FCA: On the wrong side of the argument?

By Caroline Binham and Jonathan Guthrie

After a Tory election victory, the tough approach of the chief executive of UK regulator FCA may be out of fashion
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ometime between the canon of lamb and the port, George Osborne, chancellor of the exchequer, unveiled what he called a “new
settlement” with the City of London.

Flush with political capital a month after his Conservative party’s decisive May 7 election victory, Mr Osborne declared the end of the
era when the financial services industry was “part of the problem — now it must be part of the solution”. The UK, he added, should aim
to have “the most competitive financial services in the world”.

For many in the audience — including Douglas Flint, HSBC chairman, and António Horta-Osório, chief
executive of Lloyds Banking Group — Mr Osborne’s words could not have been more welcome. After five years of feeling demonised,
under-appreciated and over-regulated, the bankers in the audience were finally feeling some love.

But Mr Osborne’s words may have carried a different message to the man sitting a bit further back in the audience than Mr Flint and Mr
Horta-Osório: Martin Wheatley.

As chief executive of the UK’s financial watchdog, the Financial Conduct Authority, Mr Wheatley has been the tormentor-in-chief for the
industry. Since the FCA was created in 2013, it has exacted ever-higher penalties from big banks following the Libor and foreign
exchange benchmark-rigging scandals; netted record levels of compensation for consumers following an insurance fraud scandal; and
notched up high-profile victories against figures such as Ian Hannam, the buccaneering former JPMorgan Cazenove dealmaker.

Under Mr Wheatley’s leadership, the FCA has also secured sweeping new powers, including oversight of payday lenders — 50,000 new
companies to supervise — and new antitrust tools.

But now the government is emphasising competitiveness over crisis. The
official view, as Mr Osborne told his Mansion House audience on June 10,
is that “there is no trade-off between high standards of conduct and competitiveness”.

Government officials have privately urged regulators to take a less heavy-handed approach, insiders say. (The Treasury denies this.)
Perhaps the question Mr Wheatley needs to be asking himself is whether the FCA itself is now part of the problem, not the solution?

“Martin has nailed his colours too resolutely to consumer protection,” one former regulator says. “The election leaves him on the wrong
side of the argument.”

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The FCA chief certainly seems aware of the shift. In a speech last month to an audience that included securities regulators from around the world, he mentioned “competition” 10 times. “Effective regulation [is] no longer seen as antithetical to growth, but as a necessary precondition for it,” he said. “Over the next [decade], we will be judged on our ability to facilitate competition; to embrace innovation without stifling it.”

**A searing experience**

Mr Osborne’s “new settlement” is a far cry from his party’s post-crisis stance towards regulation. In 2010, the new Conservative-led coalition government announced a plan to dismantle the old Financial Services Authority — discredited for its laissez-faire approach that some argue exacerbated the financial crisis — and in its place return supervision of lenders to the Bank of England, while a new, tougher watchdog would regulate financial firms with an iron fist rather than a light touch.

To lead it would be Mr Wheatley, then the head of Hong Kong’s Securities and Futures Commission. The Essex-born son of a plumber-turned-book-keeper was not tainted by association with the old FSA regime.

A searing experience in Hong Kong would shape his approach at the FCA. Tens of thousands of retail investors in the city were sold so-called minibonds — in fact they were complex derivatives underpinned by Lehman Brothers and sold on by local banks including Bank of China — that collapsed in value when the Wall Street bank imploded in 2008. The products had been approved by Mr Wheatley’s SFC. Street protests followed.

“Having an effigy of yourself burnt on the steps of your building, having banners of you with devil horns on and told to go home — that gets you to focus on your relationship to society,” Mr Wheatley says in an interview at the FCA’s Canary Wharf headquarters. “It was seeing the relationship of the regulator not just with the regulated entities but with the whole of society; that really was what Hong Kong brought home to me. We live it every day here.”

Many senior City figures would cheerfully burn effigies of Mr Wheatley too, if their hostility were not communicated more effectively in private meetings with senior Conservative politicians.

**‘Shoot first, ask questions later’**
Alarm bells first rang in the City in 2012, when Mr Wheatley promised that the FCA would protect consumers from their own “irrationality”. His comments reflected a modish enthusiasm for behavioural economics.

But his words conflicted dangerously with “caveat emptor”, or “buyer beware” — a fundamental principle to many in British business and the Conservative party. Bearing the costs of mistakes is the price individuals pay for financial freedom, they believe.

Mr Wheatley could hardly have anticipated this revival of libertarian spirits. In his first year he pledged to “shoot first and ask questions later” when it came to banning potentially harmful products. He also enforced tough new government measures for senior executives that were meant to hold them to account for failings on their watch. None of this was popular with bankers in the City. But then he handed his critics all the ammunition they needed. A decision to brief a journalist in March last year on the FCA’s plan to review the life assurance market had disastrous consequences. The UK’s major insurers saw their share prices fall due to the misperception that the regulator planned to target certain annuity products.

The irony was inescapable. The FCA is charged with ensuring markets are transparent and fair. But it took 16 hours for the FCA to issue a statement to the market. Mr Osborne wrote to Mr Wheatley to express his “profound concern” and suggested disciplinary action could be appropriate. A £3.8m independent inquiry ensued.

It found that the FCA had pursued a high-risk media strategy that failed to appreciate the price-sensitive nature of the information it was relaying to the Daily Telegraph. The 225-page report published in December was a biting indictment. The inquiry found that Mr Wheatley personally approved the kinds of pre-briefings that sparked the scandal. That he was not forced to resign over the matter piqued many in the industry, who saw a double-standard.

The fiasco underscored deeper concerns. The Practitioner Panel, a group of industry experts who challenge the regulator, said “there was an inherent danger in the FCA’s desire to court headlines to raise the profile of its work”.

The Treasury select committee, meanwhile, said the FCA was dysfunctional, deserving of special measures, and that a full inquiry should be held.

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“I don’t accept that it’s a dysfunctional organisation or that we need a root-and-branch review,” Mr Wheatley counters.

The ill-feeling between the FCA and the new select committee — which will be led again by Tory MP Andrew Tyrie — may spell trouble: for one former regulator, it is when the select committee loses confidence in the leadership of the watchdog that the writing is on the wall.

That puts Mr Wheatley in a vulnerable spot, judging by asides made by members of the former committee, many of whom will also sit on the new committee formed since May’s election.

“Our view was that it was a failing institution, simply,” says one. “We were seriously worried about it, and Wheatley doesn’t strike us as having done a good enough job.”

Mr Wheatley and John Griffith-Jones, FCA chairman, do not have fixed terms. Both are appointed — and discharged — by the Treasury. Insiders predict Mr Wheatley will leave in 2016, when he will have served four years. Mr Griffith-Jones is adamant that it was not necessary for Mr Wheatley to step down. “I don’t believe that people should be sacked every time they do something wrong; there’d be a severe shortage of people left in work.”

‘The industry is gunning for you’

Others see the fallout as a consequence of the FCA’s style of leadership. “Martin took the view that you can’t be captured by the industry and you shouldn’t ever associate with them,” says a former regulator. “Sometimes you have to take their calls and listen. Martin is so afraid of regulatory capture that he totally freezes them out. That’s fine but then the whole industry is gunning for you to fail — and at an institution like the FCA there’s bound to be a failure.”

A group that represents part of the sector complains that all but the largest companies are not handled by a single FCA official or team but are referred to a call-centre. “That is just not good enough,” a spokesman for the group says. “The time it takes to get a response is too long, and the quality of staff is not great.” The result is that the relationship between the
regulated and the regulator has become more adversarial. Some companies now would not contemplate a meeting with the FCA without a lawyer present, for instance.

“I do meet the big firms,” Mr Wheatley says. “But the truth is that we have 73,000 firms to regulate and that spreads the process thin. But I’m very keen we have a collaborative relationship with industry.”

Some of those companies are more influential than others. Mr Wheatley has not gained the kind of grudging respect from the top echelon of the City that predecessor Sir Hector Sants enjoyed as chief executive of the FSA. “I have a lot of time for Martin,” says the chairman of one large institution, “But he is not well liked.”

His diffidence can come across as arrogance, while the tendency of the FCA to reject many of the candidates put forward by boards for senior City jobs has “caused a massive withdrawal of talent”, according to the City grandee.

If Mr Wheatley’s relationship with the industry could be described as aloof, internally his staff see him as just as remote. Pale and gangly, he has the unfortunate nickname of the “Grey Vampire” among some of his more acerbic staff. “As rank-and-file employees we just don’t get to see him,” says one.

Yet those who have stayed at the FCA since the 2013 split say Mr Wheatley has ushered in changes for the better, with his unrelenting focus on protecting consumers, around which even his detractors concede he has done a decent job.

“Frankly, the emphasis on consumer protection under Wheatley is much more aligned to what I wanted to be doing and why I joined the regulator,” says a current employee.

But the forex and Libor probes have shifted attention away from these consumer protection victories. The scandals have also bumped up FCA fines, which now go to the Treasury, to record levels. But even Mr Wheatley concedes that nine-figure fines by themselves do not improve culture.
Yet those scandals have forced the issue of conduct to the fore. Putting “conduct into the boardroom” is, in Mr Wheatley’s opinion, the FCA’s greatest triumph, even if board members complain bitterly about the changes. “The climate is much more intrusive,” says one. “Board meetings last a week.”

The question that lingers is the FCA’s role in what happens next.

“I don’t feel a lot of pressure to protect consumers less,” says Mr Griffith-Jones. “And I don’t suppose there are a lot of votes in arguing for that. Where it gets a bit more complicated is around the City of London. If it has a reputation for not being straight, I think it would be very quickly damaged.”

Timeline

**April 2013** The FCA formally takes over from the Financial Services Authority as a conduct regulator to financial firms, tasked with protecting consumers

**March 2014** A botched briefing by Mr Wheatley into plans to review life assurance contracts rocks the markets. A Treasury select committee inquiry into the briefing, published in March 2015, calls the FCA “dysfunctional”.

**May 2014** Former JPMorgan Cazenove dealmaker Ian Hannam £450,000 loses appeal against market abuse fine.

**November 2014** Record fines of £1.1bn are meted out to five banks for their role in the foreign exchange rate-rigging scandal as part of an unprecedented global deal

**April 2015** Deutsche Bank is fined £227m for Libor and Euribor failings and for misleading the regulator

**May 2015** Barclays pays a record £284m to the FCA rigging for forex and other markets over five years

**June 2015** Lloyds fined £117m for its handling of compensation claims for mis-sold PPI
The Hong Kong Securities and Futures Commission’s Mark Steward is appointed enforcement director.

In his Mansion House speech, Chancellor George Osborne says the UK must have the “most competitive financial services in the world.”