CHAPTER **12**

An Overview of Enforcement by the Financial Services Authority

Enforcement by the Financial Services Authority

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CHAPTER **12**

An Overview of Enforcement by the Financial Services Authority

Enforcement by the Financial Services Authority

Robert Hadley, Philip Morgan, Neil Robson, and Rachel Stephens

A. The FSA Regulatory Regime

1. General

After midnight on November 30, 2001, the regulation of most of the United Kingdom financial services industry was put into the hands of a single regulator, the Financial Services Authority ("the FSA"). The statute governing the regulation of the U.K. financial services industry and defining the FSA's functions, duties, and powers is the Financial Services and Markets Act - 2000—universally referred to as "FSMA." The FSA replaced several self-regulatory organizations ("SROs") and, since FSMA came into force, more areas of the financial services - industry—notably mortgage business and general insurance business—have been drawn into the FSA's jurisdiction. The FSA derives its powers from Parliament but is not a government agency. It is funded by a statutory levy raised on firms in the industry and not by the government.

The FSA Enforcement Division comprises the teams that investigate possible breaches of regulation and, if appropriate, initiates proceedings (including criminal proceedings) with a view to imposing sanctions on persons guilty of regulatory breaches. It is generally Enforcement that will exercise the FSA's information-gathering powers and conduct investigations into suspected misconduct. The FSA stresses that it is not an "Enforcement-led regulator," pointing out that Enforcement accounts for a relatively small percentage (about 12%) of its annual budget. It effectively has complete discretion as to when to exercise its enforcement powers.

In practice, the FSA regards the deterrent effect of enforcement action as a key part of its overall regulatory regime. Enforcement is a tool with which the FSA enhances its supervision of authorized firms and approved persons by reference to its statutory objectives laid down in FSMA. Enforcement is a highly visible part of the regulatory landscape. However, the penalties issued in FSA enforcement cases to deter improper conduct are a fraction of the penalties sought by its U.S. counterpart, the SEC. By way of example, the penalties levied in 2004 following the overstatement of Shell's oil reserves, in what was a coordinated enforcement action by the SEC and the FSA, were $120 million in the U.S. and £17 million (about $28 million) in the U.K.[1] Nevertheless, that is the highest penalty imposed to date in the U.K.

To give an idea of the extent of formal FSA enforcement activity, the 2005-6 FSA Annual Report states that 227 investigations were closed by the FSA Enforcement Division and 81 investigations concluded with "use of powers" (i.e., sanctions such as prohibition, financial penalties, or variation of permissions).[2] That means that 146 investigations concluded in the year "without use of powers." Of those 146 investigations, 12 resulted in a private warning to the person under investigation.

This chapter provides an overview of the interaction with the FSA that firms might experience in an enforcement context, the FSA's enforcement powers and practices, and the factors to consider in responding to FSA enforcement action. Similarly, this chapter comments on the practical approach to be taken by firms and/or individuals and their legal advisers in FSA enforcement action. Much of the general practical guidance set out in the preceding chapters in relation to securities enforcement in the U.S. applies equally to the U.K. In particular, persons under investigation by the FSA will look to maintain a constructive dialogue with the FSA staff with a view to convincing them of the firm's case (usually at an earlier rather than a later stage), its good faith, its cooperative and responsible attitude, and its general fitness to operate in the regulated sector.[3]

2. The FSA's Role and Statutory Powers

a. The Statutory Objectives

The FSA's powers include a wide range of rule-making, investigatory and enforcement powers. The key function of the FSA under FSMA is to promote the four statutory objectives for the FSA laid down by FSMA:[4]

1. market confidence—maintaining confidence in the financial system;
2. public awareness—promoting public understanding of the financial system;
3. consumer protection—securing the appropriate degree of protection for consumers; and
4. the reduction of financial crime—reducing the extent to which it is possible for a business to be used for a purpose connected with financial crime.

The FSA summarizes these four objectives with one overall aim: To promote efficient, orderly, and fair markets and to help retail consumers achieve a fair deal.

b. Regulating the U.K. Financial Services Industry

Generally speaking, the FSA only regulates entities that are required to be regulated by FSMA and that have followed the necessary procedures to become authorized by the FSA. Not all aspects of the U.K. financial services industry are regulated, although many areas previously outside regulation are slowly being drawn within the scope of FSA regulation. Unregulated persons are not generally subject to the FSA's powers or the FSMA regulatory regime. Unregulated persons can become involved with the FSA, however, in the course of the FSA's role as a prosecutor of certain criminal offenses or if involved in suspected market abuse,[5] and/or where unregulated persons are subject to the FSA's investigatory powers.

Regulated entities must comply with the provisions of FSMA, and also with the subordinate legislation under it. In addition, there are day-to-day rules with which all regulated firms must comply. These day-to-day rules supplement FSMA and the subordinate legislation and are included, together with detailed guidance as to the interpretation and implementation of FSMA, in the FSA Handbook ("the Handbook").[6] The Handbook is a very substantial document divided into sections.

At the core of the Handbook are 11 basic Principles for Businesses ("the Principles") that must be followed by all FSA authorized firms:[7]

Principle 1	**Integrity**	A firm must conduct its business with integrity
Principle 2	**Skill, care, and diligence**	A firm must conduct its business with due skill, care, and diligence
Principle 3	**Management and control**	A firm must take reasonable care to organize and control its affairs responsibly and effectively, with adequate risk management systems
Principle 4	**Financial prudence**	A firm must maintain adequate financial resources
Principle 5	**Market conduct**	A firm must observe proper standards of market conduct
Principle 6	**Customers' interests**	A firm must pay due regard to the interests of its customers[8] and treat them fairly
Principle 7	**Communication with clients**	A firm must pay due regard to the information needs of its clients and communicate information to them in a way that is clear, fair, and not misleading
Principle 8	**Conflicts of interest**	A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client
Principle 9	**Customers: relationships of trust**	A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment
Principle 10	**Clients' assets**	A firm must arrange adequate protection for clients' assets when it is responsible for them
Principle 11	**Relations with regulators**	A firm must deal with its regulators in an open and cooperative way, and must disclose to the FSA appropriately anything relating to the firm of which the FSA would reasonably expect notice

As referred to below, the FSA is placing increasing emphasis on the Principles despite the technicalities inherent in detailed rules and guidance. A regulated person must be prepared to have its conduct and behavior tested against the Principles. If the FSA determines that a regulated person's conduct or behavior is not consistent with the Principles, that person is exposed to the risk of FSA enforcement action.

The FSA's approach to regulation is:

(a) risk-based;[9]
(b) accountable, with a transparent approach involving public consultation to the development of the framework and standards used by the FSA;
(c) results focused—concentrating on effectiveness; and
(d) emphasizes the responsibility of senior management.[10]

The FSA seeks to identify and measure risk in three ways:

(1) using the Advanced, Risk-Responsive Operating FrameWork ("ARROW") for assessing financial institutions.[11] The FSA seeks to identify individual material risks within each firm and assesses how those risks threaten the FSA's statutory objectives;[12]

(2) using special projects to identify industry sector risks that are likely to apply to every firm within that sector; and
(3) through wider macroeconomic analysis, involving the assessment of market developments and social and demographic trends to assess wider risks to the industry.

The FSA views its risk-based regulatory approach, ARROW, as fundamental to its operation because it focuses regulatory attention on the firms and on the activities that pose the greatest risk. The FSA has developed risk assessment frameworks for analyzing the risks presented by each regulated firm, and for identifying risks that are not firm specific and that are industry-wide. By using these techniques, the FSA can decide on which areas to focus its activities, such as on a particularly risky firm or across the industry more generally where there is widespread concern.

3. FSA Authorization and Approval

As a matter of terminology, companies and businesses that operate in the financial services sector in the U.K. are referred to as "firms."[13] Firms and persons are "authorized" by the FSA to carry out "regulated activities," which are certain defined business activities in the financial services sector. In addition, directors and certain key employees of firms are required to be approved by the FSA so that they are "approved persons" to carry out in each case a defined list of "controlled functions" within the firm's business. Third parties within the regulatory control of authorized firms may be "appointed representatives" of the authorized firm so as to operate under the principal's authorization.

Since only authorized persons may carry out regulated activities, and only approved persons may carry out controlled functions within such a business, the threat of withdrawal of authorization or approval is a significant threat to firms' businesses and approved persons' livelihoods, over and above any specific financial or other penalty that may be available to the FSA for specific offenses or regulatory breaches in a particular case. "Regulated activities" are defined in Section 22 FSMA as those activities specified by HM Treasury carried out in relation to specified investments.[14] Most activities in which a bank, broker, or other financial services business (including the life and general insurance industries) engage will be regulated activities.

A person who is not an authorized person (or an exempt person)[15] is not allowed to carry out regulated activities as a business in the U.K. This is "the general prohibition." Section 23 FSMA makes breach of this general prohibition a criminal offense. Firms that are authorized by the FSA obtain "Part IV Permissions," which detail the specific regulated activities, types of investment and customers in relation to which the firm is allowed to operate.

A key exception that may often allow U.S.-based firms to avoid the need for FSA authorization is the "overseas persons exemption." That exemption is only available where the relevant firm does not have a permanent place of business maintained by it in the U.K. It permits non-U.K. entities to undertake certain dealings with or through FSA authorized persons and, where a "legitimate approach" has been made,[16] to advise on investments or agree to arrange deals in investments without the need for FSA authorization.[17]

It should also be noted that a firm that is authorized in one European Economic Area ("EEA") Member State may, subject to certain qualifying criteria, carry out the same activities for which it is authorized in its home State in other EEA Member States without having to obtain separate authorization from all relevant EEA financial services regulators. In this way an authorized firm in the U.K. may operate or open a branch on a "passported" authorization in other EEA States, and EEA authorized firms may be "passported" into the U.K. without having to go through the full procedure of obtaining FSA authorization. A U.S. firm may therefore be able to operate or set up a branch network in the EEA with authorization in one EEA member state only.

4. FSA Enforcement

The FSA's Enforcement Division investigates suspected breaches of FSA rules or FSMA requirements. If the Enforcement staff believes a violation occurred, it then may investigate and recommend action. Before significant enforcement or disciplinary sanction is formally proposed, including any financial penalty or censure, the recommendation is considered by a separate committee of the FSA, called the Regulatory Decisions Committee ("the RDC").[18]

FSMA gives the FSA statutory investigatory powers and the power to impose various types of sanctions. Some of these actions are discussed below. However, in addition to these actions, FSMA also gives the FSA power to prosecute offenses under the insider dealing provisions of the Criminal Justice Act 1993 and under the Money Laundering Regulations 2003.[19] FSMA gives the FSA the necessary enforcement tools, including the power to interview people and require them to produce documents.

Settlement may be negotiated with the FSA at any stage of the process. The RDC is the -decision-maker for most enforcement matters that do not settle. RDC members come from a wide range of backgrounds reflecting the interests of industry and consumers. The RDC is an FSA body not an independent tribunal. The independent Financial Services and Markets Tribunal ("Tribunal") handles appeals in the decisions process for those individuals and firms who do not agree with the FSA's decision.

The FSA has the power to impose the following specific sanctions:

a. Variation or Cancellation of Authorization

In extreme cases, the FSA has the power to vary or cancel an authorized firm's permission under sections 33, 53, and 54 FSMA. The threat of this action by the FSA is extremely significant for an authorized firm since the removal of its FSA-authorization will mean that it is no longer lawful for it to conduct any regulated activities within the U.K.

b. Withdrawal of Approval/Prohibition Orders

Similarly, under Section 63 FSMA, the FSA may withdraw an individual's approval to carry out the controlled functions for which he or she was an approved person if the FSA considers him or her no longer to be "fit and proper" to carry out those functions. That makes it unlawful for the person to continue in his or her role in the regulated sector. The FSA also has the power under Section 56 FSMA to prohibit any individual that the FSA deems not to be fit and proper from performing a specific function or functions within the U.K.'s regulated regime.

c. Financial Penalties/Restitution

As an alternative to canceling the authorization of an authorized person whom the FSA believes has breached a requirement of FSMA, the FSA has the power under Section 206 FSMA to impose a penalty of such (unlimited) amount as the FSA considers appropriate. The largest financial penalty imposed by the FSA to date has been £17 million in relation to Shell's misstatement of oil reserves, which was characterized as market abuse and breach of the Listing Rules.[20] The largest financial penalty for an individual was £750,000 for market abuse and breach of Statements of Principle 2 (due skill, care, and diligence) and 3 (market conduct).[21] In addition, under Section 384 FSMA the FSA may require an authorized person to make restitution of profits realized by the firm or loss suffered by another person as a result of the firm's contravention of a FSMA requirement or market abuse.

Under Section 66 FSMA, the FSA can impose a financial penalty against an individual or publish a statement of the individual's misconduct. There is a reputational element to these penalties, and widespread knowledge amongst the financial services community that an individual has been fined or the publishing of a statement of his or her misconduct may mean that his or her ability to derive income from or be employed by financial services firms will be curtailed.

d. Injunctions

Section 380 FSMA gives the FSA the power to seek an injunction in court to prevent firms or individuals, whether authorized by the FSA or not, from breaching certain provisions of FSMA, or, if the FSA is aware that a breach has occurred and believes it will occur again, it can apply to court for an injunction to prevent a second breach. The FSA also can seek injunctions to remedy a course of conduct and/or to secure assets.[22]

e. Public Censure

Under Section 205 FSMA, if the FSA believes that an authorized person has contravened a requirement of FSMA, the FSA may publish a statement to that effect. This could have a reputational effect since the public would be aware of the rule breach. As noted above, the FSA can publish a similar statement with respect to individuals under Section 66 FSMA.

5. Major Differences from the U.S. Regimes

It may be useful at this point to highlight some of the differences between the regulatory enforcement of the financial services industry in the U.K. by the FSA and the regulatory enforcement regime in the US. Although it can be overstated, the scale of the enforcement activity is radically different, even making allowance for the much greater size of the U.S. and the U.S. markets. By way of example, in 2006 the FSA issued only 26 Final Notices imposing a financial penalty upon firms and individuals and 19 in 2005.[23] The SEC alone typically brings more actions in a month, and a much larger number of actions are brought by the self-regulatory organizations. The average FSA fine (apart from disgorgement of profit or restitutionary payments to consumers) in 2006 was £453,000 for firms and £281,000 for individuals. The largest financial penalty imposed on a firm by the FSA was £17 million,[24] and the largest fine paid by an individual was £750,000. The FSA opened 269 enforcement investigations in fiscal year ended March 31, 2006. Of those investigations, 168 related to a firm's or individual's fitness and propriety or a firm's suspected failure to meet other threshold conditions.[25]

Another significant difference is the ability to prosecute alleged violations criminally. The SEC has no criminal jurisdiction and refers potential criminal matters to the Department of Justice or state attorneys general. On the other hand, the FSA can bring prosecutions for criminal offenses. These matters primarily arise under FSMA itself, but include insider trading under the Criminal Justice Act 1993 and making misleading statements to the market under Section 397 FSMA.

Like the SEC and SROs in the U.S., the FSA expects firms to have systems and controls in place that ensure compliance with the relevant law, rules, and guidance. While it might be prudent to self-report to the relevant regulator in the U.S., regulated persons in the U.K. are, by Principle 11, subject to an overriding obligation to report matters that may be of a regulatory concern. Failure to notify the FSA of a matter that falls within the very broad terms of Principle 11 is itself a breach of the Rules that could give rise to enforcement action. [26]

The general obligation to inform the FSA of matters of which it would reasonably expect to be aware is extended further in the context of formal FSA enforcement investigations. A person under investigation has no right to "plead the Fifth" and cannot refuse to answer questions put to him or her by the FSA under its statutory compulsory information-gathering powers on the basis that to answer might incriminate him- or herself. There is a protection in criminal or market abuse proceedings in that answers given under compulsion may not be used against the interviewee in such proceedings,[27] and the FSA often chooses not to invoke its compulsory powers so as to avoid those protections. In principle, however, damaging answers can be compelled from persons under investigation notwithstanding the risk of self-incrimination.[28]

Another power given to the FSA by FSMA that has no parallel in the U.S. regulatory scheme is the power under Section 166 FSMA to require a firm to engage, at the firm's cost, a skilled person to report to the FSA on the firm's business.[29] The "skilled person" must be approved by the FSA and owes his or her primary duty to the FSA. Skilled Persons reports are referred to at Section E.6 below.

B. Recent Developments

1. The Enforcement Process Review

Following a widespread uneasiness with the FSA's approach to enforcement, and in particular at a perceived close liaison between the investigators from the Enforcement team and the RDC, the FSA agreed in July 2005 to implement recommendations relating to its enforcement processes made by the Enforcement Process Review ("EPR"), commonly referred to as the Strachan review.[30] The EPR recommended that the FSA provide:

- a clear articulation of the FSA's overall approach to the use of enforcement;
- sufficient checks and controls during the investigation phase to help deliver balance and fairness;

- transparency for those subject to enforcement action about the case they have to answer and the evidence on which it is based; and
- clarity as to the separation (required by the FSMA) between those who investigate a case and those who decide it.

The EPR made 44 recommendations designed in particular to emphasize and put into effect the separation between Enforcement or other FSA staff and the RDC and to increase disclosure of material to persons subject to enforcement. The FSA accepted and implemented all of the EPR's recommendations. While the decision-making process may have improved, it must always be remembered that the RDC is part of the FSA and not an independent decision-maker. On the other hand, the Financial Services and Markets Tribunal, referred to below, is independent from the FSA and handles appeals against FSA decisions.

2. The Shift to a Principles-Based Approach

The FSA is expressly required to base its exercise of its general functions (including enforcement) on the need to use its resources efficiently and economically.[31] Therefore, the FSA will balance the cost and the cost-effectiveness of any proposed action against the anticipated benefit. Principle 11, which states that a firm must disclose to the FSA appropriately anything of which the FSA would reasonably expect notice, is the FSA's key information gathering tool. This allows the FSA to minimize the costs of investigations.

The FSA is a principles-based regulator, and it is important to recognize the fundamental character of the Principles. There are hundreds of pages of detailed guidance as to what the FSA expects. None of these provisions override the Principles. While complying with FSA guidance will always be advanced by a firm as a defense to enforcement or disciplinary action, the fact that the FSA cannot identify a breach of a specific rule does not mean that no enforcement or disciplinary action will follow. If the FSA disapproves of conduct, it can assert that such conduct is a breach of one or more of the Principles, and initiate an enforcement action based solely on what it perceives to be a breach of the Principles.

Increasingly, the FSA enforcement actions are based upon breaches of the Principles, as opposed to the breach of a specific rule. Penalties have been incurred despite the fact that the activity in the U.K. related to a European market and trading in that market did not give rise to a complaint of a breach of a specific FSA Rule or market abuse within the FSA's jurisdiction.[32] In one case, the misuse of information gave rise to a penalty against an individual broker even though the Final Notice imposing the penalty acknowledged (a) that the information was not in fact inside information; and (b) that the broker did not positively believe that he was passing on inside information or that he deliberately conveyed that impression to clients. [33] Because the broker should have been alerted to the risk that he may have been given inside information, the FSA found that his behavior fell short of expected standards under Statements of Principle 2 and 3 (due skill, care, and diligence and standards of market conduct).[34]

3. Handbook Changes

The FSA's detailed guidance as to how it exercises its enforcement functions is set out in section ENF of the Handbook. ENF is therefore a key resource for firms faced with regulatory issues that might give rise to FSA enforcement. The FSA's decision-making process, including in the enforcement context, is laid down in the Decision Making (DEC) section of the Handbook.

The FSA published in January 2007 a consultation paper in which it announced that it intends to withdraw both ENF and DEC and replace them in their entirety. [35] They will be replaced by two new sections, the Decision Procedure and Penalties manual, DEPP, and the Enforcement Guide, EG. The FSA expected the consultation process to conclude in April 2007 and to report on it in June 2007, with a view to introducing the new DEPP and EG with effect from July 1, 2007 but the current aim is to issue a policy paper at the end of July 2007 and introduce DEPP and EG at the end of August 2007. References to ENF and DEC in this chapter are likely, therefore, to be replaced by parts of DEPP and EG in the later part of 2007. The FSA states that the consultation process is to streamline and simplify, and not to make significant substantive changes. Where appropriate, the current proposed new provisions are referenced, but at the time of publication they remain in draft and subject to the consultation process (and the numbering may therefore change).

ENDNOTES

1. Shell Transport & Trading Co., Final Notice (Aug. 24, 2004), available at - http://www.fsa.gov.uk/pubs/final/shell_24aug04.pdf.

2. FSA, Ann. Rpt., p. 141-49 (2005/06), *available at* http://www.fsa.gov.uk/pubs/annual/ar05_06/ar05_06.pdf.

3. One significant difference is that regulated firms and individuals in the U.K. are under a specific duty to self-report matters of regulatory concern to the FSA. Any question of whether to self-report is an issue of substantive compliance, where failure to do so may be a regulatory breach, and not purely a question of assessing the advantages and disadvantages of cooperation from the firm's point of view.

4. Section 2(2) FSMA lists the regulatory objectives and they are expanded upon in Sections 3, 4, 5 and 6 FSMA respectively. Financial Services and Market Act 2000 (hereinafter FSMA), C.8 §§ 2(2), 3-6, available at - http://opsi.gov.uk/ACTSs/acts2000/00008–b.htm#2.

5. "Market abuse" is a "civil offense" for which persons, including unregulated persons, can be fined or censured by the FSA. Creation of this offense was one of the major innovations of FSMA and it is defined in Section 118 FSMA. Very broadly, market abuse is behavior amounting to the misuse of non-public information, by disclosure or use equivalent to insider dealing or the manipulation or distortion of the market or creation of a false market. FSMA, § 118.

6. FSA materials are available at http://www.fsa.gov.uk. The Handbook is available at - http://fsahandbook.info/FSA/html/handbook/.

7. FSA Handbook, Principles For Business (hereinafter PRIN) 2.1.1. Similar principles bind individual approved persons. FSA Handbook Statements of Principles and Code of Practice for Approved
Persons (hereinafter APER) 4. Principles also bind the dealings of listed companies subject to the Listing Rules. FSA Handbook, Listing Rules (hereinafter LR) 7.

8. Clients of FSA authorized firms are classified into one of three categories of rising sophistication: private customers, intermediate customers, and market counterparties. The word "customer" when used in the FSA Handbook and in this chapter refers to the first two of those categories, and the word "client" refers to all clients including market counterparties. New client classifications will be introduced in 2007 with the implementation of the Markets in Financial Instruments Directive, Directive 2004/39/EC ("MiFID"). Most clients will be either "retail" or "professional" clients with a limited third category "eligible counterparty" or "ECP" for certain limited business. The distinctions and the effect of each classification are not the same as under the present COB (Conduct of Business) section of the Handbook, and the FSA will introduce a new Conduct of Business section, to be known as "COBS" with the implementation of MiFID on November 1, 2007.

9. FSA Handbook, Supervision (hereinafter SUP) 1.3, discusses risk-based approach to regulation of supervision. *See also* Callum McCarthy, Chairman, FSA, Risk Based Regulation: The FSA Experience, Address Before the Australian Securities and Investment Commission, available at - http://www.fsa.gov.uk/___/Library/Communications/Speeches/200__/021____.shtml.

10. *See* FSA Handbook, Senior Management Arrangements, Systems and Controls (hereinafter SYSC) 1.2.1 G; SUP 1.1.4G.

11. FSA, The FSA's Risk-Assessment Framework (Aug. 2006), available at http://www.fsa.gov.uk/ pubs/policy/bnr_firm-framework.pdf.

12. "ARROW" is described in detail in the FSA publication "The FSA's risk assessment framework" Aug. 2006, available at http://www.fsa.gov.uk/pubs/policy/bnr_firm-framework.pdf.

13. The choice of this term is disapproved by the purist. Many "firms" will of course be companies despite the use of the term in a legal context in England and Wales usually excluding corporate entities.

14. FSMA, § 22. The order specifying the "regulated activities" and "investments" is the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (as amended), generally referred to as the Regulated Activities Order or "RAO." Financial Services and Markets Act 2000 (Regulated Activities) Order 2001, S.I. 2001/54, art. 4 (U.K.) as amended in S.I.

2006/2383 (hereinafter RAO). A very wide range of financial services activities are specified including accepting deposits, dealing in investments (either as agent or principal), arranging deals in investments, managing investments, safeguarding and administering investments, establishing and operating collective investment schemes and advising on investments. Specified investments include deposits, contracts of insurance, consumer mortgages, shares, debentures and such derivative instruments as options, futures and contracts for differences.

15. An “exempt” person is one exempted from the need for authorization by HM Treasury under Section 38 FSMA or an appointed representative of an authorized person under Section 39 FSMA in relation to the regulated activity in question. FSMA, §§ 38-39.

16. A “legitimate approach” by the overseas person is an approach to the relevant U.K. person that is either (i) solicited by the U.K. person, or (ii) within exemptions to the financial promotion rules in Section 21 FSMA. Communication of an invitation or inducement to engage in investment activity is prohibited by Section 21(1) FSMA unless the communication is made by or approved under the section by an authorized person. FSMA, § 21, ¶ 1. The prohibition may be relaxed by order of HM Treasury and this was done by, now, The Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the “Financial Promotion Order” or “FPO”). Financial Services and Markets Act 2000 (Financial Promotion) Order 2005/1529 (U.K.) (hereinafter FPO). Note that the Government intends to review the detailed implementation of Section 21 FSMA and the FPO in 2007. Those exemptions to Section 21 FSMA are very detailed and require close examination but broadly they exempt communications to institutional investors, FSA authorized firms and certain other categories of sophisticated investors.

17. RAO, art. 72.

18. The RDC is the arm of the FSA that is actually responsible for making significant FSA enforcement and authorization decisions such as whether to impose sanctions and if so what sanctions.

19. The Money Laundering Regulations impose certain obligations on firms and individuals in the regulated sector in respect of, for example, client identification procedures, breach of which amounts to criminal offenses.

20. Shell Transport & Trading Co., Final Notice (Aug. 24, 2004), available at -http://www.fsa.gov.uk/pubs/final/shell_24aug04.pdf.

21. Jabre, Final Notice (Aug. 1, 2006), *available at* http://www.fsa.gov.uk/pubs/final/jabre.pdf. The conduct involved was short-selling stock in respect of which Mr. Jabre had confidential non-public information. The hedge fund for which he worked was also penalized £750,000.

22. The FSA’s policy on applying for injunctions is set out at FSA Handbook, Enforcement (hereinafter ENF) 6.6.

23. Details of FSA fines are available on the FSA website at e.g., http://-www.fsa.gov.uk/Pages/About/Media/Facts/Fines/2006.shtml.

24. Although that is exceptional—the second highest fine (as opposed to disgorgement/ compensation payments) so far is £4 million.

25. FSA Annual Report 2005/06 Appendix 9. Enforcement Activity 2005/06.

26. Statement of Principle 4 has a similar requirement for Approved Persons.

27. FSMA, § 174.

28. Further, once a formal investigation is started by the appointment of investigators under the FSA’s FSMA powers, the FSA investigators have statutory powers to compel co-operation not only from regulated persons or persons connected with them but also from persons outside the regulated sector who are unconnected with any regulated person. The powers of investigators are set out at Sections 171 to 173 FSMA.

29. There is a loose analogy with the appointment in the U.S. of compliance monitors imposed on companies by the SEC and Department of Justice in settlements, but the role and purpose is of course different.

30. The Enforcement Process Review report, a wide-ranging review of the FSA’s enforcement process, was led by David Strachan, *available at* http://www.fsa.gov.uk/pubs/other/enf_process_review_report.pdf.

31. FSMA, § 2(3)(a) FSMA. *See also* SUP 1.3.1G.

32. *See* Citigroup Global Markets Ltd., Final Notice (June 28, 2005), available at -http://www.fsa.gov.uk/pubs/final/cgm/28june05.pdf. The total financial penalty imposed was £13.9 million for contravention of FSA Principles 2 (due skill, care, and diligence) and 3 (management and control), which consisted of £9.9 million disgorgement of profit and a further £4 million penalty. *Id. See also* Deutsche Bank AG, Final Notice (Apr. 11, 2006), *available at* http://www.fsa.gov.uk/pubs/ final/deutsche.pdf.

33. Pignatelli, Final Notice (Nov. 22, 2006), *available at* http://www.fsa.gov.uk/pubs/final/ pignatelli.pdf.

34. *Id.*

35. FSA, Consultation Paper 07/2, Review of the Enforcement and Decision Making Manuals (January 2007).