HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

Baroness Kramer
House of Lords
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Dear Susan,

FINANCIAL SERVICES AND MARKETS BILL: POWERS OF THE FINANCIAL CONDUCT AUTHORITY IN RELATION TO FRAUD

Thank you for your contributions during the Grand Committee debates on the Financial Services and Markets Bill so far. During the debates on 30 January, I committed to write to you on the specifics of the Blackmore Bond case, as an example of the Financial Conduct Authority's (FCA's) powers and functions in relation to fraud, and how they relate to the regulatory perimeter. During the debate on 6 February, I committed to write to you on resourcing for anti-fraud work and enforcement in the FCA and the National Crime Agency (NCA).

Firstly, I would like to elaborate on my remarks during the debate on 6 February regarding the FCA's powers in relation to fraud. If fraud is committed by an authorised firm in the course of a regulated activity, or if it carries out a regulated activity without the correct authorisations, the FCA can take action against the firm on the basis of a breach of the FCA's rules, FSMA requirements, or under other legislation under which the FCA authorises certain firms. Where a firm is regulated under Part 4A of FSMA, if a senior manager within the firm is responsible for the fraud, or has culpably failed to prevent one occurring within the area of their responsibility, the FCA can also take action against that senior manager.

Where a firm is authorised for one activity, but is also carrying out an unregulated activity, and the fraud relates to that unregulated activity, the FCA's powers against the firm and any senior manager responsible for the fraud will depend on the specific details of the case in question and the type of firm. However, in most cases, in the case of a serious fraud the FCA is able to take regulatory action against the firm, on the basis that the firm does not meet the conditions for authorisation.

If a firm provides regulated products or services without being authorised (unless exempt) they may be carrying on unauthorised business in contravention of the "general prohibition" in section 19 of FSMA or they may be breaching an authorisation requirement of other legislation under which the FCA authorises firms. Much of the FCA's fraud pursuit work relates to scammers in this context.

The FCA does not have powers to investigate a firm that is unauthorised and not carrying out any regulated activities (unless, for example, that unauthorised person is carrying out market abuse, where the FCA has a specific role expressly set out in FSMA, or the misconduct otherwise falls within the FCA remit). In circumstances where problems fall outside FCA's statutory remit, the FCA assists other agencies and regulators wherever it can.

Regarding the specific case of Blackmore Bond, the firm was not authorised under FSMA and the issuance of its bonds was not a regulated activity for which it was required to be authorised.

The FCA did take action towards firms involved in the promotion of debt securities issued by Blackmore Bond. This is because, although the issuing of minibonds is not ordinarily a regulated activity, the promotion of such bonds may be regulated by the FCA, depending on the specific circumstances.

As an unauthorised firm, Blackmore could only communicate a financial promotion that was approved by an authorised person or within the scope of an exemption in the Financial Promotion Order 2005 (for example, there are exemptions for promotions to high net worth and sophisticated investors).

Consequently, the firms which approved the financial promotions used to market Blackmore Bond were authorised persons and the FCA was therefore able to investigate these firms, even though Blackmore Bond was not itself an authorised firm. The FCA took supervisory action against these authorised firms, and no further financial promotions were approved for Blackmore Bond after March 2019. In addition to its own actions against authorised firms, the FCA also assists other agencies and regulators where it can. In the case of Blackmore, the FCA passed relevant information to the City of London Police and liaised with the Insolvency Service.

Since the events of Blackmore Bond and London, Capital & Finance (LCF), the FCA has taken further action to protect consumers from the potential harms from investments in minibonds. In November 2019, the FCA announced a temporary ban of the promotion of high-risk 'speculative illiquid securities' to ordinary retail investors, which includes the type of minibonds sold by Blackmore and LCF. This took effect from 1 January 2020. The permanent ban and new rules were confirmed in December 2020 and took effect from 1 January 2021.

Furthermore, in response to the April 2021 consultation on the regulation of non-transferable debt securities (NTDS), the government has set out its intention to include NTDS, including minibonds, within the scope of the reformed Prospectus Regime. This would mean that issuers of minibonds would be required to offer their securities via a regulated platform when making offers over a certain threshold. These platforms will be regulated by the FCA, with offers subject to appropriate due diligence and disclosure. This will provide stronger protection for investors.

You also asked about the number of vacancies in the anti-fraud and enforcement divisions of the FCA. According to information provided by the FCA, from 1 January 2022 to 31 December 2022, the FCA's overall headcount increased by 12% in line with its strategic growth plans. The FCA expects to continue to expand its headcount steadily to meet a growing remit and to meet resource requirements, for example to deliver its role in building a regulatory framework tailored to the UK. Regarding your specific question, as at 10 February, the FCA had 85 vacancies in the Enforcement and Market Oversight Division, out of a total of 678 roles. The FCA is focused on filling all these vacancies in order to build capacity and resilience. This will enable the FCA to act faster against firms causing harm to consumers and markets.

You also asked about the number of staff focussed on anti-fraud matters in the NCA, and the NCA's budget for this work. The Government has invested £100m in the Fraud Reform Programme, part of which will go to the NCA to improve the UK law enforcement response to fraud. This investment will support the Agency to increase the size of operational teams dedicated to fraud; build new, multi-agency intelligence capabilities; and amplify more consistent messaging to the public. NCA capabilities and resources are focused on high priority operational demands across serious and organised crime threats, including several hundred NCA officers involved in responding to fraud.

I look forward to further discussing these issues throughout the passage of the Bill. I am copying this letter to all Peers who spoke during the debates, and I am placing a copy of this letter in the Library of the House.

Yours sincerely,

BARONESS PENN