAS-Imposes-Penalties-on-Standard-Chartered-Bank-and-Standard-Chartered-Trust-for-AMLCFT-Breaches.aspx
40. https://www.centralbank.ie/docs/default-source/news-and-media/legal-notices/settlement-agreements/public-statement-relating-to-settlement-agreement-between-central-bank-of-ireland-and-bank-of-ireland.pdf
41. https://www.gfsc.gg/commission/enforcement/public-statements; https://www.jerseyfsc.org/media/1415/2017-07-13-final-nwog-public-statement.pdf
42. http://www.bma.bm/BMANEWS/Bermuda%20Monetary%20Authority%20Fines%20Sun%20Life%20Financial%20Investments%20(Bermuda)%20Ltd%20$1,500,000%20and%20Restricts%20Licence.pdf

more difficult to launder money through the conventional financial services system. What was originally legislation targeting the global narcotics trade and the volume of cash it generated, has evolved into a comprehensive framework of rules across the globe that can be challenging to implement effectively; and now aimed at preventing and detecting all types of financial crime including: tax evasion, corrupt payments and bribery, human trafficking, narcotics trafficking, securities fraud and other criminal enterprise.

The rise of cryptocurrencies presents a new threat from an AML perspective. Virtual, web-based currencies can circumvent all the controls in the conventional financial system that have been so laboriously built-up over the past three decades. Regulators, which have not historically employed many cutting-edge technology experts or invested particularly heavily in their own technology, are moving at some pace around the globe to develop the right skillsets and are also endeavouring to create the right AML regulatory frameworks for this evolving industry. The 5th Money Laundering Directive in the EU is one such example of an AML regulation now being updated to include cryptocurrencies in its scope.

Individuals are also not immune. Regulators repeatedly communicate their commitment to pursue individuals for compliance failures and in this era of individual accountability, it seems likely that we will soon see more cases around the world.

Despite this changing landscape, through our review of enforcement actions and our work with firms around the globe, we see some consistent themes emerging in relation to failures in AML systems and controls (see Table 1).

The real goal though for firms is not to simply implement new rules and respond to regulatory concern; **it is to prevent and detect criminal money being laundered and terrorism being financed**. In all of this complexity and change, this sometimes can be forgotten.

Table 1: AML and financial crime control failing areas

Governance findings:	Operational findings:	Three lines of defence findings:
▪ Insufficient knowledge of the firm's AML and financial crime risks ▪ Poor governance arrangements, including inadequate discussion of AML in board meetings ▪ Inadequate board and committees, with insufficient levels of financial crime responsibility and unclear lines of escalation ▪ Senior management not being sufficiently involved in key AML decisions ▪ Duplication of roles and responsibilities between committees ▪ Lack of knowledge or action taken following alerts issued by regulators ▪ Tone from the top does not promote an AML-compliant culture ▪ Lack of MI or MI is produced without adequate trend analysis; or substantial volume of MI that contributes to inadequate oversight ▪ Ineffective or inappropriate MLRO reporting lines and a lack of MLRO independence	▪ Lack of appropriate process, systems and controls around EDD and PEPs ▪ Inadequate or ineffective risk assessment ▪ Inadequate screening of relationships and all relevant parties ▪ Lack of awareness of AML risks or controls ▪ Under investment in AML technology and dedicated AML expert resources ▪ Inadequate policies and procedures to ensure financial crime risk is considered, for example in the development of new products or new markets ▪ Reliance on head office to undertake due diligence where transactions are led by another group entity ▪ Delegation to third party providers or outside resources without adequate oversight	▪ Lack or ownership and accountability by the business for the first line financial crime risks and controls ▪ AML is given insufficient importance in second and third lines of defence ▪ Lack of clear segregation of duties regarding roles and responsibilities for AML processes and controls ▪ Ineffective reporting lines for second and third lines of defence ▪ Insufficient skills, resources and training of control staff responsible for AML and financial crime ▪ Inappropriate frequency, nature or breadth of financial crime monitoring tests ▪ Financial crime annual plan and monitoring plan is not reviewed and signed off by appropriate stakeholders ▪ Financial crime monitoring plan is not sufficiently risk-based, through use of a detailed enterprise risk assessment and regulatory footprint analysis

Author
Malin Nilsson
Managing Director, Duff & Phelps
malin.nilsson@duffandphelps.com

All in it together

Consequences for regulatory breaches still vary widely between jurisdictions, particularly when it comes to offshore financial centres. For businesses with a global footprint, this makes a strong case for global standards to manage this unpredictability.

Despite cross-border cooperation between regulators and global regulatory trends, substantial differences in standards persist, which opens the door to regulatory arbitrage. These differences exist not only between offshore and onshore jurisdictions, but between offshore jurisdictions themselves. Some, such as those in the Channel Islands, have regulatory regimes that match and, arguably, surpass in many cases, the standards of the major onshore centres. Others, not so much.

Frequently, these differences come down to the level and extent of supervision and enforcement activity, rather than the legislation and regulations themselves. Certainly, for areas such as AML, regulatory requirements across jurisdictions are fairly consistent; the key is how they are applied. It is not simply a case of looking at the number of fines or penalties imposed, either; the first civil penalty in Jersey is yet to be levied, for example, but the other enforcement tools which the regulator uses also carry significant weight. In the British Virgin Islands, meanwhile, while fines are common, they are often viewed as being for administrative failings.

For those firms with international operations that poses a question: Should they implement global standards across their operations, meeting the highest standards even in those jurisdictions where the consequences for failure are lower?

The case for global standards

On the one hand, there might seem little benefit in doing so, in the current situation. Where an office has operated to lower regulatory expectations for years, the cost of bringing it up to a higher, global standard will be significant – with the risk of enforcement action seemingly low if the local regulator is not known to take such steps. It could even cause the business to be uncompetitive against others continuing to operate to a lower requirement.

For those with investors and finance providers in Europe and the U.S., however, global standards make sense, as the impact of failures is increasingly global: Regardless of where money laundering or sanctions breaches occur, the damage to a group's reputation remains. In many cases this will outweigh the cost of any regulatory fine. It is often the investors and providers of finance, as well as the local regulators, who determine the true expectations firms must meet.

Two other factors also offset the costs for international businesses which raise standards in jurisdictions with weaker enforcement regimes. The first is that global standards provide some opportunity for economies of scale, enabling groups to centralise aspects of compliance policy and control. Though not eliminating the need for local regulatory expertise, firms' local offices can avoid having to reinvent the wheel every time they seek to respond to changing regulations and enforcement priorities.

The second consolation they can take, meanwhile, is that those failing to apply higher standards are unlikely to be avoiding the cost, just postponing it. Opportunities for regulatory arbitrage continue to exist, but they also continue to shrink; and enforcement regimes, while at different stages of development, are largely trending the same way. The savings from taking advantage of remaining disparities will, in most cases, prove short-lived.

4. Trends in penalty amounts

Globally, fine amounts have edged up following a massive fall from the peak of the big benchmark manipulation cases in 2013 and 2014. This in large is dominated by U.S. enforcement actions.

Of the large fines globally included in the scope of this research, fines against firms increased from US$19.7 billion in 2015 to US$25.9 billion last year. For the first six months of 2018, meanwhile, the total was US$8 billion.

That, though, obscures a more complex picture. First, the overall figure is heavily influenced by activity of the U.S. regulators. In 2017, the U.S. accounted for US$24.4 billion of the total, an even higher proportion than usual. Moreover, this figure is itself skewed by some large fines in bribery cases against non-financial firms; AML and fraud cases against financial services firms; and other fines relating back to the financial crisis cases. Even more significantly, two extremely large fines (relating to disclosure and client communications) together account for half the 2017 U.S. total.

Less expensive…

In fact, the overall trend seems to be towards less reliance on fines in financial services. In the UK, for instance, total fine amounts are down from a peak of £1.5 billion in 2014 and £958.4 million in 2015 to £865.2 million in 2017; this 2017 figure is, however, largely skewed by a £510 million penalty issued by the Serious Fraud Office to a non-financial firm in relation to corruption, false accounting and failure to prevent bribery.[43]

That is not to say the traffic is all one way. There's evidence, for instance, that China is ramping up enforcement action and fines (although published data is difficult to come by). It is also interesting that in the area of AML – regularly in the top five categories for fines – regulators without much of a track record for issuing fines have become more active. We see this particularly with the French PSRA and the Central Bank of Ireland, for example.

43. https://www.sfo.gov.uk/cases/rolls-royce-plc/

We see no sign yet of a return to the peak penalty levels seen earlier in the decade. Those huge fines also largely reflected the size of the organisations involved; big banks get fined big amounts and small firms are fined smaller amounts.

Despite the drive from regulators to promote individual accountability, there is a similar declining trend globally in the fine amounts against individuals from 2016 to 2017, and this trend looks set to continue for 2018. When we look at individual jurisdictions, however, these vary widely, with the U.S., Europe (excluding the UK) and Hong Kong having increased fine amounts; this is despite, except for Europe, a decline in number of fines.

But change is coming

Arguably, the pattern of declining fines against firms is also evidence of two other trends. The first is some disillusionment on the part of regulators with the efficacy of fines on firms to alter behaviour – at least when applied on their own. Following the discovery of the benchmark manipulation cases, regulators tested almost to destruction the theory that very high penalties would result in cultural change within financial services firms affected. The evidence that they do is, at best, mixed.

Regulators are therefore questioning the effectiveness of large fines and are coming up with new ways to tackle abuses, including a greater emphasis on restitution and disgorgements (see Nick Bayley's article: Making good: New thinking on compensation for public market investors).

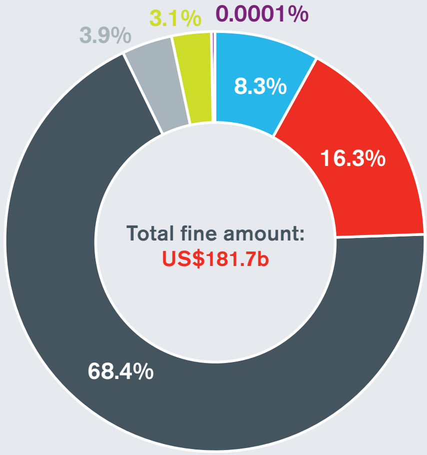
That is not to say we will not continue to see significant numbers of penalties imposed against firms – and large fines for the worst failures and biggest businesses. It does, however, mean that regulators, particularly in the most established financial centres, may be less solely reliant on them in future. Instead, we could see the employment of a more sophisticated approach, in which a range of sanctions targeted at firms, are used in conjunction with an increased emphasis on individuals.

The second trend is related to this: Billion-dollar fines have simply lost their power to shock, not just in the industry but also among the public. Like the regulators, the public too have perhaps been left wondering if the firms affected really feel the impact. That does not mean that they want to see abuses go unpunished. It just means they are no longer impressed with big fines that only hurt the shareholders. Instead, they want to see individuals held to account. With the introduction of accountability regimes across the globe, it may only be a matter of time before the number of fines and the profile of cases against individuals rival those made against firms.

PENALTY AMOUNTS BY REGULATORY CATEGORY 2013-17

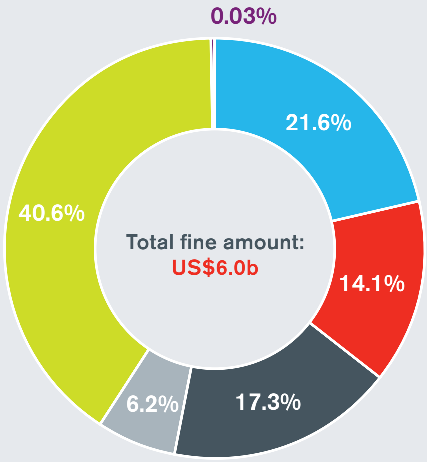
Market Conduct
Financial Crime
Conduct of Business Obligations
Regulatory Obligations
Corporate Governance
Privacy and Cybersecurity

US



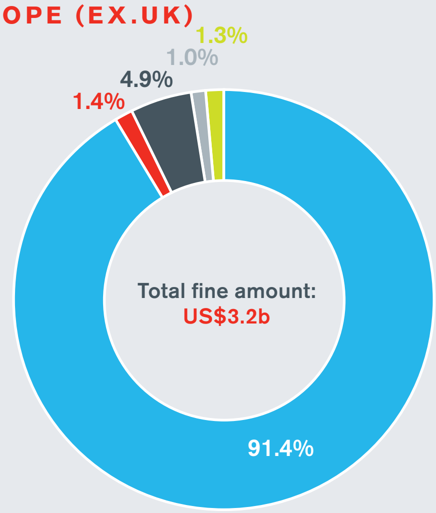
For the period of 2013-2017, the top five areas by penalty value in the U.S. in scope of this research are: disclosures to clients (Conduct of Business Obligations) by a considerable margin at US$104 billion; market manipulation (Market Conduct) at $11.7 billion; arrears handling (Conduct of Business Obligations) at US$11 billion; sanctions (Financial Crime) at US$10 billion; and tax evasion and bribery (Financial Crime) with both at US$5 billion.

UK



For the period of 2013-2017, the top five areas by penalty value in the UK in scope of this research are: firm management (Corporate Governance) at US$2.6 billion; market manipulation (Market Conduct) at US$1.2 billion; bribery (Financial Crime) at US$660 million; conflicts of interest (Conduct of Business Obligations) at US$408 million; and unfair treatment of customers (Conduct of Business Obligations) at US$138 million. Of note, almost half of the total is due to FCA fines against five banks totalling £1.1 billion (over £200 million each) for FX failings.[44]

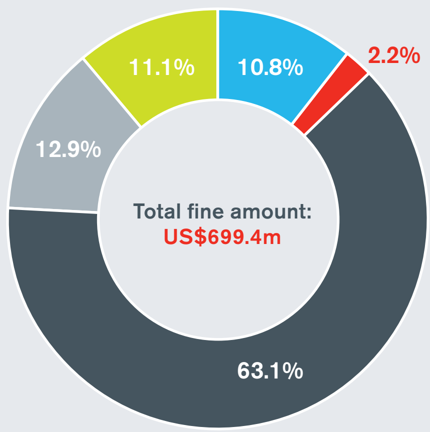
EUROPE (EX.UK)



For the period of 2013-2017, the top five areas by penalty value in Europe in scope of this research are: anti-competitive behaviour (Market Conduct) at US$2.8 billion; conflict of interest (Conduct of Business Obligations) at US$78.5 million; market manipulation (Market Conduct) at US$77.8 million; disclosure to clients (Conduct of Business Obligations) at $50 million; and firm management (Corporate Governance) at $40.5 million. Of note, almost a quarter of the penalties total for anti-competitive behaviour is due to a fine by the European Commission for €485 million against three banks for euro interest rate derivatives cartel.[45]

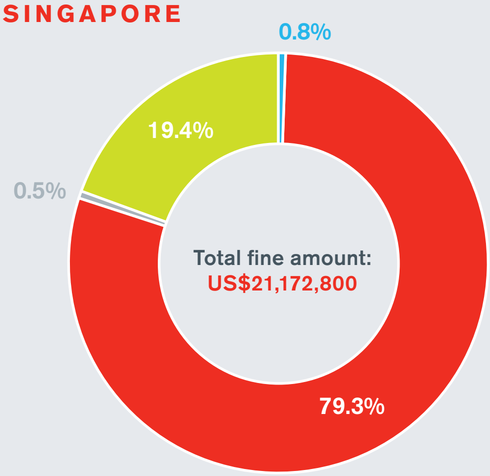
Market Conduct
Financial Crime
Conduct of Business Obligations
Regulatory Obligations
Corporate Governance
Privacy and Cybersecurity

HONG KONG



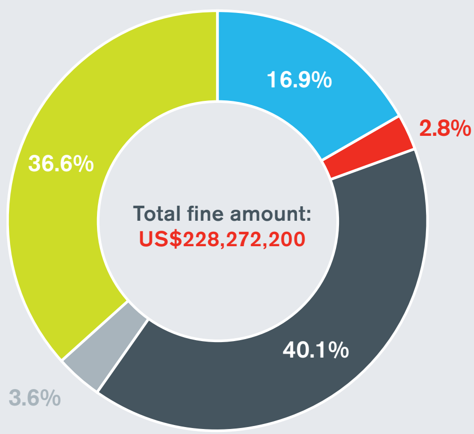
For the period of 2013-2017, the top five areas by penalty value in Hong Kong in scope of this research are: miss-selling and suitability (Conduct of Business Obligations) at US$30 million; disclosures to clients (Conduct of Business Obligations) at US$27 million; firm management (Corporate Governance) at US$11.5 million; regulatory reporting (Regulatory Obligations) at US$9.5 million; and trading (Market Conduct) at US$3.3 million. Of note, a large fine of HK$400 million (US$50 million) by the SFC against HSBC Private Bank (Suisse) SA in relation miss-selling and suitability forms the bulk of the fines in disclosures, miss-selling and suitability to clients.[46]

SINGAPORE



For the period of 2013-2017, the top five areas by penalty value in Singapore in scope of this research are: AML (Financial Crime) at US$8.5 million; customer due diligence (Financial Crime) at US$8.5 million; firm management (Corporate Governance) at US$3.9 million; insider trading (Market Conduct) at $140,000; and unlicensed activity (Regulatory Obligations) at US$102,000. Of note, Regulatory Obligations dominated figures from 2013 to 2015, which was replaced by Financial Crime in 2016 and 2017. A fine of SGD$13.3 million by the MAS for AML failures against BSI Bank[47], as well as other AML related fines that year that were large, contributing to the rise in the financial crime total.

AUSTRALIA



For the period of 2013-2017, the top five areas by penalty value in Australia in scope of this research are: firm management (Corporate Governance) at US$85 million; miss-selling and suitability (Conduct of Business Obligations) at US$68 million; market manipulation (Market Conduct) at US$35 million; overcharging (Conduct of Business Obligations) at US$11 million; and regulatory reporting (Regulatory Obligations) and AML (Financial Crime) both at US$6.8 million. Of note, the firm management related penalties by ASIC against two big banks of AU$50 million each in 2017 make up a large portion of these fine totals.[48]

44. https://www.fca.org.uk/news/press-releases/fca-fines-five-banks-%C2%A311-billion-fx-failings-and-announces-industry-wide
45. http://europa.eu/rapid/press-release_IP-16-4304_en.htm
46. https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR138
47. http://www.mas.gov.sg/News-and-Publications/Enforcement-Actions/2016/MAS-directs-BSI-Bank-to-shut-down-in-Singapore.aspx
48. https://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-393mr-asic-accepts-enforceable-undertakings-from-anz-and-nab-to-address-conduct-relating-to-bbsw/

Author
Mark Turner
Managing Director, Duff & Phelps
mark.turner@duffandphelps.com

Running out of puff?

Whistleblowing has come a long way in the last decade. And there's a long way still to go.

Attitudes to whistleblowing have slowly but surely transformed over recent years. When CEO and whistleblower Michael Woodford exposed the accounting scandal at medical equipment and camera business Olympus, one of Japanese largest corporates, he was considered by some to be a traitor – and not just by those inside the company.[49]

At the time, his concerns were not just for his career, but his safety. As he says, people have been killed for a lot less than the US$1.7 billion at the heart of the scandal. "I was scared," he has recalled. "Wouldn't you be?"[50]

Today much has changed. Woodford now has a TV deal,[51] and the role of whistleblowers is recognised and protected by governments, regulators and businesses alike. We've come a long way. Global rules on whistleblowing are gradually beginning to show signs of convergence, with greater legal protection and a recognition of their value in promoting compliance and identifying abuses being either implemented or proposed in recent years in several major economies, including the U.S., UK, China and Australia to name but a few.

But it would be rash to think that changes to rules and protections are done. In the UK for example, the number of whistleblowing cases in asset managers in 2017 was 21, its lowest in years and just half the number there were in 2014. And the total number of reports received by the FCA is down, too – 1,047 last year, from a high of 1,360 in 2014.[52] Whilst there may be positive reasons for some of this decline, possibly including firms' own internal processes improving and underlying issues being fixed, the direction of travel feels slightly at odds with whistleblowing becoming culturally accepted and encouraged.

A big sacrifice

There's speculation that some recent decisions by regulators have undermined the message of support for whistleblowing, which was originally conveyed in the UK's 2015 shakeup of the area, led by both the PRA and FCA that required firms to put in place adequate policies on dealing with whistleblowers and a senior manager to take responsibility for overseeing them. The rules aimed "to encourage a culture in which individuals working in the industry feel comfortable raising concerns and challenge poor practice and behaviour".[53]

Critics, and a number of high profile whistleblowers themselves, point out that there is still some way to go before those who raise the most serious of concerns can do so without fear of losing their careers.[54]

The problem is more fundamental, however. Partly, it is that there are still cultural barriers that discourage "disloyalty" and view whistleblowing with suspicion. Mostly, it is that the cost for many whistleblowers is still too high, and the benefits unclear. Many who whistleblow may want to do the right thing, but they are measuring that against massive uncertainty around the impact on their career, their personal life and financial future. How many are willing to put their neck on the line for the greater good?

Since 2012, U.S. regulators have addressed this with financial incentives for whistleblowers. Other regulators have not, so far, followed suit. The FCA considered the question of financial rewards in 2014, only to reject the idea over doubts about evidence for its effectiveness and concerns over the costs associated with incentive schemes.[55] Instead, its most recent development has been to insist on each firm appointing a senior manager as a "whistleblowers' champion" – part of the SMCR that entered into force in the UK banking sector in September 2016.[56]

Time will tell whether this proves enough to reverse the trend of declining whistleblowing numbers. The early indications, however, are not encouraging. Where firms can focus their efforts in the meantime is to review their internal whistleblowing arrangements to ensure they are compliant, fit for purpose and fully supported by senior management and the Board.

Equally, management can set a positive tone from the top, fostering an organisational culture where whistleblowers feel empowered and confident to come forward without fear of repercussions, and where whistleblowers are viewed as acting in the best interest of the company and the industry.

49. https://www.cass.city.ac.uk/news/2013/november/i-am-seen-by-most-of-corporate-japan-as-a-traitor
50. https://www.youtube.com/watch?v=M4Y36QynUgU
51. https://www.telegraph.co.uk/business/2017/11/11/olympus-whistleblower-lands-tv-deal-japan-faces-wave-fresh-scandals/
52. https://www.ft.com/content/a4647046-5470-11e8-b3ee-41e0209208ec
53. https://www.fca.org.uk/news/press-releases/fca-introduces-new-rules-whistleblowing
54. https://www.ft.com/content/9fbe05cc-569e-11e8-bdb7-f6677d2e1ce8
55. https://www.fca.org.uk/news/statements/financial-incentives-whistleblowers
56. https://www.handbook.fca.org.uk/handbook/SYSC/18/4.html?date=2016-03-07

Author
Nick Inman
Managing Director, Duff & Phelps
nick.inman@duffandphelps.com

No Simple Solution

The MIC regime in Hong Kong is going to require firms to look more closely at their governance structures.

In part it was the constitution of governance structures globally that led to new powers to hold individuals in financial firms to account. The SMCR in the UK and MIC regime in Hong Kong have both sought to remove ambiguity around roles – and responsibilities – within organisations: to bring clarity where complexity prevented accountability.

Since the introduction of the new regime, during the brief months leading up to the deadline in July 2017, Hong Kong's financial regulator, the SFC has processed a vast number of people as MICs: over 10,000 individuals – 40% of them never licensed before.[57]

That has a number of consequences. The first, and perhaps the most obvious, is that we should see increasing actions taken against individuals. While the MIC regime was an initiative of the SFC's licensing division, rather than its enforcement or supervisory divisions, the latter divisions have been clear to staff when conducting inspections and investigations that they are to establish the responsible individuals at the outset when they discover any potential weaknesses in licensed firms.

Now that a reasonable period has elapsed since the implementation of the regime, cases against such individuals are likely to start coming through over the next year as these inspections bear fruit.

The new regime is also likely to lead to more formal governance structures, in particular within local and smaller firms in Hong Kong that may previously have been behind the curve. Indeed, the acknowledgement of firms' efforts in strengthening their governance structures was the focus of comments by the SFC's Chief Executive Officer when announcing full implementation of the new regime. [58]

For many firms, though, there is a lot more work to be done.

A new approach

Most European firms of any size usually have an array of committees ranging from Audit, Risk to Valuation, as well as an executive committee that typically meets monthly and a board meeting typically quarterly. Some of the SFC's discussion around the MIC regime would give the impression that this is much the same in Hong Kong. While there are some exceptions, for many firms it is not.

Most companies in Hong Kong will have a board that only meets annually to sign off the accounts – this is in line with the Companies Ordinance under which a company can be formed with just one director. There is little formality otherwise. "Board" in Hong Kong is a slightly loose term that, most fund managers, for example, will assume is referring to the fund board, not the management board.

It looks doubtful that this can last in the new environment. The MIC regime is not simply about having someone to blame – and penalise – when things go wrong; it is designed to ensure that the right people, processes and management information are in place to protect investors and meet regulatory obligations. Changes will come piecemeal. In January, for example, a thematic review of best execution has led many to consider whether they need to introduce regular reviews and sampling of the quality of execution: This is no longer simply a trading issue; it is a compliance issue, too.

57. https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR13.
58. ibid

5. Spotlight on sectors

Big banks are still attracting the largest fines from financial regulators. Similar to previous years, investment banking globally was the recipient of the lion's share of penalty amounts handed out in 2017, with fines totalling US$20.6 billion. We can safely predict this trend will continue, with investment banks leading the penalty amounts for the first half of 2018 at US$4 billion.

In common with every year bar one since 2013, it is the securities-issuing business of those banks that is the primary target. The exception was 2015, when it was the FX markets service line that bore the brunt of penalty amounts. (That sector has also been among the top recipients of fines in four out of the last five years.) In fact, the investment banks have been particularly heavily hit by regulators across their fixed income markets, sales and trading and treasury services.

Mis-selling and residual benchmark manipulation cases are still making themselves felt.

New frontiers

However, that does not mean other sectors can relax.

For a start, even looking simply at the aggregate of the fines, several other sectors globally are seeing fine totals regularly exceeding US$1 billion. A steady flow of big bribery cases in the past few years, not least in 2017, has elevated the prominence of the non-financial corporate sector, which ranked second only to investment banking in the last two years. Also included are consumer banks, as well as asset and wealth managers, which have each respectively paid out over US$18.7 billion and over US$8.3 billion between 2013-17.

Added to that, regulators are proving unafraid of expanding their remit to cover sectors that have previously received little attention. Both the U.S. Justice Department and European Securities and Markets Authority levied big fines (or agreed settlements) with ratings agencies in the last year, for example – for mortgage ratings in the run up to 2008 financial crisis in the case of the former, and transparency failings for the latter.

Added to that, we are seeing increased enforcement against unlicensed activity. An expanding regulatory perimeter is resulting in greater oversight of businesses such as consumer credit firms (including payday lenders)[59] and claims companies (particularly around PPI)[60] in the UK – both sectors that had been very lightly or completely unregulated in the past.

Size isn't everything

The willingness of regulators to tackle new sectors could be important, as fintech businesses continue to disrupt financial services markets – and particularly if and when the big technology players make serious moves into this space. It should mean that simply identifying a business as a technology firm rather than a financial services company is unlikely to get participants a free pass. Regulators will insist on a level playing field for everyone to protect consumers.

That should please the likes of asset managers that have feared unfair competition. But they should not take too much comfort from regulators' expanding remit, nor the apparent focus on investment banks when it comes to fines.

As said previously in this report, the level of fines simply reflects the organisations involved: The largest organisations can expect more significant penalties. That does not mean others won't be sanctioned.

In fact, asset and wealth management remain a key focus for regulators. Look at the number, rather than cumulative value, of fines across regulators and this becomes clear. Both sectors have been among the most frequently sanctioned by regulators in both 2017 and 2018 (to date), and one or other is among the top five in every year since 2013, other than 2014.

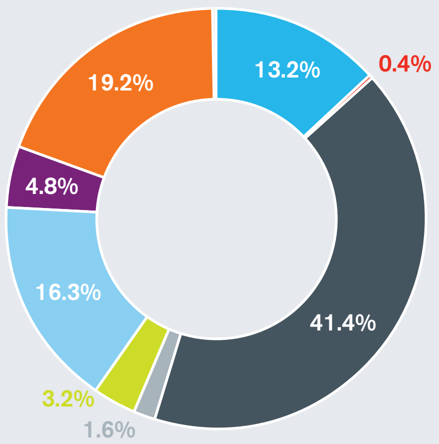
If asset managers expect an easy time, they are likely to be disappointed.

59. https://www.fca.org.uk/news/press-releases/agenda-priorities-consumer-credit
60. https://www.fca.org.uk/publications/policy-statements/ps17-3-payment-protection-insurance-complaints

FREQUENCY OF PENALTIES GLOBALLY BY SECTOR 2013-17

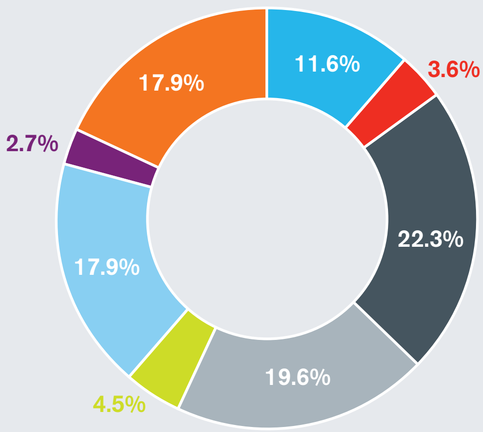
Consumer Banking
Corporate Banking
Investment Banking
Insurance
Investment Services
Asset and Wealth Management
Treasury Services
Non-Financial/Corporate Services

US



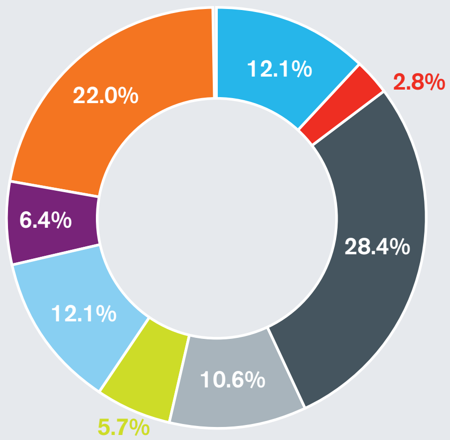
For the period of 2013-2017, the top five service lines by the number of penalties for regulatory category failings in U.S. enforcement actions in scope of this research are: securities issuing (Investment Banking); non-financial (Corporate Services); wealth management (Asset and Wealth Management); commodities markets (Investment Banking); and mortgage lending (Consumer Banking).

UK



For the period of 2013-2017, the top five service lines for the number of penalties by regulatory category failings in UK enforcement actions in scope of this research are: wealth management (Asset and Wealth Management); Insurance Advisory (Insurance); FX markets (Investment Banking); non-financial (Corporate Services); and support services (Corporate Services) and general liability (Insurance).

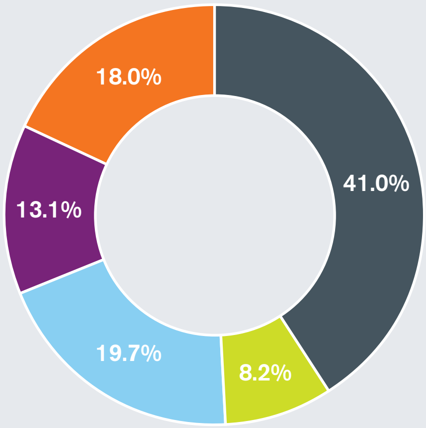
EUROPE (EX.UK)



For the period of 2013-2017, the top five service lines for the number of penalties by regulatory category failings in European enforcement actions in scope of this research are: FI Markets (Investment Banking); Asset Management (Asset and Wealth Management); general liability (Insurance); corporate services (Compliance); and retail deposits (Consumer Banking).

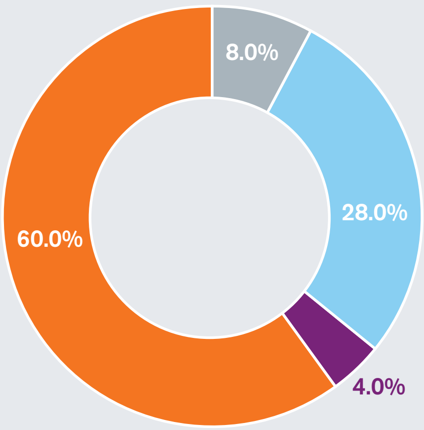
Consumer Banking
Corporate Banking
Investment Banking
Insurance
Investment Services
Asset and Wealth Management
Treasury Services
Non-Financial/Corporate Services

HONG KONG



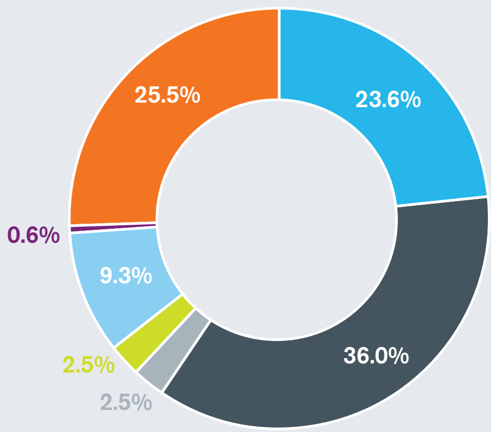
For the period of 2013-2017, the top five service lines for the number of penalties by regulatory category failings in Hong Kong's enforcement actions in scope of this research are: retail brokerage (Investment Banking); equities markets (Investment Banking); cash clearing (Treasury Services); wealth management (Asset and Wealth Management); and asset management (Asset and Wealth Management).

SINGAPORE



For the period of 2013-2017, the top five service lines for the number of penalties by regulatory category failings in Singapore's enforcement actions in scope of this research are: compliance (Corporate Services); support services (Corporate Services); wealth management (Asset and Wealth Management); asset management (Asset and Wealth Management); life and pensions (Insurance): and internal treasury (Treasury Services).

AUSTRALIA

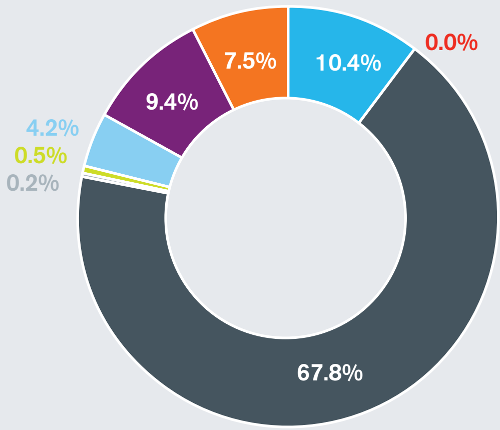


For the period of 2013-2017, the top five service lines for the number of penalties by regulatory category failings in Australia's enforcement actions in scope of this research are: non-financial (Corporate Services); retail lending (Consumer Banking); retail brokerage (Investment Banking); institutional brokerage (Investment Banking); and sales and trading (Investment Banking) and wealth management (Asset and Wealth Management).

PENALTY AMOUNTS BY SECTOR 2013-17

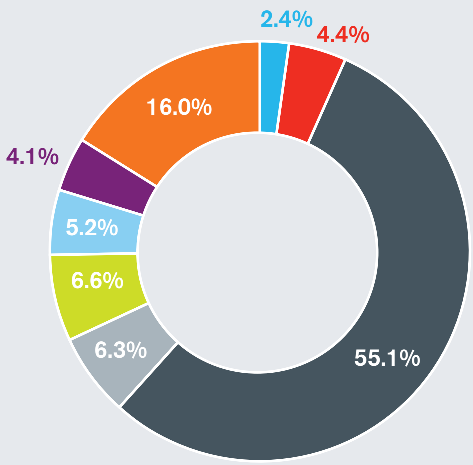
Consumer Banking
Corporate Banking
Investment Banking
Insurance
Investment Services
Asset and Wealth Management
Treasury Services
Non-Financial/Corporate Services

US



For the period of 2013-2017, the top five service lines by penalty value in the U.S. in scope of this research are: securities and issuing (Investment Banking) at US$103 billion; cash clearing (Treasury Services) at $15.2 billion; mortgage lending (Consumer Banking) at $15 billion; FX markets (Investment Banking) at US$10 million; and non-financial (Corporate Services) at US$9.3 billion. Of note, U.S. regulators are consistently fining the largest amounts year on year in investment banking, both with the largest fines overall as well as in cumulative value. This sector has attracted 67.9% of the total amount in fines throughout the period.

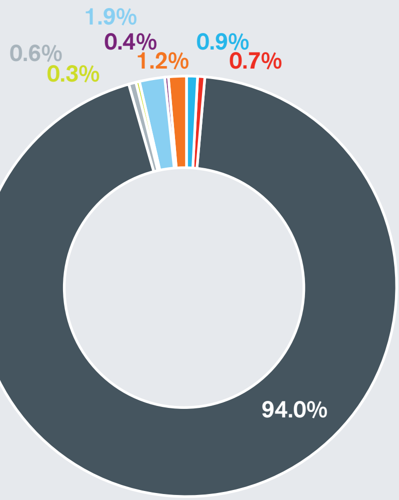
UK



For the period of 2013-2017, the top service lines by penalty value in the UK in scope of this research are: FX markets (Investment Banking) at US$2.2 billion; FI markets (Investment Banking) at US$681 million; non-financial services firm (Corporate Services) at US$640 million; and custody safekeeping (Investment Services) at US$247 million; and general liability (Insurance) at US$246 million. Of note, while it is still a focus for regulators throughout the period, investment banking saw numerous high fines across the years 2014 and 2015 due to LIBOR and FX failings which is subsequently raising the overall figure.

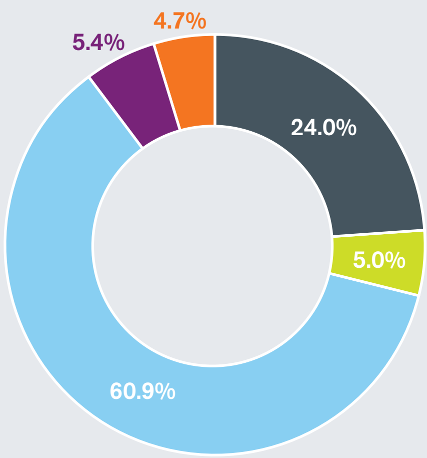
Consumer Banking
Corporate Banking
Investment Banking
Insurance
Investment Services
Asset and Wealth Management
Treasury Services
Non-Financial/Corporate Services

EUROPE (EX.UK)



For the period of 2013-2017, the top five service lines by penalty value in Europe in scope of this research are: FI markets (Investment Banking) at US$2.8 billion; FX markets (Investment Banking) at US$140 million; asset management (Asset and Wealth Management) at US$56 million; retail brokerage (Investment Banking) at US$23 million; and compliance (Corporate Services) at US$18.2 million. Of note, investment banking has been a consistently been the leading sector year on year, except in 2017 where asset management rose in prominence. A large portion of the Investment Banking figures is due to penalties totalling €1.5 billion by the European Commission against eight banks for participating in cartels in the LIBOR and EURIBOR interest rate derivative industry.[61]

HONG KONG

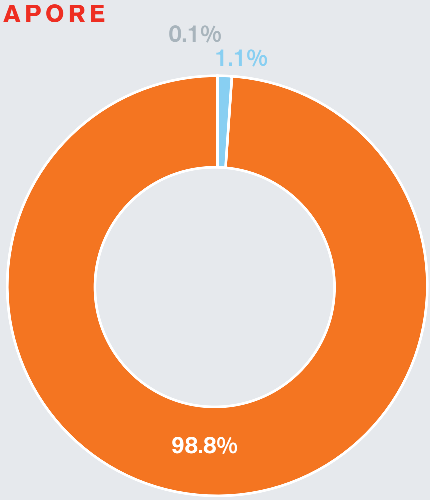


For the period of 2013-2017, the top five service lines by penalty value in Hong Kong in scope of this research are: wealth management (Asset and Wealth Management) at US$53 million; equities markets (Investment Banking) at US$8.6 million; securities issuing (Investment Banking) at US$5.2 million; asset management (Asset and Wealth Management) at US$5 million; and retail brokerage (Investment Banking) at US$4.3 million. Of note, while Investment Banking is consistently in focus, a fine by the SFC of HK$18.5 million for internal control failures[62] brought Corporate Services up to the highest ranked in 2016, and a large fine in 2017 by the SFC of HK$400 million[63] meant that asset and wealth management dominated the figures for 2017 at 87% of the overall total.

61. http://europa.eu/rapid/press-release_IP-13-1208_en.htm
62. https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=16PR83
63. https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR138

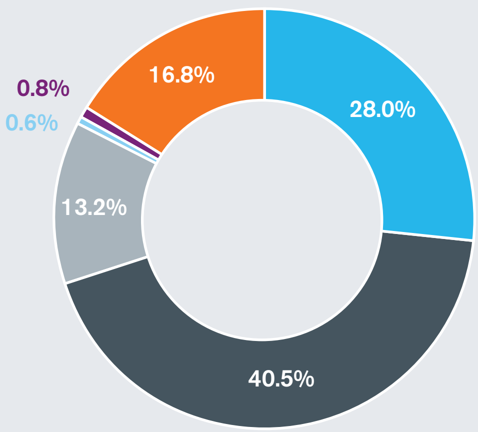
Consumer Banking
Corporate Banking
Investment Banking
Insurance
Investment Services
Asset and Wealth Management
Treasury Services
Non-Financial/Corporate Services

SINGAPORE



For the period of 2013-2017, the top five service lines by penalty value in Singapore in scope of this research are: compliance (Corporate Services) at US$21 million; asset management (Asset and Wealth Management) at US$164,000; wealth management (Asset and Wealth Management) at US$67,500; and life and pensions (Insurance) at £15,000. The size of penalties by Singapore's regulators are lower compared to others globally, however a large penalty was issued by in 2016 by the MAS for SG$13.3 million against a large bank for compliance failings,[64] contributing to this service line's high total figure.

AUSTRALIA



For the period of 2013-2017, the top five service lines by penalty value in Australia in scope of this research are: sales and trading (Investment Banking) at US$77 million; retail lending (Consumer Banking) at US$43 million; non-financial services firms (Corporate services) at US$38 million; general liability (Insurance) at US$30.1 million; and mortgage lending (Consumer Banking) at US$9.8 million. Of note, Australian regulators have directed the largest fines most consistently to the Consumer Banking sector, however Investment Banking makes up the largest proportion of fine amounts across the whole period for fines of AU$50 million each to two large banks in 2017.[65] That said, the fine amounts in consumer banking have been on a steady decline since it peaked in 2014, with a large fines in 2017 by AUSTRAC against Tabcorp (AU$45 million)[66] and by ASIC against Swann Insurance (AU$39 million)[67] contributing to the high fine amounts for both the non-financial services sector (Corporate Services) and Insurance respectively.

64. http://www.mas.gov.sg/News-and-Publications/Enforcement-Actions/2016/MAS-directs-BSI-Bank-to-shut-down-in-Singapore.aspx
65. https://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-393mr-asic-accepts-enforceable-undertakings-from-anz-and-nab-to-address-conduct-relating-to-bbsw/
66. http://www.austrac.gov.au/media/media-releases/record-45-million-civil-penalty-ordered-against-tabcorp
67. https://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-446mr-swann-insurance-refunds-39-million-in-add-on-insurance-premiums/

Author
Hannah Rossiter
Director, Duff & Phelps
hannah.rossiter@duffandphelps.com

A quiet revolution

An increase in enforcement action by the French regulator should prove helpful for firms operating in the country.

Faster and more frequent: That is what French fund managers can expect in terms of enforcement from the country's financial regulator the AMF going forward. At its annual forum for compliance officers held in March this year, the regulator confirmed it would aim to complete 60 inspections of firms in 2018 – double the number of the previous year.

About half of these would be new "spot inspections" or "contrôles courts", an abridged inspection process that could in theory lead to rapid enforcement action if the regulator feels sanctions are warranted. Counterintuitively, that is good news for firms.

Although the new inspection regime could lead to enforcement against firms, that is not its primary function. Rather, the regulator is using these inspections to assess and understand current practice around certain key issues in the industry. Where it finds things working smoothly, it will move on. Where it identifies problems, there will be new guidance to clarify its expectations and inform the industry.

In this respect, the spot inspections are similar to the thematic reviews of the FCA in the UK. They are also part of a wider effort from the AMF to increase transparency, being clearer about both its priorities and requirements. It has also now committed to an annual statement outlining its enforcement priorities. This year these comprise five areas, including valuations, regulatory capital and practices around stock lending – areas where the spot inspections will focus.

Again, there are international precedents here; the SEC publishes similar guidance each year. For France, though, the commitment to this level of transparency on enforcement priorities is new, and perhaps overdue.

A question of clarity

Both the publication of priorities and clarification of regulatory requirements will help firms know where they stand on important issues, which has arguably not been the case in the past. Recent cases on performance fee calculations stand out as an example of this, one of which has already been decided by the AMF.

In that decision, the AMF determined the method to calculate the fees had disadvantaged investors, despite that it was one of a number of other methods that could reasonably have been used. This was not disputed, but the regulator effectively ruled that where a variety of calculation methods were possible, the firm should consider them all and apply the one which was in the best interests of the investor. Failure to do so constituted overcharging[68] – even though independent experts demonstrated that the impact on the performance fee of using another method was minimal.

Crucially, this specific requirement to consider other possible calculation methods was not stipulated anywhere in regulation or guidance.

It is arguable that the AMF's position simply reflects the well-understood regulatory principle to act in the investor's best interests. It is also perhaps right that, as in other areas, ignorance is no defence. Nevertheless, many firms in this jurisdiction will appreciate the increased insight that is now promised into the thinking of the regulator – and the increased opportunities to act accordingly to avoid enforcement action.

68. www.amf-france.org/technique/multimedia?docId=workspace://SpacesStore/14d5efac-a700-4c6a-a4c9-769e1c772848_fr_1.0_rendition

Authors
Keith McCarthy
Principal, Kroll
keith.mccarthy@kroll.com

Paul Nash
Associate Managing Director, Kroll
paul.nash@kroll.com

It is good to talk

There is increasing international cooperation in the fight against financial crime – and increasing expectations that businesses play their part.

Information and intelligence sharing between law-enforcement authorities and financial regulators has improved significantly in recent years. That's true both domestically and, perhaps more significantly, internationally.

The channels are both formal and informal. The latter are used most often early on in investigations, with informal discussions helping overseas agencies navigate the legal and administrative requirements to request information or push for action. The range of formal mechanism and tools for cooperation, meanwhile, has expanded, perhaps most significantly in tax evasion: Bilateral tax information exchange agreements (TIEAs) are widespread and used regularly, while the Organisation for Economic Co-operation and Development's (OECD) Common Reporting Standard allows tax information to be shared automatically.

Even in bribery and corruption, though, where cross-border cooperation is frequently used, we see improvements: In France, for example, which has long been criticised for a lack of enforcement by the OECD and others, Sapin II has brought the law into line with the likes of Britain and the U.S. The new anti-corruption agency (Agence Française Anti-Corruption) is now considered a serious partner in the fight against corruption and is actively liaising with its overseas counterparts as a result.

This increased cooperation is evidenced by a joint U.S. and French bribery resolution announced in early June 2018 that they had agreed separate deferred prosecution agreements (DPAs) totalling US$585 million with Société Générale in relation to allegations that the bank's executives bribed officials in Libya's development fund.

There are, of course, still barriers. Most obviously, politics plays a role, and the sharing of information and cooperation between countries suffers when diplomatic relationships break down. More commonly, the issue is simply one of resources. Where multiple jurisdictions are involved in building a case against an individual or business, the ability to do so – and the speed with which it can be done – depends heavily on the capabilities of the agencies involved. These continue to vary widely, particularly between the developed and developing world.

Nevertheless, the overall trend is towards a greater willingness and ability for regulators and law enforcement agencies to work together to tackle financial crime.

Growing expectations

The increased sharing of information is not limited to state agencies, however; it increasingly involves private enterprise, too. The Joint Money Laundering Intelligence Taskforce (JMLIT) set up by the UK in 2016 to tackle money laundering is a good example, bringing together more than 40 UK and international banks, the British Bankers Association and law enforcement agencies.

The initiative reflects an increasing recognition on the part of law enforcement that sharing focused intelligence with banks and others can help increase its understanding of the methods being used in financial crime. It is a two-way street, however, and the desire to cooperate with the private sector comes with greater expectations in terms of the standards of governance and recordkeeping within those businesses. And increasingly this is an obligation.

Again, it is efforts to tackle tax evasion that provide probably the best examples. In particular, the UK's Criminal Finance Act last year introduced strict liability for organisations failing to put in place reasonable procedures to prevent the facilitation of tax evasion directly by the organisation or by an "associated person".

The Act introduces the prospect of unlimited fines, and, critically, even if the offence is in another jurisdiction, it may still be pursued in the UK. Firms therefore need to ensure they have the proper records, due diligence, governance and compliance systems in place to prevent tax evasion and other financial crimes – not just so they can help UK authorities and its foreign partners get the information they need, but also to avoid prosecution themselves.

6.

The future in focus

The wheels of justice turn slowly, but grind exceedingly fine, goes the old saying. At least one part of that is true. Cases dating back to the financial crisis are only now, a decade on, finally over; cases relating to benchmark manipulation are largely complete, but some still drag on. Criminal trials are on-going.

The regulatory pipeline is long. As such, the best guide for the enforcement action we will be discussing in two or three years' time are the cases already beginning or in progress today. As we note elsewhere in this report (see John Byrne's article: Knowing the Rules), regulatory notices, announcements and speeches all offer powerful clues as to the big issues of tomorrow for enforcement, too. Already in the first half of 2018, we see some consistent trends with previous years in the areas of actions against firms for failings relating to firm management (corporate governance), AML, regulatory reporting and conduct of business such as mis-selling and suitability, disclosures to clients and overcharging.

At least some of what we are likely to see, therefore, should not come as a surprise. More than once, we have noted that a rise in action against individuals seems likely, not just in the UK and Hong Kong where new regimes have been introduced, but worldwide. Regulators are talking much more about holding individuals to account. It would be surprising if action did not follow.

Data demands

Developments in technology loom large. The demands around GDPR in Europe have received extensive coverage; the increasing focus on cybersecurity by global financial regulators is also well recognised.

There are a couple of related issues less commented on, however. One is the challenge new – and not so new – presented by communications channels. Last year saw the FCA fine an investment banker for sharing confidential

information on WhatsApp[68]. That raises interesting questions as to if (and how) firms should be monitoring employees' use of social media and external electronic communications platforms. Anecdotally, in some jurisdictions, communication platforms like WhatsApp and Telegraph are practically the business communication channel of choice precisely because they are completely private and fully encrypted.

The second issue is the increased opportunity that new technologies bring to old disciplines. Regulatory reporting is likely to see a renewed focus. This reflects both the increased ability of firms to capture and share much more of their data and the value it can then deliver to regulators through the use of sophisticated analytical tools.

Many regulators have invested heavily in systems and people to be able to use the data from these reports to understand market activity better and identify risks and abuses. Their ability to do so is severely compromised if the data is poor: Garbage in, garbage out.

Regulators are therefore going to be increasingly impatient with firms whose reporting is inaccurate, in the wrong form or untimely.

A long road back

A decade on from the global financial crisis, trust in the financial services industry is still proving slow and difficult to restore.[69] The message that public enforcement action sends, that wrongdoers will

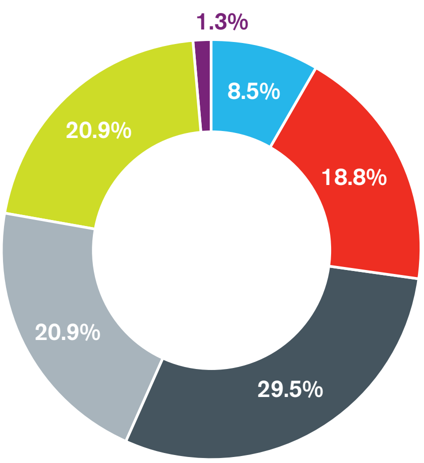
69. https://www.fca.org.uk/news/press-releases/fine-former-investment-banker-sharing-confidential-information-whatsap

be held to account, undoubtedly has an important role to play in restoring that trust. So, should we worry if the number of cases and fine amounts fall? As ever, the impact of enforcement activity will be as much down to how regulators act as to what they act against. The regulators' drive to individual accountability really therefore, has to be seen in enforcement outcomes against senior individuals.

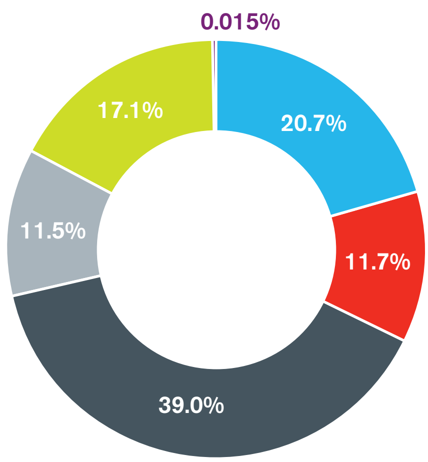
This focus on individual accountability is unlikely to be entirely welcomed by everyone in the industry, but it should be. At least part of the lack of trust in financial services seems to result from the perception that those responsible for the financial crisis were never properly held to account.

Abuses and misconduct that are left unaddressed are not simply forgotten, and failing to deal firmly and publicly with the perpetrators can do lasting damage to the industry. The enforcement machine may sometimes turn slowly but turn it must. The outcomes regulators produce are some of the most tangible ways in which regulators can demonstrate that they are serious about protecting investors and consumers. However long the regulatory pipeline, if it never brings closure, memories can be longer still.

FREQUENCY OF PENALTIES GLOBALLY BY REGULATORY CATEGORY 1H 2018



GLOBAL PENALTY AMOUNTS BY REGULATORY CATEGORY 1H 2018



- Market Conduct
- Financial Crime
- Conduct of Business Obligations
- Regulatory Obligations
- Corporate Governance
- Privacy and Cybersecurity

70. http://cms.edelman.com/sites/default/files/2018-03/Edelman_Trust_Barometer_Financial_Services_2018.pdf

Appendix

REGULATORS INCLUDED IN THE RESEARCH

United States	Consumer Financial Protection Bureau, U.S. (CFPB)
	Commodity Futures Trading Commission (CFTC)
	Federal Deposit Insurance Corporation (FDI)
	Board of Governors of the Federal Reserve System (FED)
	Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac)
	Federal Deposit Insurance Corporation (FDIC)
	Federal Energy Regulatory Commission (FERC)
	Federal Housing Finance Agency (FHFA)
	Financial Industry Regulatory Authority (FINRA)
	Financial Crimes Enforcement Network (FinCEN)
	The National Credit Union Administration (NCUA)
	Office of the Comptroller of the Currency (OCC)
	Public Company Accounting Oversight Board (PCAOB)
	Securities and Exchange Commission (SEC)
United States cont...	U.S. Department of Housing and Urban Development (HUD)
	U.S. Department of Justice
	U.S. Department of Labor
	20 State Attorneys
	16 State Departments

United Kingdom	Financial Conduct Authority (FCA)
	Financial Reporting Council (FRC)
	Information Commissioner's Office (ICO)
	Prudential Regulation Authority (PRA)
	Serious Fraud Office (SFO)
Europe (ex UK)	European Commission (EC) - Europe
	Financial Market Supervisory Authority (FINMA) – Switzerland
	Federal Financial Supervisory Authority (BaFin) – Germany
	Comisión Nacional del Mercado de Valores (CNMV) – Spain
	European Central Bank - European Union
	Autorité de Contrôle Prudentiel et de Résolution (ACPR) - France
	Autorité des marchés financiers (AMF) – France
	Central Bank of Ireland (CBI) – Ireland
	Data Protection Commission (DPC) – Ireland
	Irish Financial Services Regulatory Authority (IFSRA) – Ireland
	Autoriteit Financiële Markten (AFM) – The Netherlands
	De Nederlandsche Bank N.V (DNB) - The Netherlands
	Finansinspektionen (FI) - Sweden
	Swiss Financial Market Supervisory Authority (FINMA) - Switzerland
Asia Pacific	Australian Securities and Investments Commission (ASIC) – Australia
	Australian Transaction Reports and Analysis Centre (AUSTRAC) – Australia
	Securities & Futures Commission (SFC) – Hong Kong
	Monetary Authority of Singapore (MAS) – Singapore

2. REGULATORY CATEGORY DESCRIPTIONS

Market Conduct
This regulatory theme covers issues related to market integrity, including market manipulation, insider trading, short selling and related violations, disclosures, anti-competitive behaviour, trading errors, breach of takeover rules, illegal activity and misuse of non-public information.

Financial Crime
This regulatory theme covers issues related to fraud, money laundering and bribery and corruption, including CDD/KYC, sanctions, and tax evasion.

Conduct of Business Obligations
This regulatory theme covers issues related to the responsibility to treat customers fairly and to safeguard client assets, including arrears handling, client asset/cash, client data/confidentiality, client orders execution, complaint handling, conflict of interest, customer authorisation, disclosures and communications to the client, mis-selling and suitability, overcharging, unfair contracts, unfair treatment.

Regulatory Obligations
This regulatory theme covers issues related to the interaction between a regulator and a supervised person or firm, including capital and liquidity, gatekeeper failures, individual misconduct, industry threshold conditions, non-cooperation with the regulator, record keeping, regulatory reporting, unlicensed activity, stakeholder duties, and other regulatory obligations.

Corporate Governance and Oversight
This regulatory theme covers issues related to senior management, including firm management, stakeholder duties, and corporate governance.

Privacy and Cybersecurity
This regulatory theme covers issues related to data protection/privacy, cybersecurity and IT resilience.

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CONTACTS

Julian Korek
Managing Director
julian.korek@duffandphelps.com
+44 (0)20 7089 0800

Nick Bayley
Managing Director
nick.bayley@duffandphelps.com
+44 (0)20 7089 4933

Chris Lombardy
Managing Director
chris.lombardy@duffandphelps.com
+1 646 867 7824

Monique Melis
Managing Director
monique.melis@duffandphelps.com
+44 (0)20 7089 0820

Nick Inman
Managing Director
nick.inman@duffandphelps.com
+852 2281 0130

www.corlytics.com

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