Latest from the FCA: more to do on market abuse

In its latest issue of Market Watch (No. 51) the FCA makes some observations about market abuse awareness and controls in relation to market makers which have broader relevance to firms with market abuse risks on their radar. In this briefing we highlight some of the key messages for firms - some will be familiar, yet the FCA continues to find failings in these areas. Ignorance is no excuse and firms should take heed.

Key lessons: market abuse awareness

- All employees (at all levels) must understand their role in controlling flows of confidential and inside information. Whilst compliance teams are generally alert to potential market abuse risks, senior management and other team members can have inconsistent levels of awareness of market abuse risks across the business.
- There must be evidence of sufficient challenge from the second and third lines of defence.
- Firms should conduct sufficiently regular and detailed market abuse risk assessments to identify and monitor market abuse risks. Firms not doing this regularly will find it difficult demonstrating to the FCA that effective controls are in place.

Key lessons: information barriers

- All information barriers must be clearly defined and understood - that is, not only between the private side and public side operations. For example, a barrier between sales and sales-trading staff sitting within close proximity to a market making team presents a 'significant challenge' in maintaining effective barriers.
- Senior management classified as 'permanent insiders', who are situated (or have an additional desk) within close proximity to a market making desk and have access to market makers' trading positions, could present a conflict of interest.
- Firms demonstrate the most effective controls by physically segregating individuals or teams that regularly have access to confidential or inside information. However, where physical segregation is not possible, firms should take extra steps to ensure they properly manage and maintain information barriers. This could include specific training for staff operating in these areas and ensuring proper integration of compliance representatives with front line operations to improve manual surveillance capabilities and information management.

Key lessons: wall-crossing procedures and insider lists

- Documentation of wall-crossing procedures is poor. Firms should be aware of the procedural and record keeping requirements imposed by MAR in relation to both wall-crossed and non-wall-crossed market soundings.
- The most effective procedures use compliance as 'gatekeepers' to centralise a consistent approach to wall-crossing.
- Firms should review insider lists regularly to ensure they are accurate and suitably detailed.
- Firms should adopt a stringent 'need to know' principle to keep the number of people privy to inside information to the minimum necessary to perform a particular role or task to the appropriate standard.

Key lessons: monitoring and surveillance

- Periodically monitoring the trading activity of market makers when individuals at the firm have been wall-crossed is an important step in mitigating the risks of market abuse. All firms should consider performing this type of enhanced monitoring where individuals are wall-crossed.
- Take care when selecting suitable surveillance tools and setting alert parameters (particularly given the UK small and mid-cap equity market can include periods of very high volatility, in terms of share price and trading volumes).
- The most effective surveillance programmes involved significant and careful calibration of both the alert parameters and alert logic based on the surveillance officers' experience of trading patterns and clients.

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