

An aerial night view of a city, likely London, showing a mix of modern and classical architecture. A prominent feature is a modern, curved building with a blue and white facade, illuminated from within. Other buildings are lit up with warm yellow lights, and the streets are visible with some traffic. A yellow banner is overlaid on the left side of the image.

**What the  
FCA's 2018/19  
Business Plan  
means for  
your firm**



Building a better  
working world



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The FCA's attention for 2018/19 – as for many firms – will major on Brexit, but firms will also need to focus on core priorities, such as culture, cyber, innovation and financial crime, as well as address emerging concerns in pensions advice and high-cost credit.

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■ Section 1

# Executive summary

# Executive summary



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This year, the Financial Conduct Authority's (FCA) annual Business Plan and Sector Views represent a tough balancing act between dealing with Brexit and addressing core priorities. Unsurprisingly, considerable FCA time and resource will be dedicated to EU withdrawal activities. However, this in no way diminishes the expectation that firms should continue to demonstrate that culture and good conduct are well embedded, regardless of the level of regulatory intervention.

Firms should therefore view the topics included within the Business Plan with a keen resolve, given the level of scrutiny involved in their selection. Many of the items are not new, and this reflects the FCA's ongoing commitment to creating a fair, transparent and well-functioning financial services market for all consumers.

New priorities in this plan	What firms can expect
Long term savings, pensions, and intergenerational differences	<ul style="list-style-type: none"> <li>▶ Focus on long term customer outcomes, specifically at, and in the build up to, retirement</li> <li>▶ Further reviews of the suitability of pensions transfer advice</li> <li>▶ Identification of potential weaknesses in the non-workplace pensions and savings market</li> </ul>
High-cost credit	<ul style="list-style-type: none"> <li>▶ Exploration of alternatives to high-cost credit</li> <li>▶ Focus is moving from payday lending to mainstream products (e.g., overdrafts) and specific specialist areas (e.g., catalogue credit)</li> </ul>

Continuing priorities	What firms can expect
Firm's culture and governance	<ul style="list-style-type: none"> <li>▶ Further extension of Senior Managers and Certification Regime (SM&amp;CR) across the industry</li> <li>▶ Focus on firm's remuneration arrangements, particularly in the consumer credit market and on firms that are not subject to the FCA remuneration codes</li> </ul>
Financial crime and anti-money laundering (AML)	<ul style="list-style-type: none"> <li>▶ Enhanced AML and Counter-Terrorist Financing (CTF) focus in capital markets and e-money sectors</li> <li>▶ Tackling of increasingly sophisticated scams in pensions and investments</li> </ul>
Data security, resilience and outsourcing	<ul style="list-style-type: none"> <li>▶ Proportionate supervision over high and lower-impact firms</li> <li>▶ Thematic and firm specific reviews of Third Party Risk Management (TPRM)</li> </ul>
Innovation, big data, technology and competition	<ul style="list-style-type: none"> <li>▶ Greater use of technology by the FCA to aid supervision</li> <li>▶ Outputs delivered from the review into the digitalisation of retail banking models</li> </ul>
Treatment of existing customers	<ul style="list-style-type: none"> <li>▶ Focus shifting to General Insurance (GI) and retail banking, including:                             <ul style="list-style-type: none"> <li>▶ Review of pricing practices in GI</li> <li>▶ Improving competition in cash savings and current account markets</li> </ul> </li> </ul>

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“This year is a challenging one for the regulator. To achieve our priorities, as well as plan for EU withdrawal, while continuing to deliver our core regulatory activities effectively, will require us to use our resources efficiently and flexibly”

**Charles Randell**  
Chair, FCA

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In addition to its cross-sector priorities, the FCA outlines key sector focus areas. The FCA's sector priorities are again supported by its separate publication 'Sector Views', which provides an insight into demographic and economic changes relevant for each industry, changes in consumer behaviour and specific areas of concern. Brexit, of course, features heavily and most prominently across investment management, wholesale and general insurance sectors.

#### **Banking and capital markets**

Following the implementation of the Markets in Financial Instruments Directive (MiFID II) and the new IPO rules, wholesale banks should focus on embedding these programmes, along with assessing the impact of industry codes of conduct in unregulated markets and developing transition plans from LIBOR to alternative rates.

Regulatory change and evolving technology is driving the emergence of new models in retail lending and banking. Attention has turned to improving the performance of the debt management sector, for example through the use of data analytics to identify financial difficulty.

Following the regulatory change associated with the introduction of Open Banking and PSD2, retail banks should focus on measuring customer outcomes and how this challenges the traditional value chain. Firms should balance new opportunities for growth with the emerging risks that arise from working with third parties and the challenges of maintaining accurate customer data.

#### **Wealth and asset management**

The extension of SM&CR impacts a number of wealth and asset management firms, particularly complex global firms with business models that rely heavily on delegation and outsourcing.

Investment managers have seen significant regulatory changes through the introduction of Packaged Retail and Insurance-based Investment Products (PRIIPs) regulation, MiFID II and latterly through the Asset Management Market Study (AMMS). The AMMS has seen a shift in approach towards treating Authorised Fund Managers as agents of the investors in their funds, not just product providers. More than ever, investment managers will need to be accountable to their underlying beneficiaries to deliver value that is not just limited to price.

Delivering value is a theme that carries into distribution of retail investments and the FCA highlights the growth of platforms. A further market study, reporting in summer 2018, will address any concerns that these platforms are not doing enough to secure good outcomes for consumers.

#### **Insurance and pensions**

Demands on insurers and pensions providers continue to be wide ranging and complex. The FCA has set out a broad agenda encompassing the Retirement Outcomes Review, the effectiveness of Independent Governance Committees (IGCs), implementation of the Insurance Distribution Directive (IDD), assessment of GI pricing practices and diagnostic work relating to long-term savings and non-work place pensions. This is coupled with the renewed importance of ensuring operational resilience given the array of legacy systems in the sector.





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“Brexit means the FCA faces a challenging year. It faces new responsibilities and complications that will impact all areas of its work. We are pleased to see the FCA confronting this positively and transparently.”

**John Cole**

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## EU withdrawal

The FCA's Business Plan has been considerably impacted by Brexit. We welcome its transparency in reconciling its ongoing priorities with the need to dedicate a high level of resource to EU withdrawal. Brexit will have a significant effect on firms and the overarching regulatory environment.


Much of the immediate focus of the industry has been planning for a 'cliff edge' in March 2019. However, the political agreement between the UK and EU on a Brexit implementation period, coupled with the Government's commitment to a temporary licencing regime for European Economic Area (EEA) firms if necessary, has provided the FCA with a small amount of breathing space. Firms have been told that they need not apply for new authorisations at this stage for activity currently passported into the UK. If the implementation period is ratified, EU law should remain applicable within the UK until the end of 2020 and most significantly, maintaining the current authorisation regime and passporting rights between the UK and EU.

There is still, however, much to consider. Firstly, the implementation agreement is still not confirmed, and may not be for some time. The industry has not yet seen any recognition of the transition period from EU authorities. This means UK firms operating under passports into the EU are being asked to continue planning for all contingencies including a no-deal scenario. This leaves the UK with an asymmetric approach, providing EU-authorized firms operating under passports into the UK additional time, whilst pushing UK-authorized firms operating in the EU to continue targeting March 2019 for implementation. Firms may find themselves struggling to satisfy the demands of both their UK and EU27 regulators.

In addition, the Government will need significant technical assistance in its negotiations with the EU and other countries on potential free trade agreements, along with advice on legislation regarding the removal of the UK from the EU. The FCA Handbook will need to be amended and reviewed in light of the legislative changes. Focus must also turn to delivering good cooperation agreements with EU authorities to ensure transparency during the implementation period. Furthermore, importance should be placed upon supporting any long-term reciprocal access or regulatory model that the UK and EU consider. We are pleased to see the FCA emphasising the importance of close cooperation with both the EU and global authorities.

The additional costs of Brexit mean adjustment to the FCA's budget. They have identified £30 million of additional Brexit costs, of which £19 million will come from reallocating existing funds and reserves. This will require £11 million of new money. The FCA has proposed that £5 million of this should come from additional fees charged to firms, with a focus on those most likely to be affected by EU withdrawal. The remaining £6 million will be funded from specific firms so that the costs of work associated with on-shoring credit rating agencies and trade repositories, will be recovered once final costs and the number of firms affected have been identified. Firms may wish to seek further clarity on how this might impact them.

Planning and resourcing strategies under Brexit uncertainty will remain challenging, particularly when reviewed alongside the FCA's other priorities. Firms will need to balance these multi-dimensional agendas against their business priorities.



■ Section 2

# EY thematic cross-sector insights

Firms' culture and governance

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Financial crime (fraud and scams) and anti-money laundering (AML)

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Data security, resilience and outsourcing

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Innovation, big data, technology and competition

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Treatment of existing customers

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Long-term savings and pensions and intergenerational differences

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High-cost credit





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## Firms' culture and governance

Through extending the scope of SM&CR to cover all firms, the FCA hopes to achieve increased transparency and greater clarity relating to accountability and responsibility. In addition, the application of conduct rules and the requirement for firms to continually assess a larger population of employees as fit and proper should drive better behaviours across the industry. The desired result being better treatment of consumers through a decreased risk of mis-selling and a better quality of service.

**“Effective governance requires individual accountability for outcomes, transparent decision making and diversity of thought. The embedding and extension of the SM&CR across the industry provides the basis against which to assess customer outcomes and culture.”**

**Samantha Carruthers, EY Retail Banking and Wealth Management**

### EY summary insights on these issues

#### Extension of Certification Regime (CR) to insurers

Whilst insurers will be familiar with the senior manager requirements under the SM&CR, the Certification Regime will be new for them. The regime is due to start for insurers on 10 December 2018.

#### Extension of SM&CR to solo regulated firms

2018 will also see the publication of final rules for the extension of SM&CR to solo regulated firms including insurance brokers and Authorised Fund Managers (AFMs). This is seen as a potential remedy to governance findings in the FCA's Asset Management Market Study.

#### Whistleblowing

A focus on whistleblowing as a way in which to monitor a firm's culture was highlighted in the Business Plan along with the FCA's commitment to provide whistleblowers anonymity.

#### Remuneration

The FCA expects firms to be able to demonstrate that their remuneration approach is not resulting in harm to consumers, with their focus turning to those that are not currently subject to its remuneration codes, e.g., consumer credit firms.

#### Public register

In 2017, the FCA proposed that under SM&CR only approved senior managers will be included in the Financial Services Register. In line with the feedback, the FCA plan to consult on policy proposals to introduce a public register.

### What this means for your firm

Setting the parameters for those who pose 'significant harm' is critical. Our experience in banking shows that a timely start of the CR programme is key, given the level of communication, challenge, multifunctional collaboration and board input. In addition, insurers will need to:

- ▶ Revise their fit and proper framework
- ▶ Deliver conduct rules training
- ▶ Develop the certification process, including embedding of ongoing monitoring programmes

The delay of policy statements should not stop firms from starting their change projects, to ensure effective implementation. Individuals across solo regulated firms, including insurance brokers and AFMs, will need robust communications and training plans.

Firms need to review and address gaps in current procedures and channels. Any improvements should demonstrate a change in culture and behaviours.

Firms, and accountable individuals not currently subject to remuneration codes, should consider whether their existing schemes support the code. Compliance to these codes should be overseen by remuneration committees.

If a public register is established, the onus is likely to remain on firms to own and manage the fitness and propriety of their staff. Hence, they should continue to implement certification processes and programmes to monitor compliance with conduct rules.



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## Financial crime (fraud and scams) and anti-money laundering (AML)

The regulators drive for the use of advancing technologies in financial crime prevention, as well as risk assessment in capital markets and e-money, will play a significant part in enhancing the integrity of the UK financial system whilst supporting healthy competition. The FCA also expects consumers to see a direct benefit from the ScamSmart campaign, which aims to empower them with the knowledge to protect themselves from fraud and scams.

“The FCA is championing RegTech in the fight against financial crime through the reduction of operational costs and improving data analytics to target criminal behaviour, focusing in the near-term on capital markets. EY is delighted to host the FCA’s TechSprint in May which will explore use cases.”

**Debbie Ward, EY Financial Crime**

### EY summary insights on these issues

#### Money Laundering (ML)

The FCA has reiterated the increasing risk of ML through capital markets, which is also highlighted in the 2017 National Risk Assessment. It is seeking to determine the extent of the issue, as well as assessing ML and Counter-Terrorist Financing (CTF) risks in the e-money sector.

#### Innovation opportunities

Through innovative technology solutions, the FCA will be exploring opportunities to enhance firms’ financial crime controls. It is convening an international TechSprint to assess the opportunities in this area.

#### Fraud and scams

The FCA continues to focus on the protection of consumers from fraud and scams through its ScamSmart campaign, particularly highlighting the risks of pension and investment fraud. It will work with The Pensions Regulator to deliver an awareness campaign to tackle these types of scams.

#### EU withdrawal

Depending on the transition agreed and the UK’s appetite to remain aligned to EU legislation, the UK adoption of future AML and CTF legislation emanating from the EU could be impacted, particularly amendments to the Fourth Anti-Money Laundering Directive – 4AMLD (now ‘5AMLD’). Similarly, there could be an impact on the directive on countering ML by criminal law.

### What this means for your firm

Firms in the capital markets and e-money sector should anticipate enhanced AML and CTF regulatory focus, and assess the robustness of existing controls to mitigate associated risks.

Firms should explore new technologies to achieve cost efficiencies and improve the quality of AML, CTF and sanctions risk management.

Firms are able to gain cost efficiencies using artificial intelligence and machine learning to improve transaction monitoring, outsource arrangements, and change the way in which KYC is conducted via use of automation.

In light of the FCA’s focus on pensions and investment fraud, firms should ensure that these risks are appropriately considered in their business risk assessments.

Firms should monitor communications regarding the implementation of EU AML and CTF legislation post-Brexit and assess any gaps in control frameworks against changes in the two new directives. In particular, the changes to enhanced due diligence and the proposed change in the definition of ML should be assessed.





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## Data security, resilience and outsourcing

As a result of its push for increased resilience and transparency through independent assurance testing, the FCA expects the industry will see both reduced disruption to critical services and decreased risk of personal data loss.

This regulatory focus supports mechanisms such as GDPR, empowering consumers to take control of their digital identity and choose financial service providers on the basis of real and independently verified indicators of service quality.

**“The FCA’s Business Plan outlines plans to strengthen assessments on ‘high-impact’ firms and shine a light on firms of lower impact. Plans are in motion to gain transparency over industry-wide third and fourth party concentration risk.”**

**Steve Holt, EY IT and Cyber Risk**

### EY summary insights on these issues

#### Operational Resilience (OR)

OR will continue to be a dominant theme for the FCA in the foreseeable future. The Prudential Regulation Authority (PRA) has also recently identified OR as a priority risk. ‘Lower impact’ firms will be subject to heightened regulatory scrutiny via sector-specific thematic reviews, a move consistent with the FCA’s strengthened supervision of higher-risk institutions.

#### Service quality data

To help determine consumer understanding of bank’s resilience, the FCA expects banks to publish service quality data on technology and resilience issues from August 2018, as per the Competition and Markets Authority’s recommendations. We also expect greater coordination between regulators locally and globally on OR.

#### Third Party Risk Management (TPRM)

There will be a greater focus on TPRM this year as the FCA seeks to conduct proactive supervision, both thematic and firm specific, across the industry. We expect systemic and concentration risks, along with an understanding of the fourth-party landscape, to be leading sub-themes this year.

### What this means for your firm

There will be no ‘jurisdictional hiding places’ for high or low impact firms as regulatory coordination is enhanced. Firms require clear risk appetite definitions, strong governance, direction and accountability as well as clear regulatory reporting channels.

The finance industry’s recording and reporting of resilience KPIs are generally immature. Banks need to develop a framework and metrics to monitor and report the resilience of critical processes and systems.

The industry should drive the use of utility-type structures to improve the standards and transparency of TPRM in a cost-optimised way. The EY TPRM survey\* noted that 6 out of 10 FS organisations are considering the use of TPRM utilities.

\*Third Party Risk Management Survey – To be published Spring 2018



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## Innovation, big data, technology and competition

The FCA's automation and efficiency drive, in combination with Open Banking, is supportive of new digital services suited to current consumer lifestyles such as app-centric banking and improvements to existing products that provide finance e.g., enhanced underwriting. The FCA is also conscious that these initiatives may introduce new areas of risk which require ongoing monitoring and management, such as the appropriate use of data.

**"As Open Banking APIs are developed, it is pleasing to see the FCA tackle the topic of data head-on, recognising the value it can bring to consumers and the need for protection from authorised firms to ensure that consumer propositions are secure and simple to use."**

**Imran Gulamhuseinwala OBE, EY Global FinTech Lead**

### EY summary insights on these issues

#### Big data and automation

The FCA continues to lead the global charge on innovation in financial services. In particular, it is focusing on increased use of big data and automation, recognising both potential opportunities and threats posed.

#### Retail banking strategic review

The FCA will also consider the effects of emerging and traditional retail banking business models. Its review will evaluate the rise of digital channels against the fall of branch banking. A key output will consider how competition, conduct and consumer rights will be impacted in the future.

#### Regulatory Technology (RegTech)

There is a drive to use RegTech to create efficiencies in regulatory reporting and oversight. The FCA is testing automated reporting and will experiment with supervisory tools using natural language processing and semantic detection, as well as employing machine learning to automate the detection of false advertising and unauthorised online activity.

#### Global regulatory sandbox

The sandbox allows testing of innovative business models in a controlled environment and has been recognised internationally as a considerable success. After consultation across the financial services industry, the FCA will be adding an international element to this initiative.

#### Cryptocurrencies

Although broadly outside its regulatory perimeter, the FCA will be considerate of the impact of cryptocurrencies and technologies on consumers, particularly the risks associated with Initial Crypto Offerings. These risks and others will be further explored through a regulatory taskforce comprising of the FCA, the Bank of England and the Treasury.

### What this means for your firm

Firms will need to demonstrate robust governance and controls around the application of these technologies. Auditability of decisions made by algorithms is a focus area.

Assuring quality customer outcomes through digital services has been challenging. Firms should investigate how new products and services that record all customer interactions within digital channels can help.

Machine learning, robotics and digitalisation can create efficiencies across many manual processes. Firms should consider how using these technologies can support their own reporting and supervision processes.

The new global sandbox offers the opportunity for firms to test their offerings across multiple different jurisdictions, thus facilitating scalability.

Those involved in distributed ledger and cryptocurrency, particularly firms packaging cryptocurrency as a form of investment, should consider and prepare for the potential impacts of greater regulation on their industries.





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## Treatment of existing customers

Concerns over the way existing customers are treated by the industry continues to direct focus in this area. Greater transparency around product features, performance and costs will help consumers to understand the value they are receiving from their insurance and banking products.

**“The FCA continues to look at the treatment of long-standing customers, extending its focus into general insurance and retail banking. Firms should be ready for the challenge of demonstrating that their existing customers don’t receive a poor deal compared with new customers.”**

**Steve Southall, EY Insurance**

### EY summary insights on these issues

#### **Treatment of existing customers in general insurance and retail banking**

The FCA’s focus on existing customers has shifted from the life insurance sector to general insurance and retail banks. The aim is to ensure that existing customers are not treated less favourably than new customers. The FCA’s conclusion on pricing practices in retail general insurance, and its decision on whether to be more interventionist, will be of interest to insurers and the wider financial services industry.

#### **Claims Management Companies (CMCs)**

As it prepares to regulate CMCs, the FCA will look at whether inefficient practice is leading to the inflation of motor claims, thus bringing this area of the insurance value chain under greater regulatory scrutiny.

#### **Competition in the current account market**

The FCA is serious about increasing competition in the current account market. Firms should prepare to share product features in a standardised way so that existing customers can easily compare the offerings of different market providers.

### What this means for your firm

General insurers should review their treatment of existing customers and prepare for further scrutiny of their pricing strategies, policies, systems, use of data, and governance of their pricing frameworks.

As CMCs prepare for regulation, insurers and brokers should also consider FCA concerns over the claims-handling process. Referrals, volume discounts and other practices should be assessed for fair customer outcomes.

Incumbent firms could be competitively disadvantaged by new entrants with simpler product features and lower overhead costs. This will be more compelling now that overdraft fees and product features appear on price comparison websites.



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## Long-term savings and pensions and intergenerational differences

Changes to pension freedoms, auto-enrolment, and sociodemographic changes call for consumers to take greater responsibility for a widening array of long term financial security options. The FCA has shown growing concern that this in turn may be causing adverse consumer outcomes.

The regulator is initiating more specific retirement remedies, and it may intervene heavily in areas such as pension transfers. The result could lead to improvements to industry-wide treatment of long-term savings and pension customers.

**“The FCA’s concerns on long-term savings and pensions are no surprise, and are the culmination of several years of review and diagnostic activity. Firms should be ready to demonstrate that they are delivering the right outcomes for their customers, and can continue to do so.”**

**James Tufts, EY Life and Pensions**

### EY summary insights on these issues

#### Poor practices in long-term savings and pensions

The FCA continues to address the impact of demographic and social changes on longer term customer outcomes, with a range of ongoing initiatives and a willingness to intervene where it sees poor practice. The FCA has taken a broad view of the risks across these markets, including looking at areas which may come under future scrutiny through its refreshed pension strategy.

#### Retirement Outcomes Review and pension transfers

The Retirement Outcomes Review will conclude this year, bringing together over two years of the FCA’s review and diagnostic activity on the impact of pension freedoms. This could represent a critical turning point for the industry.

The FCA’s ‘extreme concern’ regarding the potential exploitation of consumers who lack pension knowledge is a reminder that the regulator will intervene where it fears there may be adverse consumer outcomes in relation to pension transfer practices.

#### Non-work place pensions

Additional research and diagnostic work is also underway on the levels of long-term savings and non-workplace pensions, potentially extending the FCA’s conduct focus across the sector. The regulator will look at charges, barriers to customer switching, and impact on competition and customer outcomes. These themes have been a feature of previous FCA reviews on the sector.

### What this means for your firm

The FCA’s activities continue to build on previous years’ thematic and supervisory reviews into poor practices in the long-term savings and pensions markets. Firms should be ready to demonstrate solid progress against these important initiatives.

Firms should be ready to meet this challenge which may include consideration of proactive customer rectification programmes.

Firms should be proactively engaging with these reviews to anticipate the likely areas of weakness in business processes, and how they can be addressed.





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## High-cost credit

The FCA's goal is to encourage those products with the most detrimental pricing structures to be re-fashioned or driven out of the market. Achieving this regulatory aim will be particularly beneficial to the most vulnerable customer groups.

Alternatives to High-Cost Short-Term Credit (HCSTC) will emerge during 2018, but regulators and the industry should be mindful of the potential impacts for free banking. They should also be aware of the models required for customers with lower credit ratings and how changes to these could impact accessibility to credit.

**“We are pleased to see increased attention on high-cost credit, supporting the FCA's focus on ensuring markets and products work for the most vulnerable in society. Further remedies to the sector will need to balance fairer treatment with access to, and provision of, consumer credit, under evolving banking models.”**

**Sajedah Karim, EY Retail Banking and Wealth Management**

### EY summary insights on these issues

#### High-Cost Short-Term Credit (HCSTC)

The FCA is building on work already completed in the HCSTC sector. Additional intervention is expected this year, with an emphasis on finding alternatives to HCSTC for vulnerable customers.

#### Focus shift onto mainstream lending

Previously the FCA focused on more specialised markets (e.g., payday loans), reacting with enforcement actions and the high-profile price cap on HCSTC. Attention has shifted to other sectors, including mainstream lending – particularly overdrafts – where pricing structures can be opaque and can penalise specific customer cohorts.

#### Outcomes in specialised credit sectors

The FCA has also made clear that they will continue to seek better outcomes in other specialised sectors, including rent-to-own, home collected credit and catalogue credit. Focus areas across these sectors include transparency of fees and charges, and risks associated with rolling over loans and product add-ons.

### What this means for your firm

We expect firms to come under pressure to find alternatives to HCSTC. Those with expensive charging structures should expect to be subject to scrutiny and may wish to consider proactive review activity. The FCA has made it clear that current models are not appropriate, particularly for vulnerable customer groups.

Firms should review pricing structures for overdraft lending, including both authorised and unauthorised overdrafts. Consideration should be given to the existence of pricing cliffs, maximum charges and whether alternatives can be provided for consumer groups who are the most impacted.

Firms should consider the impact of any pricing changes ahead of the Strategic Review, with updates on this expected in Q2 of 2018.

Management information presented at decision-making forums should highlight consumer outcomes in relation to each of the FCA focus areas and how decisions are taken in response to outcomes.



■ Section 3

# EY industry sector insights

Wholesale financial markets

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Investment management

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Retail lending

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Pensions and retirement income

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Retail investments

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Retail banking

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General insurance and protection



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## Wholesale financial markets

**“An expanded regulatory perimeter, additional transaction-reporting requirements and increased experimentation with advanced analytics mean that wholesale firms’ control functions will need to evolve.”**

**Stuart Crotaz, EY Corporate and Investment Banking**

### EY summary insights on these issues

The Markets in Financial Instruments Directive (MiFID) II deadline has passed and the wholesale industry is in the validation phase. The regulator has signalled that it will take action around MiFID II, including the assessment of implementation efforts, particularly around the expansion of the transaction reporting regime. The focus will be on identifying potential misconduct within the fixed income, commodities and non-standard derivatives markets, with further supervisory work to be undertaken in the areas of best execution, research, Payment For Order Flow (PFOF) and conflicts of interest.

Significant structural changes to the wholesale market have also taken place in the form of new trading venues and limiting over-the-counter trades. The FCA will be closely monitoring the impact of these. In addition, the FCA highlights primary markets as an area where they will be monitoring compliance with new rules, including conflicts of interest.

The FCA has signified willingness to act outside of its regulatory perimeter, particularly where malpractice impacts on market integrity or the FCA’s objectives. To enforce conduct standards in unregulated markets, the FCA intends to recognise some industry codes of conduct and will be consulting on this. Expected examples of this include the FX Global Code and the Fixed Income and Currencies and Commodities (FICC) Markets Standards, which may lead to FCA action in these areas in later years.

In July 2017, Andrew Bailey announced that the FCA will not require banks to submit to LIBOR post 2021. This year’s plan sets out expectations for market participants that use LIBOR to actively prepare for the possibility that LIBOR will not be produced following this date.

The FCA also highlights the key risks and benefits of using technology within wholesale markets, such as AI, machine learning and algorithms. Firms should be evolving in their ability to identify and manage risks, including operational resilience, which derive from embedded technology solutions. One area of focus will be middleware, whereby key services or operations are outsourced to specialist firms to increase the cost efficiency of meeting regulatory requirements.

### What this means for your firm

Firms should continue to focus on responding to the evolving regulatory environment, including:

- ▶ Conducting MiFID II and IPO rules health checks in preparation for supervisory visits;
- ▶ Assessing which industry codes of conduct are relevant and how to meet their requirements;
- ▶ Assessing the impact of LIBOR and establishing a transition plan to alternative rates.

In addition, we expect a renewed focus on technology and innovation. Hence, firms should consider:

- ▶ How the FCA will use advanced analytics and prepare to respond to requests arising from this;
- ▶ How to understand the applicability of regulations to new products and services arising from FinTech and RegTech, including how to test them;
- ▶ How to increase the integrity and accuracy of data to support regulatory demands and transformation of control functions.





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## Investment management

“The FCA’s primary investment management focus remains unchanged, achieving the right outcomes for investors. As well as monitoring the effectiveness of significant regulations impacting investors (PRIIPs and MiFID II), the FCA activities will centre on value for money, governance, controls and fund liquidity management.”

**Uner Nabi, EY Wealth and Asset Management**

### EY summary insights on these issues

The investment management industry has seen significant regulatory change through the introduction of PRIIPs, MiFID II and latterly through the Asset Management Market Study (AMMS). The AMMS, in particular, has seen a shift in approach towards treating the Authorised Fund Managers (AFMs) as agents of the investors in their funds, not just product providers. More than ever, investment managers will need to be accountable to their underlying beneficiaries to deliver value that is not just limited to price.

Although reiterating the importance of a firm’s culture and governance in building public trust, the FCA has stipulated a step change for asset managers through the remedies announced following the AMMS. For example, AFM boards will now need at least two independent directors. In addition, the board must: conduct a value assessment for each fund against a non-exhaustive list of prescribed elements; conclude that each fund offers good value or take corrective action if it does not; and explain the assessment annually in a report made available to the public.

The FCA has acknowledged the rapid growth in the proportion of investor money that is passively managed, driven by the growth in exchanged traded funds (ETFs). The FCA plans to publish further research on this during 2018/19. In the meantime, MiFID II may act as a further growth driver for passives.

The extension of SM&CR significantly impacts investment management firms, particularly when considering the complexity of a global firm and business models that rely heavily on delegation and outsourcing.

### What this means for your firm

Investment managers should consider the rule changes following the AMMS at the same time as addressing the expectations from the FCA Business Plan. Firms should:

- ▶ Review their implementation of PRIIPs and MiFID II, ensuring effectiveness despite the ongoing uncertainties around cost disclosures
- ▶ Regularly assess the adequacy of governance and conduct arrangements
- ▶ Establish the required framework and processes to conduct the value assessments, related governance and disclosures required by AMMS
- ▶ Commence the process of making the necessary changes to fund boards
- ▶ Consider the ongoing viability of some share classes and where necessary, the funds themselves

Through these actions, investment managers will be able to comply with specific requirements and demonstrate the behaviours expected as good agents.

Firms should also learn from the implementation of SM&CR in the banking sector and plan now for its introduction during 2019.



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## Retail lending

“Regulatory change, evolving customer needs and rapidly developing technology are driving the emergence of new models in retail lending. When undertaken responsibly, this will lead to enhanced market resilience and opportunities for sustainable growth.”

**Jenny Clayton, EY Retail Banking and Wealth Management**

### EY summary insights on these issues

Market pressure driven by an increase in competition and consumer indebtedness will mean a challenging time for firms that are not prepared to adapt their approach to underwriting, the use of technology and product development. While opportunities for business growth are available, firms need to ensure their lending practices remain resilient to macro-economic events, and can evidence ongoing consumer affordability in line with their changing circumstances and needs.

The increasing proportion of consumers on lower or irregular incomes provide a challenge for industry underwriting practices. Our experience suggests that the product governance process is key: firms should understand who the relevant target consumer is and what good outcomes look like for them, as well as understand the risks, and identify the appropriate metrics required for ongoing monitoring and oversight. With this in place, firms can innovate with confidence.

Firms also need to evolve their arrears management practices. Data analytics can be used to better understand customer segments, such as identifying those at risk of financial difficulty, and intervene accordingly to improve consumer outcomes and capital provisioning requirements. Where debt management third parties are deployed, lenders should be mindful that they cannot discharge their regulatory obligations, and should closely consider the impact of the FCA’s Debt Management report findings on their business model.

Affordability for motor finance has been highlighted by the FCA but firms should also consider unfair contract terms, including onerous conditions on pricing and penalties. Finally, the Mortgage Market Study final report, due in Q4 of 2018, is expected to consider the impact on competition when lenders use accredited brokers. Remuneration models will be under scrutiny and the industry should expect this to also impact on conveyancer and surveyor panels, to assess whether these provide any discernible advantage to consumers.

### What this means for your firm

The FCA has stated that it will be using outcome indicators to assess areas of consumer harm such as affordability and suitability. Firms should be utilising customer data that is available to help identify market opportunities, predict customer affordability resilience and flag areas of customer vulnerability.

Firms should review their underwriting criteria and make alterations to capitalise on the growing market opportunity brought about by labour market changes in employment types and an aging population.



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## Pensions and retirement income

“The FCA’s focus on improving governance and value for money for customers through the remit of Independent Governance Committees, as well as its pension strategy re-fresh, demonstrates the high priority of this sector to its conduct objectives.”

**James Tufts, EY Life and Pensions**

### EY summary insights on these issues

The FCA’s focus on long-term savings and pensions as a cross-sector priority highlights the increasing significance and breadth of the issues in this area.

As well as the cross-sector activities including the Retirement Outcomes Review, pension transfers, and non-workplace pensions, the FCA continues its sector focus on potential conduct concerns arising from consumers contributing towards – and accessing – their retirement savings. This includes the role of Independent Governance Committees (IGCs) in improving governance and value for money and their remit beyond workplace pensions, as well as increased efforts to safeguard consumers against pension fraud and mis-selling. The FCA identified some positive findings relating to the role of IGCs for workplace schemes in its initial report in 2016, such as influencing reductions in costs and charges, and this current review will look to assess IGCs’ broader effectiveness.

Aside from its own activity, the FCA’s work with The Pensions Regulator on a joint pension strategy (including their joint call for input) is a welcome initiative to provide clarity on how the sector should be regulated following the significant market changes resulting from pension freedoms, auto-enrolment, and other changes. The FCA sees one of the biggest potential harms facing the sector as the prospect of consumers not having adequate levels of income to fund their retirement. Through its strategic re-fresh, the FCA is considering a broad range of factors across the full spectrum of accumulation through to decumulation, and where they (and The Pensions Regulator) may need to increase the scope of regulation. This could lead to further intervention on whether there is sufficient access to pensions, whether they are well funded and well run, and whether they offer good value for money to consumers.

### What this means for your firm

Firms in this sector face significant areas of regulatory intervention, driven by pension freedoms, auto-enrolment and social and demographic changes. It represents an opportunity to demonstrate how firms are responding to changes in consumer behaviours by delivering products that are appropriately targeted and bring value for money for consumers.

As well as the specific regulatory activity, the pension strategy review gives firms the opportunity to influence the FCA’s direction of travel and help set the regulatory approach in the sector for the next 5-10 years.





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## Retail investments

**“The Platforms Market Study, due in summer 2018, is likely to radically change the platforms market and firms need to proactively consider what changes to business models are necessary to survive and flourish.”**

**Simon Turner, EY Wealth and Asset Management**

### EY summary insights on these issues

The FCA recognise that the Retail Investment sector is critical in helping to improve the longer term financial health of consumers. The FCA's concerns have traditionally centred on the conduct of firms advising consumers on this journey, ensuring that advice offered leads to suitable investment products and services.

The FCA priorities maintain the regulator's intense focus and encouragingly, the FCA notes over 93%\* of the advice it reviewed last year was suitable and it plans to redirect its efforts towards advice on the purchase of complex investment products. Typically, such products are used by wealth managers to meet the needs of more sophisticated consumers, and firms should expect more intensive regulatory attention in the coming year.

Following the introduction of the Retail Distribution Review (RDR) rules in 2013, the number of firms providing investment advice has declined, and over the last few years the Government has encouraged the FCA to explore ways of closing the 'advice gap'. This includes consumers with small amounts to invest who find it challenging to access affordable advice. The Business Plan highlights the continued work of the Financial Advice Market Review (FAMR) and the FCA's continued support for the development of 'robo advice'. Robo advice uses technology to make cost effective advice more widely available and has the potential to allow low cost competitors to supply highly standardised services to retail investors.

A growing proportion of consumers prefer to make their own investment decisions, without advice. The FCA highlights the growth of retail investment platforms which provide services for these consumers. The Platform Market Study, reporting in summer 2018, will address concerns that these platforms are not doing enough to secure good outcomes for consumers. The FCA could reclassify some of the services provided by these platforms as advice rather than mere administration and as advisers, platforms would be under a duty to secure value for money for consumers. This work complements the new rules facing the manufacturers of investment products and will transform the business models of many wealth and investment management firms.

### What this means for your firm

The FCA's supervision teams will continue to conduct assessments across all categories of advice providers. Firms should look to match the FCA approach and proactively identify areas of concern.

Firms should embrace the role technical innovation has to play, which has the potential to transform both the method and availability of advice. Robo advice challenges the current model of bespoke, relatively high cost services and all firms should closely monitor the FCA's efforts in this area.

The Platforms Market Study may produce recommendations that radically change the business models of firms such as treating platforms as advisers or imposing a duty to secure value for money for consumers. Proactive work by firms may offer a competitive advantage.

\*The FCA Business Plan 2018/19



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## Retail banking

“Regulatory change and technology are fundamentally altering retail banking in terms of consumer behaviour, and how firms build competitive advantage. The FCA is focused on ensuring this innovation is positive for consumers.”

**Hamish Thomas, EY Payments**

### EY summary insights on these issues

The FCA views retail banking as the “gateway into financial services for most consumers”\*. The current evolution in retail banking will be felt across multiple sectors.

The trends identified by the FCA can be grouped into three main areas: regulatory change, opportunity from new technology and emerging risks.

Firms are working hard to embed and embrace large regulatory change programmes, including ring-fencing and the Second Payment Services Directive (PSD2). Increasingly, the FCA is not defining success as simply reaching a regulatory implementation milestone, but how it can be evidenced in terms of defined improvements for consumers. The specific outcomes they measure will be different in each case, but examples would include increased competition, expanded access to appropriate products for consumers, or showing a reduction in associated complaints.

Open Banking and PSD2 are causing a marked shift in retail banking relationships. The traditional value chain is becoming exposed, with a range of new entrants looking to carve out activities that are valuable to them. FinTech entrants may challenge for seemingly unprofitable activities, but in reality this offers them useful customer insights and information. The FCA will begin monitoring Account Information Service Providers and Payment Initiation Service Providers for the first time, as it aims to develop its understanding of these new business models.

While new products and delivery models may improve customer experience in the long run, the regulator also expects firms to exercise caution in not creating new opportunities for fraud or encouraging customers to make impulsive financial decisions. The continued move to online services puts vulnerable customers at risk of becoming further disconnected from the retail banking system, so it must be managed properly.

Increasingly, firms are being challenged on the accuracy of the customer information they hold and provide to others, such as to credit reference agencies. The FCA is concerned that inaccurate data may cause potential customers to be excluded from financial services.

### What this means for your firm

FinTech firms may find profitable opportunities in non-traditional customer segments, but often they require large data sets to make their analytics effective. Existing firms already hold this customer information, but it is often disjointed across legacy systems. Understanding where each organisation has difficulty allows them to select and utilise their most effective technology enablers. FinTech firms can be a strategic collaboration partner, not just a competitive threat.

Firms should ensure they understand not only their legal liability, but also any exposure to reputational damage, should something go wrong when working with third parties or new distribution channels.

\*The FCA Sector Views 2018



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## General insurance and protection

“With activity spanning across wholesale broking practices through to retail pricing and vulnerable customers, the FCA continues to drive a regulatory conduct programme that could have significant impact on the way GI firms do business in the market.”

**Steve Southall, EY Insurance**

### EY summary insights on these issues

Value has again been a consistent theme of FCA work in general insurance (GI) and protection in recent years and this is reflected in their plans for the sector for 2018/19. We believe attention this year will likely be focused on the FCA's conclusion to its first diagnostic review into GI pricing practices. Regardless of whether the FCA decides on a more interventionist approach, firms in the sector should prepare for further scrutiny of pricing strategies, governance and controls and how these are implemented in practice.

The FCA will continue with its substantial programme of activities in the sector, with reports on the wholesale insurance brokers study and the review of value in GI distribution chains. This is the third time that the FCA has looked at this area and we are likely to see recurring themes, such as oversight by principals, robustness of due diligence procedures and quality of management.

The review on access to travel insurance represents an opportunity for a collaborative approach across the industry to address the barriers vulnerable customers have faced in accessing this product at a reasonable price. The implementation of the Insurance Distribution Directive (IDD) in October 2018 will give the FCA further impetus to review and intervene where it sees issues with poor product design and communication. The FCA also highlights, in its view on the sector, the importance of operational resilience in the face of cyber-attacks, IT outages and loss of customer data – a challenge for many insurers due to the prevalence of legacy systems across their business.

### What this means for your firm

The 2018 interim report for the Wholesale Insurance Broker Market Study will be of considerable interest to a sector already impacted by Brexit and other disruptions, including the ongoing challenge of a prolonged low ratings environment. Firms should prepare for the results from the review of general insurance distribution chains, as the FCA is likely to expect swift action.

Some insurers' IDD programmes are already well advanced, however, the extension of the implementation date to October 2018 could result in a pause for breath. Firms should not lose sight of the remaining challenges they will need to meet ahead of IDD implementation. In anticipation of the GI pricing review, firms should assess the effectiveness of pricing strategies, policies, governance and controls.



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