Managing an internal investigation chapter summary

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The purpose of this chapter is to consider the practicalities of handling an internal investigation by firms regulated by the Financial Conduct Authority ("**FCA**") or the Prudential Regulation Authority ("**PRA**"). It provides some suggestions on how firms can manage an internal investigation and analyses the issue of legal privilege, which must be considered in the context of the documents that are generated as part of an investigation.

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Introduction

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Managing an internal investigation into allegations of misconduct can be a complex and sensitive matter for any organisation. It is important to ensure that the investigation is properly structured. First, so that the investigation properly addresses the issues of concern and ensures that appropriate remedial action is identified where required.

Secondly, to make sure that proper processes are followed. This will assist in ensuring the integrity of the investigation, the credibility of evidence obtained and compliance with legal and regulatory duties, including employment rights and the regulatory requirements and expectations of the PRA and FCA.

Thirdly, to give due consideration to whether it is appropriate and/or necessary to notify any third parties, such as the FCA, PRA or other enforcement agencies; and fourthly, to give appropriate consideration to what the firm wants to protect as legally privileged, so that information is not unnecessarily discloseable to third parties and in any subsequent litigation or government investigation.

These considerations are all the more important for organisations operating in the regulated financial services sector. The FCA and PRA are likely to take into account the fact that the firm has carried out an effective and thorough investigation in determining any regulatory action to be taken. The regulators may also require firms to adhere to agreed protocols in the conduct of investigations so that evidence is gathered in a manner that does not preclude its future use by the regulator. More generally, the PRA and FCA are required to take into account the extent to which firms have identified and proactively resolved a problem that amounts to a breach of their rules, as well as the level of cooperation shown by the firm, both in deciding whether to take action (as mentioned in its Enforcement Guide at EG 2.12), and in assessing the level of any penalty they decide to impose. Conversely a failure to properly investigate matters or cooperate fully with the regulators will be regarded as aggravating factors which would increase the prospects of enforcement action being taken and potentially lead to the imposition of more serious sanctions.

Firms should consider at the outset what they want to, or may have to, notify to the regulators and subsequently share with them, but also what they might want to keep separate and legally privileged - and those considerations should inform the structure of any written output from the investigation.

Any investigation is likely to have a significant impact on a firm. As well as taking up management time, it may damage staff morale and could (if made public) potentially affect a firm's reputation and standing in the market. In addition to the cost of any reputational damage, the firm may have to bear the cost of external professional advice.

This chapter discusses the practicalities of handling an internal investigation into matters that might affect a regulated firm. It provides some suggestions on how firms can manage an internal investigation and discusses the difficult issue of legal privilege which must be considered in the context of the documents that are generated as part of an investigation.

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Early identification of issues and scope

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If a firm identifies that a particular issue presents a risk at an early stage, it will be in a better position to control its response to the issue and its communications with the regulator. Assessing the issue and scope will enable the firm to identify whether it is appropriate to undertake an investigation at all, or whether (for example in the case of potential criminal behaviour) it should give the authorities the opportunity to investigate first.

The key to a successful internal investigation is, where possible, to clearly identify the appropriate scope of the issues at the outset, based on defensible and proportionate analysis and assessment. Consideration for the scope should include affected individuals, business areas and the jurisdictional scope as well as the risk of impact on customers, the markets, investors and other key stakeholders. The scope needs to be adequate but efficient - an overbroad scope can risk being seen as too slow and obfuscatory. It may be better to adopt an incremental approach which recognises that the scope may need to expand if information is gathered which points in that direction, rather than delaying commencing any investigation and remediation work.

The ability to conduct an internal investigation, before and after any external notifications to regulators, will depend largely upon the trigger event and the views and wishes of the regulator.

In cases where the facts indicate serious regulatory or criminal breaches, the firm will most likely to notify the appropriate regulator immediately in accordance with FCA Principle 11 and the PRA's Fundamental Rule 7, as well as the provisions of the SUP 15 chapter of the FCA handbook.

There may be some less serious matters where it may be appropriate to gather appropriate information to enable an informed and useful report to be made to the relevant regulator. The rules and requirements of SUP 15 and the guidance on Principle 11/ Fundamental Rule 7 should be considered carefully. In particular, the FCA has recently brought several enforcement fines against firms where the content and promptness of notifications and ongoing communications about an issue have fallen short of its expectations and standards. Where financial crime issues arise, the firm will also need to consider whether it is under an obligation to report matters to the National Crime Agency (**NCA**).

In practice the extent to which the firm is able to conduct an internal investigation will vary depending on the seriousness and gravity of the issues, the speed with which the regulators refer the matter to their enforcement teams, the scope and speed of the regulator's investigation, and the strategic considerations in play. In cases given less priority by the regulator, the regulator may well accept a proposal from the firm to carry out an initial investigation internally and to report the findings to the regulator.

It is worth bearing in mind that the existence of an external investigation does not necessarily mean that the firm should not conduct any internal work. For example, the firm might consider it necessary and appropriate to meet its regulatory obligations - including its obligation to act in the best interests of its customers - where a remediation exercise might be appropriate; a form of investigation might be necessary to remediate accounting or IT failures or investigate an employment matter and take appropriate action; or a firm's non-executive directors might form the view that they should commission a review of the issues.

Many firms' Senior Managers (SMFs) will want to carefully consider their personal accountability to take reasonable steps to prevent and stop regulatory breaches by the firm. Discharging their duties may involve ensuring that appropriate review and enhancement is undertaken internally. Additionally, the issue in question may cast doubt on some of the firm's staff, including Approved Persons, and their suitability to perform controlled functions or be associated with the firm's regulated activities. Firms may take the view that they need to take steps promptly to satisfy themselves whether particular staff members may have breached the law or regulatory standards, and whether those staff members can remain in place, and to enable them to complete regulatory references in the form now required for all regulated firms in SYSC 22 of the FCA's handbook. In these circumstances some form of employment-led response might not be able to wait for the outcome of a regulator's investigation.

The firm should bear in mind appropriate liaison with the FCA before undertaking internal work and should also ensure that any work is coordinated across teams who may be leading different aspects of the response to the issue. The FCA's Enforcement Guide at chapter 3.11 provides some guidance in this regard. If the FCA or PRA perceives that an internal investigation could be damaging to its own investigation, for example where there is a suspicion that insider dealing is in operation, then the FCA or PRA may request that no further steps are taken by the firm. The FCA's view of the value of internal investigations has evolved in recent years. A speech was given in 2016 expressing the view that firm-commissioned reports are "not that important"[1], and of concern where they cause a delay in reporting the matter to the FCA, and in 2017 that they are "helpful starting points" but of "limited determinative value."[2]

If an internal investigation is carried out and the firm wishes to get recognition for cooperation from the regulator by providing a copy of the report, the firm should carefully consider the structure and work product, including whether the report or separate annexes to it will be privileged and whether it is willing to waive that privilege on a limited basis to the regulator. Summary reports can be a useful tool to enable communication of key findings with various stakeholders such as whistleblowers, the board, and the regulators while preserving confidentiality in a detailed privileged report. Discussing the proposed scope and purpose of the investigation with the FCA prior to commencing the investigation work will also assist. The FCA sets out guidance on its approach to these firm-commissioned reports in Chapter 3 of its Enforcement Guide.

By handling an internal investigation efficiently and effectively, and reporting promptly and accurately to the regulator throughout the process, a firm has the opportunity to reduce the negative outcome of any action taken by the regulator - for example by avoiding formal enforcement action or, in the event that enforcement action is taken, achieving a reduction in the level of fine imposed under the FCA's or PRA's fining policies.

Compliance Tip:

The key to a successful internal investigation is to be able to take a proactive approach to identifying and addressing any issues that may arise. Even where a firm has identified an issue at an early stage and taken steps to launch an internal investigation, the opportunity to dictate the scope and outcome of an investigation may nonetheless be lost.

This may arise where the regulator is not satisfied that the firm has the resources and/or expertise to conduct the investigation, or where the regulator is alerted to the issue from another source. Even if the ultimate outcome of an internal investigation is the commencement of disciplinary action by the regulator, firms will generally be given credit for early identification, notification and clarification of an issue. Such credit may be in the form of a decision by the regulator not to take action, or a reduction in the level of the penalty that the regulator decides to apply. It may also be possible to focus the scope of the regulatory intervention to the facts as established by the internal investigation and avoid the prospect of the regulator commencing its own fresh enquiries.

The key messages are:

- the need for good systems and controls to facilitate early identification of an issue requiring investigation;
- immediate consideration of notifications to regulators and, for listed companies, to the market;
- establishing systems and procedures to ensure that an internal investigation can be instigated and carried out within a short timeframe;
- considering whether the issue to be investigated may have resulted in a breach by the firm of its regulatory or legal obligations, and/or detriment to customers;
- planning the purpose, scope, governance, and output of an investigation in advance of commencing it;
- dealing with issues raised by an investigation in a proactive way so as to minimise the risk of regulatory intervention, including positive steps to address improvements identified, any customer impact and considering a remedial action programme; and
- keeping senior management informed and aware of their responsibilities.

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[1] as described by FCA Head of Enforcement Mark Steward in a conference speech on June 9, 2016.

[2] Click here to view this document

Internal and external triggers

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The matters or events that might trigger an internal investigation into whether a firm or an individual has engaged in conduct which breaches regulatory or other legal obligations might include, for example, the discovery of a fraud or other misconduct by the firm itself, allegations made by whistleblowers, issues arising from disputes with clients, problems identified via internal monitoring, issues raised with the firm by internal audit, compliance, external consultants or auditors, and issues raised with the firm by regulatory or law enforcement authorities.

In practice, the trigger event will often determine the extent to which the firm is capable of managing and conducting the investigation itself.

If the event arises as a result of an external source, a firm's ability to be proactive in taking control of the investigation may be compromised. Even in these circumstances, however, swift and positive action may allow a firm to regain the initiative and avoid a situation where the FCA or PRA steps in and takes over.

Examples of external trigger events include the following:

- a customer complaint (oral or written) or civil claim against the firm;
- a whistleblower report;
- a tip off, by anonymous letter or telephone call;
- an issue raised by the firm's auditors;
- an internal report seen by the FCA/PRA during a routine supervision visit;
- a request for information from an external body, including the FCA, the Financial Services Ombudsman, the Serious Fraud Office (**SFO**) and the NCA; and
- notice of an FCA/PRA investigation/intervention or investigation by another enforcement agency or regulatory body.

The whistleblowing context and applicable rules are considered further below.

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Escalation procedures

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Irrespective of where the trigger event arose, once a potential investigation has been identified, it is vital that senior management is informed. A firm will want to ensure that the firm's escalation procedures are adhered to. The substantive accuracy and effectiveness of escalation procedures, including clarity as to personal responsibility for escalation, are receiving increasing regulatory scrutiny. The FCA has recently criticised firms' escalation and updating procedures in Final Notices, where they concluded that poor escalation and monitoring of issues contributed to slow response and remediation. So procedures can be extremely important, particularly in large organisations where issues can more easily lose momentum and progress can be difficult to identify.

The firm's expectation of the type of issues which should be escalated must be clearly expressed in the firm's procedures, as should the identify of the individual responsible for each aspect or stage of escalation.

When considering the individuals to whom matters are to be escalated, a firm must ensure that the individuals are "appropriate". This means that the individuals must have the necessary skills and experience to consider and understand the implications of an issue and have the authority to launch an internal investigation, or take other appropriate action. They should also have the requisite degree of objectivity, able to manage any residual conflict of interest, and where appropriate a degree of independence.

Use of the term "independent" by external investigators, including lawyers, has become more closely scrutinised recently by courts, the press and by Parliament. Care should be taken in using the term "independent", both for its impact on claiming legal privilege (which it can undermine) and in how it is explained to auditors and witnesses.

The firm will need to consider carefully what information should be escalated and how that should be done in light of the importance of ensuring that legal privilege is not compromised in relation to relevant communications and documents. It is essential to identify a client team and restrict the distribution of privileged material to that client team in order to help preserve legal advice privilege.

In circumstances where the "appropriate person" is absent from the office, the firm's procedures should ensure that any communications which could potentially trigger an investigation are re-directed to another member of staff.

Compliance Tip:

Review escalation procedures in light of recent FCA enforcement decisions to ensure that they are clear as to who is responsible for escalation, to whom they should escalate the information, the quality and detail of information to be provided and the ongoing updating process and governance.

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Raising staff awareness

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It is important that a firm trains its staff to recognise when particular matters might need to be escalated - for example, complaints, suspicions of criminality or breaches of law, or regulatory requirements involving colleagues, customers or other parties. In practice, the FCA or PRA will generally communicate matters that are likely to prompt an investigation to the Chief Executive or individuals with whom the FCA/PRA has day-to-day contact from a supervisory or other perspective, such as those working in legal, compliance or regulatory relations teams. Firms should bear in mind that any member of staff could potentially receive information that could prompt an investigation, and should therefore consider training and briefing a wider population of relevant staff.

It is also important that protocols are put in place at the start of an investigation or escalation of an issue to ensure that communications about it are appropriate. Thought should be given to how such communications may appear if produced to a regulator or third party, and where such communications can be avoided without the protection of legal privilege, since they could become discloseable in any related litigation or investigation. For example, documents such as witness interviews are unlikely to be privileged where litigation is not in contemplation. Investigation reports and notes of witness interviews should be prepared on the understanding that the firm may have to waive privilege in due course. Individuals who may become witnesses and have some first-hand knowledge of events and all those involved in the process, should be warned to communicate carefully and with circumspection to avoid speculation or other informal communications being recorded in writing. Staff should be reminded that social media platforms such as instant messenger in addition to email and recorded lines could fall to be disclosed.

Compliance Tip:

At an early stage in any investigation, it is crucial that all potentially relevant members of staff are given guidance to respond in an appropriate way. The use of e-mail, instant messenger and other social media for example, to escalate or discuss an emerging issue or investigation, may lead to staff forwarding or discussing sensitive information in an unguarded way and in a non-privileged setting. This may have repercussions at a later stage if the firm is required to disclose documents.

Equally, in some circumstances, especially when events are changing rapidly, oral communications risk being ignored or overlooked and not recorded. It may, therefore, be helpful to develop a short written form template for staff to record the basic details of a matter to be escalated to the compliance department, or an in-house legal team, together with accompanying guidance notes.

The template could be incorporated within the staff procedures (in either the written or the on-line version). This may help to restrict the likelihood of disclosure of unhelpful, or potentially damaging, information at an early stage. It might also prompt employees to escalate matters to the "appropriate person".

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Document preservation

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Early steps should be taken to issue document preservation instructions in order to secure (but not necessarily as this point harvest) potentially relevant evidence. The appropriate instructions will depend on the nature of the issue, the level of sensitivity and the location of material, but thought should be given to instructing IT departments to suspend routine destruction programs. This could include putting a halt on the automatic over-writing of back-up tapes, and retaining any telephone records, web and phone logs. It is important to have regard to all forms of electronic communications and retrieve data likely to be needed (for example older data on back-up tapes which are harder to identify and copy). Thought should be given to the various types of device and communication tools, including phones and any instant messaging platforms, handheld devices and security passes. Careful consideration should also be given to the dissemination of a document retention notice (so as not to risk any "tipping off" incident if the recipients include suspects) and who should be told not to attempt to destroy material. For example, where criminal wrongdoing is suspected, it might be appropriate to capture data first.

Early consideration should also be given to applicable data protection and privacy laws. These laws impose restrictions around the review of employees' personal data, in particular where covert searches are anticipated. In the UK, firms should consider conducting a Data Protection Impact Assessment in compliance with the General Data Protection Regulation. There are a number of gateways permitting harvesting of data but the applicability of these should be considered at the outset. Other jurisdictions have additional legislation concerning use and removal of data, and so local laws should be consulted in respect of any data held overseas. Penalties for breach can be significant (including criminal sanctions), and may impact the admissibility of evidence in any subsequent proceedings (e.g. in relation to termination of employment) in certain jurisdictions, so local advice should be obtained in advance of such searches and of transfer of data.

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Establishing the purpose, governance and output of the investigation

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As soon as a firm establishes that it is necessary to conduct an internal investigation, it will need to think ahead to what the purpose of the investigation is, and what the output will be. These matters are essential to define in order to identify risks and to conduct the investigation appropriately and efficiently. A governance framework should also be devised. A small team should be established to lead any investigation. Involving lawyers will assist in establishing privilege, which is a difficult area of law at present and requires particular consideration. The method and form of reporting to senior managers and other stakeholders should be carefully. Identifying and managing potential conflicts of interest should be considered and addressed early on in the process. That analysis will influence the team used.

It is vital, at the outset, that the various "stakeholders" in the investigation -- for example, the firm's senior management team, human resources, legal, compliance, internal audit and the relevant business unit -- discuss and agree the objectives and scope of the investigation. It may also be important to involve the communications or reputation management team at an early stage.

Compliance Tip:

In general terms, the main objectives of an internal investigation should be to:

- understand and assess the nature and scope of what has occurred together with the degree of knowledge and involvement of relevant individuals (including the extent to which individuals ought to have been aware even if in fact they were not);
- ensure that evidence is secured and preserved;
- assess the effect the issue will have on the firm's business and take appropriate steps to mitigate any ongoing impact;
- identify any breakdown in systems and controls and/or breaches of internal processes and procedures;
- identify whether customers have been disadvantaged and quantify any loss, or propose a methodology to do so;
- minimise the impact of an identified issue in order to give the firm time to propose a remedial course of action;
- report promptly at an appropriate level internally and externally;
- prevent or manage adverse publicity as far as possible;
- decide how to manage communications with staff;
- provide recommendations for enhancements and lessons learned; and
- maintain a good relationship with the regulator(s).

Where an internal investigation is proposed in response to a concern expressed by the regulator, the objectives of the investigation are likely to be the same or similar to those set out above. In such circumstances, however, a firm must also seek to reassure the regulator that it has adequate resources and expertise to manage the investigation, and that the investigation will be independent, always keeping in mind the extent to which the investigation may distract the internal investigators from their usual day-job.

If a firm can assure the FCA/PRA that it is properly handling an investigation, it may discourage them from appointing external investigators (or it may help to limit the scope of such external investigation). As noted above, the firm should consider engaging with the appropriate regulator at an early stage to agree the parameters of the investigation and how it will be conducted.

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Developing the action plan

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Once the objectives of the investigation have been agreed, a firm may find it helpful to prepare an action plan to address the scope and timetable for the investigation. The complexity of the plan will depend largely upon the size of the firm, the nature of the matters under investigation and the timescales involved. At its simplest, the plan should deal with the following:

- the scope of the investigation, including relevant business areas and jurisdictions;
- which areas will be reviewed;
- tasks to be assigned to named individuals;
- whether any tasks may require the involvement of external parties such as professional advisers;
- an investigation timetable;
- anticipated interim reporting both internal and external; and
- identification of dependencies within the plan and clarification of timescales.

The existence of a written plan will enable senior stakeholders to assess the progress of the investigation and to demonstrate that the investigation is being conducted within an agreed set of parameters. It may be necessary to amend the plan as the investigation proceeds to take account of any new developments. It will also be important to identify early on where immediate interim remedial measures should be taken to mitigate any potential loss, detriment to customers and/or the risk of any misconduct recurring. The firm should consider engaging with the FCA/PRA on such steps and keep the regulator informed of developments throughout the investigation process.

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Deciding to use an internal or external investigation team

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Once the firm has decided to launch an internal investigation, one of the first considerations is to determine whether the matter can be dealt with by an in-house team, or whether the investigation should be carried out by an external professional firm. It may be possible (and necessary in urgent cases) for an individual to carry out an internal investigation. In other cases, it may be necessary to establish a team of individuals, drawn from different disciplines within the firm and externally, to deal with the issues raised by the investigation.

Using an in-house team to conduct the investigation may be advantageous as team members will be familiar with the firm's policies and procedures, its business and its employees. This may result in the investigation being concluded more quickly. The main disadvantages of using an in-house team can be that duties may need to be temporarily re-allocated to other members of staff, it may not be seen as sufficiently independent and (if particularly lawyers are not involved) the scope for protecting the working papers with legal privilege is lower.

The advantage of employing an external professional firm is that the firm will obtain access to specialist legal and forensic expertise, will be able to bring an objective approach and, will present less disruption to existing workload - although will of course entail fees. The FCA and PRA may look more favourably upon a report prepared by a recognised external professional firm, particularly as such firms should be familiar with the type of report required in the circumstances and are more likely to be considered neutral and objective - provided the investigation terms of reference make clear that is their remit. This is particularly likely to be the case where the issues under investigation raise questions with regard to the nature or strength of the firm's systems and controls or it otherwise becomes difficult to identify an internal team with sufficient authority and/or absence of conflict of interest. In some cases confidentiality and discretion, which may impact fairness on individuals being investigated, could point toward an external team.

A key factor to consider will be whether aspects of the investigation work can be structured to attract legal professional privilege. In order to maximise the possibility that the output of the investigation is subject to legal professional privilege, the investigation should normally be led by in-house counsel (provided they are clearly acting in a legal, as opposed to a business advisory, capacity) or an external law firm. Legal privilege may be particularly important to the firm where the issues being investigated could give rise to litigation or employment claims or government investigations and the firm wants to protect material from being disclosed.

Compliance Tip:

The decision to use an internal team, or to appoint an external professional firm, will depend upon a number of factors, including:

- the resources available to the firm in terms of staff and money;
- the expertise and experience of the in-house team;
- the timeframe within which the investigation must be carried out;
- the sensitivity or potential seriousness of the issue; and
- the importance of retaining legal professional privilege.

Whatever route the firm chooses to take, it is important to ensure that it does not focus on the matter that is the subject of the investigation to the detriment of other important considerations. It is important that compliance or other staff are not taken away from tasks which will leave other aspects of the firm's risk management exposed.

A blend of in-house and external professional representation on an investigating team is common and may be appropriate and could be considered, particularly where an external professional firm has a close working relationship with the firm.

In any event, the investigating team should identify the stakeholders (client team in privilege terms) to whom it is requested to report and keep them updated on developments in the investigation. It may be that in some circumstances, for instance where a whistleblowing claim has been made and an allegation of victimisation could be made, that the matter will be kept more separate from senior individuals who might otherwise be kept informed.

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Resourcing an investigation

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The resourcing of an investigation will depend greatly on the nature and extent of the underlying issues to be investigated. Whether an investigation team is appropriate, and the composition of any such team will have to be considered on a case-by-case basis depending on the type of issue under investigation and the type of experience that is required. An investigation team will, however, often include the following individuals:

- a team leader, who is a member of, or in direct communication with, the Board or other governing body (possibly a non-executive director);
- a senior legal person, to advise on detailed rules and other issues such as legal privilege, data protection and confidentiality;
- a member of internal audit, or an accountant, to consider any detailed financial and/or accounting issues;
- a senior IT person;
- a member of staff from the business unit(s) relevant to the investigation, but only to the extent that they are not implicated or involved in the matter to which the investigation relates;
- a member of the HR team, who can act as a liaison between the investigation team and any employees impacted by the investigation; and
- a secretary, paralegal or other member of clerical staff to undertake filing, copying, and other administration work.

Firms will need to ensure that the individuals do not hold any responsibilities or functions which could be said to give rise to a conflicts of interest with the subject matter of the investigation

Once the team has been identified, individuals should be briefed on their roles, the terms of reference of the investigation, timescales for reporting, confidentiality issues, mode of communication during the investigation (so as to protect legal professional privilege) and other relevant matters. The team leader should coordinate the efforts of the team and report to the senior management on a regular basis.

If key members of staff are to join the investigation team, with the result that they are likely to be taken away from their normal activities, it may be necessary for the firm to re-allocate responsibilities. This will be particularly relevant to compliance, legal and audit, as well as staff in operational areas who may be carrying out other important regulatory and risk management functions.

Firms should note that failure to staff a particular business unit properly can lead to action against the firm for failing to have appropriate systems and controls in place, and/or to individual disciplinary action against the firm's SMF Managers (see, for example, APER 4.5.9G(3)).

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Accommodating the investigation team

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Practical arrangements for accommodating the investigating team can be planned in advance and may include the following:

- a dedicated room, with access to telephones, photocopying facilities and lockable storage, ideally away from the business;
- making laptops, voice recording and other equipment available for use by the team, where necessary;
- the services of support staff;
- lists of senior management contact telephone numbers, e-mail addresses etc (kept up to date) and contact details for other individuals who may need to be contacted (for example, IT personnel);
- outline of any necessary draft board resolutions (or equivalent) authorising an internal investigation and guidelines on how to secure senior management approval for an urgent investigation outside working hours;
- arrangements for the secure storage of confidential documents;
- a protocol for copying and removing documents and for creating the investigation report and other written material during the course of the investigation.

As much as possible should be organised or prepared in advance and relevant staff should be trained to carry out the procedures should the need arise.

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Managing staff and public relations

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The question of whether to disclose that an investigation has been launched, and the related issue of deciding to whom this information should be disclosed, must be addressed at an early stage. Where the investigation has been triggered by notification of information from the FCA or the PRA, consideration should be given to the provisions of s348 of FSMA 2000 and whether an obligation of confidentiality arises. Firms whose securities are listed will also need to carefully consider whether obligations arise to disclose matters to relevant markets / exchanges and, if so, at what point disclosure obligations might arise. Market and regulator notifications should be carefully coordinated. There may also be a need to notify auditors as part of the annual external audit process. Similarly insurance coverage and notifications should be assessed in appropriate cases to avoid losing possible coverage.

Where a matter is likely to become public and is significant, the firm should brief its internal PR staff, and prepare draft press responses in the event of questions. Depending on its size and the likely attention of the issue, the firm might also consider retaining an external PR firm.

Those staff who will be questioned during the course of the investigation, the staff who are members of the investigating team, and the firm's senior management will need to be advised and kept informed as appropriate. The frequency and form of such updates should be agreed in advance as part of the plan. The question of whether all staff should be informed about an internal investigation, will depend on the size and culture of the organisation, and the subject matter of the investigation. There is a risk that rumours spreading around the organisation could disrupt work and affect staff morale. It could also lead to documents being produced in chats or emails (for example speculating on events) which become discloseable in an investigation or related litigation. The decision to make a staff announcement may also be influenced by the likelihood that the investigation will be "leaked" to the press or announced to the market. A firm should ensure that it has a policy governing staff relations to which it can refer for guidance in the event that it has to inform staff. It may be appropriate, for example, for a firm to conduct a short and confidential meeting with relevant staff to inform them that the organisation is investigating certain matters, in order to provide reassurance to staff and to inform them of the importance of keeping information confidential.

Compliance Tip:

The handling of publicity internally and externally will be amongst the most important matters for firms carrying out an internal investigation, and these issues are likely to be of significant concern to firms' senior management. How a firm responds to regulatory allegations, breaches or other misconduct can have a significant impact on their brand and reputation. Firms' interests may be served where they are perceived to be handling matters in a clear and transparent manner, and where they demonstrate a commitment to "putting right" any failings that have occurred. By contrast, a crisis handled badly can destroy brand reputation, employee morale, consumer and investor confidence and the chances of commercial success. Effective public relations planning and management are therefore crucial. The level of public and press interest in internal investigations has become increasingly difficult to predict in recent years, and it is easy for businesses to be caught out by unexpected disclosures and coverage.

A business should develop plans and strategies to manage a crisis in order to minimise any consequent reputational damage. The plan should include provisions to deal with all audiences who may affect the reputation of a firm and its ability to continue to operate. This includes the media, government, regulators, consumers and other third parties. Every situation is different, but in the context of regulatory intervention, the firm should as a minimum be:

- preparing and implementing a media relations plan;
- setting up a media and investigation response team if one does not already exist;
- drafting responses to media enquiries in advance and ensuring their accuracy by checking with relevant team members;
- monitoring developments on an ongoing basis;
- implementing an ongoing briefing plan for all key stakeholders -- staff, customers, regulators, peers, members of the public, government, etc; and
- reviewing events, reacting and preparing to change its approach as the situation shifts.

With an external public relations policy, the ultimate objective will be to ensure that the firm's stakeholders (customers, shareholders), and other third parties including the regulators, only receive information which has been approved and released by the firm's senior

management. Again, depending upon the size of the potential issue, a firm may wish to seek advice from an external public relations consultant to assist in managing the public relations issues.

Reporting findings to senior management

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One of the aims of most internal investigations will be to deliver a report, usually (though not always) in writing, to the Board or other governing body. This should outline:

- the nature and extent of issues, problems or failings identified;
- the root cause of any failings, including any failings in systems and controls identified;
- the potential risks arising for the firm as a result of the matters uncovered (e.g. legal risks, regulatory risks, risks to customers);
- the proposed solutions;
- whether any reporting obligations arise;
- whether any redress or remediation is appropriate; and
- the planned next steps.

In some circumstances, for example where feedback is to be shared with a whistleblower in accordance with SYSC 18 or otherwise to help resolve the matter, the firm might consider producing a short summary report and a more detailed set of findings over which privilege can be retained.

The internal investigation report is an important document that may succeed in heading off regulatory intervention. The firm should aim to:

- address any particular concerns raised by the FCA, PRA or others, as appropriate - for example, addressing perceived deficiencies in systems and controls, or developing new policies and procedures aimed at preventing recurrence of the breach;
- provide relevant background information, organisation charts, technical information as and where necessary to assist in the understanding of an issue;
- set out the facts in a clear and concise manner;
- outline steps already taken to address the issue(s) and prevent recurrence; and
- propose remedial action or next steps, having regard to the FCA or PRA's statutory objectives (e.g., consumer protection, reduction of financial crime).

The report should usually be presented to the Board (or key members of it), or other governing body, in a way that facilitates consideration of the issues raised but without being open to the challenge that it has been inappropriately amended or softened, which might undermine its validity. A regulator or prosecuting authority may ask for drafts of the report in order to test this risk, which the firm may wish to waive any privilege. The outcome of the meeting should be to secure the Board's commitment to the next steps, including any regulatory notification/update and, where relevant, to achieve redress. To meet the senior management's collective and individual obligations, the fact that the matter was fully considered, and the action steps agreed, should be carefully documented.

Compliance Tip:

The written report may eventually need to be made available to the FCA or PRA (or other authorities) even where it is privileged, where the firm decides to do so for strategic or relationship reasons. In many cases, a firm will have notified the appropriate regulator of the existence of an internal investigation and the regulator will be expecting a copy of the written report. A decision will need to be made about providing the report and on what basis this is done (for example, by doing so under a limited waiver of privilege to help preserve privilege against third parties).

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Conducting staff interviews

The Compliance Handbook 000000019

As part of an internal investigation, it may be necessary to interview employees, directors or other individuals who work with, or for, the firm. It is important that the investigating team adheres to the firm's policies for dealing with staff and acts in accordance with employment law. Ideally, a protocol regarding staff interviews should be available for the investigating team to use in these circumstances. In addition, the investigating team may need to coordinate with employment lawyers, for example, if any of the interviews are of a whistleblower or any witnesses could be asked questions which have a disciplinary impact. The FCA or other regulators may request that particular individuals are interviewed and/or that interviews are conducted under certain conditions, including that no privilege is claimed over them. For example, the FCA or other regulators may request that an interview be recorded and that any recording be provided.

Wilt it is likely that interviewees will need to be given a notice known colloquially as an "Upjohn warning"[3] at the start of interviews held by lawyers which explain that the lawyer acts for the firm and not the individual employee, that any privilege attaching to the interview belongs to the firm not the individual, and that the firm may waive the privilege. These warnings can lead to difficult questions from employees about whether they should have their own lawyer, and can lead to interviews terminating. Firms will need to consider how to address these situations, and balance the need to be co-operative with the regulators and obtain information with other issues, such as treating employees fairly.

Compliance Tip:

It is often helpful to emphasise that the purpose of the investigation is to identify the facts and relevant circumstances. However, the investigation team should be careful to avoid any suggestion that the employee concerned will not be subject to disciplinary proceedings or that their evidence will not be used since that action may prove necessary depending on the outcome of the investigation. Consideration should be given to providing interviewees with some information prior to the interview so that they know what to expect. Questions which may need to be answered before or during the interview include:

- Who will be present at the interview?
- How long is it expected to last?
- Will the interview be recorded, and will the interviewee be entitled to a copy of the transcript, or any other notes taken? NB any privilege which may attach to notes or other records of the interview may be lost if a copy is provided.
- Will notes or other records of the interview be passed to any regulatory or law enforcement authority? A decision may not yet have been taken but the employee should be informed of the firm's right to waive privilege in interview notes including by transmitting them to the authorities.
- Can the interviewee have someone else present (e.g., an independent legal advisor, or union representative)?
- What is the interview about and what particular areas does the firm wish to focus on?
- Will the interviewee be provided with an opportunity to review any relevant documents (for example, emails) prior to the interview?
- Would it be appropriate to allow the interviewee to take some time out from day-to-day duties to enable the interviewee to prepare?
- Can answers be anonymous or will I be able to be identified? If so, to who?
- What happens next?

Only a team member with appropriate experience and skills should conduct interviews for the purposes of an internal investigation. It may be appropriate for this part of the investigation process to be delegated to an external resource. The interviewer will need to prepare carefully for the interview and a detailed note or transcript of the interview should be made. Another individual who will take notes and/or operate recording equipment should generally accompany the interviewer. Firms will need to consider the issue of legal privilege when conducting any interview and determining what records should be made. The issue of when legal privilege arises in the context of an interview with a witness conducted as part of an internal investigation is an area of considerable difficulty at present and depends on various considerations and factual circumstances. The investigating team should ensure that they are properly advised

on this topic before undertaking an interview. Where any critical new information is disclosed during the course of an interview, there should be an established process enabling the interviewer to report the information to the team leader.

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[3] a name derived from the US case Upjohn Company v. United States (449 U.S. 383 (1981))

Disciplining staff

The Compliance Handbook 000000020

Where a member of staff is suspected of serious wrongdoing which may pose a threat to the company, amount to a breach of the FCA's conduct rules, or impact on fitness and propriety (for certified persons and SMF Managers) and/or that may ultimately lead to dismissal, the firm's employment procedures should provide for staff to be suspended, pending the outcome of an investigation. In this way, the firm is in a position to use the employee's obligations to the firm as a means of continuing to seek information and assistance from the employee as part of any internal investigation. However, suspensions are considered to be a draconian step in the UK, so careful consideration should be given to whether the suspension is appropriate and in accordance with employment law. An alternative may be to transfer the employee to an entirely different role where he can be securely ring-fenced from the matters under investigation. However, this will generally only be feasible if the employee does not pose an immediate risk to the business, cannot tamper with the evidence or interfere with witnesses and if the employee's contract permits such a step. In some cases conduct may be so serious as to require dismissal. The regulator should be consulted in appropriate cases where the firm is determining what steps to take.

Where an SMF Manager has been suspended from their normal duties, the firm should give immediate consideration to filing a "qualified" Form C with the FCA or PRA as appropriate (see SUP 10.A.14 (for FCA Approved Persons) and PRA Rulebook: Senior Managers Regime - Applications and/or Notifications (for PRA Approved Persons).

Compliance Tip:

Where the fitness and propriety of an individual employee has been called into question pending the outcome of an internal investigation, a firm may wish to consider any practical steps it may take to protect its position:

- consider the individual's security access and whether it can/should be removed, or whether the individual should be closely supervised;
- if the individual is in a customer-facing role, it may be prudent to conduct a sample check of customer files, even if the allegations are not directly linked to dealings with customers however consideration should be given to data protection issues arising from such a step;
- make sure that the individual is not in a position to cause harm to the company or its customers; and
- address as a matter of urgency any systems and controls deficiencies which the matter has revealed.

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Internal reporting and defamation

The Compliance Handbook 000000021

Any internal reporting on the progress and findings of an internal investigation is important management information. Firms should note that care must be exercised in the production and circulation of such reports, not only to safeguard against a loss of privilege and to protect a whistleblower's identity and right to confidentiality, but also to avoid the risk of defamation. The author of an internal report can potentially find himself, or herself, the target of a claim for defamation by an individual named in a report, even if the report has been circulated only within the firm. While there are defences to such a claim, including justification (i.e., that the contents of the report are true), defending any action is likely to be an expensive and time-consuming exercise.

Generally, the risk of successful claims for defamation can be lowered if the author of an internal report follows certain guidelines, though specialist advice should always be taken and the risks will depend on the circumstances. Considerations include the following:

- • Be clear and concise in reporting facts and conclusions. Consider carefully before engaging in speculation, or report unsubstantiated comments.
- • Do not name individuals unless necessary and avoid naming third parties.
- • Limit the circulation of the report to those who have a legitimate interest, or a duty to receive it, and circulate using an appropriate method of communication.
- • For major "open" reports which may be published, consider a form of "maxwellisation" process which gives key individuals who are criticised an opportunity to comment prior to publication.

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When is it necessary to notify FCA or PRA?

The Compliance Handbook 000000023

As soon as a firm becomes aware of information having a regulatory impact it should consider its obligations to notify the PRA and FCA. The notification obligations arise under Principle 11 of the FCA's Principles for Businesses and the PRA's Fundamental Rule 7, as well as within SUP15 of the FCA Handbook and the Notifications chapters in the PRA Rulebook. These rules should be considered carefully.

In practice, when a firm becomes aware of an issue requiring internal investigation, it is likely to be appropriate to notify the FCA under Principle 11 and, where applicable the PRA under Fundamental Rule 7. In more significant cases, the FCA/PRA will expect to be informed of (and consulted on the scope of) any planned investigation and to be kept informed of the progress as well as the outcome and any immediate interim remedial steps taken.

Where a notification is made orally to a contact at the regulator in the first instance, the firm should consider following this up in writing to enable it to evidence the content and date of the information it provided and to avoid any misunderstandings.

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Notifying the FCA under SUP 15 of the FCA Handbook

The Compliance Handbook 000000024

SUP 15.3.1 provides that the firm must notify the FCA "immediately it becomes aware, or has information which reasonably suggests, that one of the following events has, or may have occurred, or may occur in the foreseeable future". There follows a detailed set of rules and circumstances which should be considered carefully. They include, in summary:

- failure by the firm to comply with one or more of the threshold conditions for authorisation;
- any matter that could have a serious adverse impact on the firm's reputation;
- any matter that could affect the firm's ability to continue to provide adequate services to its customers and that could result in serious detriment to a customer of the firm;
- any matter in respect of the firm which could result in serious financial consequences to the financial system, or to other firms.

The FCA/PRA guidance on matters the meaning of "a serious regulatory impact" states that firms should consider both the probability of the event happening and the severity of the outcome should it happen (SUP 15.3.3G). In these circumstances, a firm is encouraged to notify its supervisory contact by telephone "or other prompt means of communication" before making a written notification (SUP 15.7.2G). This notification obligation applies to the most serious matters affecting a firm or the financial system.

Firms should have regard to the terms of the Final Notice in the matter of Hastings Insurance Services Limited, on July 24, 2008, in which the FSA appeared to criticise the firm for a delay of four days from the identification of a possible problem to notification of the issue to the regulator.

SUP 15 contains numerous other specific notification requires and should be considered in detail. Other SUP 15 provisions which may be relevant include:

SUP 15.3.11 requires a firm to make an immediate notification of any of the following:

- a significant breach of a rule (which includes a Principle, Statement of Principle, or a COCON rule);
- a significant breach of any requirement imposed by the Consumer Credit Act 1974 or by regulations or an order made under the Consumer Credit Act 1974;
- a breach of any requirement imposed by FSMA or by regulations or an order made under FSMA by the Treasury;
- a breach of any requirement imposed by or under either the Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017 (SI 2017/701) or the Data Reporting Services Regulations 2017 (SI 2017/699);
- the bringing of a prosecution for, or a conviction of, any offence under FSMA or the Consumer Credit Act 1974;
- a breach of an applicable provision imposed by MiFIR (Regulation (EU) No 600/2014) or any onshored regulations which were previously EU regulations adopted under MiFID (Directive 2014/65/EU) or MiFIR;
- a breach of an applicable provision in the UK Capital Requirements Regulation (UKCRR) or any onshored regulations which were previously EU Regulations adopted under the Capital Requirements Directives or under the UK CRR;
- a breach of any requirement in regulation 4C(3) (or any successor provision) of the Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2007;
- a breach of an applicable provision of the UK auctioning regulations;
- a breach of the AIFMD UK Regulation;
- a breach of the *benchmarks regulation* (apart from Annex II to that regulation) or of any applicable onshored regulations which were previously EU regulations or imposed under the *benchmarks regulation*; or
- a breach of any applicable onshored regulations which were previously EU regulations adopted under the Insurance Distribution Directive, Directive (EU) 2016/97;

by (or, as regards a prosecution, against) the firm or any of its directors, officers, employees, Approved Persons, appointed representatives or tied agents.

A firm must make a notification of the matters above immediately it becomes aware or has information which reasonably suggests that any of the matters set out above has occurred, may have occurred or may occur in the foreseeable future.

SUP 15.3.12G states that "significance" should be determined having regard to the following factors:

- potential financial losses to customers or to the firm;
- frequency of the breach;
- implications for the firm's systems and controls; and
- delays in identifying and rectifying the breach.

SUP 15.3.15R requires immediate notification of any civil, criminal or disciplinary proceedings against a firm. There are also detailed provisions in SUP 15.3.17R regarding notification of matters relating to fraud, errors and other irregularities. There are separate notification rules under SUP 15.3.26R applying to firms which are UK AIFMs (alternative investment fund managers), notifications relating to competition law infringements (SUP 15.3.32R); Lloyd's of London and insolvency, bankruptcy and winding up (SUP 15.3.21R).

There is separate provision in SUP 15.11 regarding notifications which may need to be made about individuals for breach of the COCON rule and disciplinary action. The firm should also consider the notification obligations in SUP 10C.14 regarding notifications about SMF Managers under the SMCR.

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FCA Principle 11 notifications

The Compliance Handbook 000000025

Principle 11 requires firms to "deal with its regulators in an open and cooperative way, and must disclose to the FCA appropriately anything relating to the firm of which that regulator would reasonably expect notice". Principle 11 is intended to be broad and to prompt the firm to consider carefully what information would be expected by the FCA. SUP 15.3.8G sets out a (very much) non-exhaustive list of the types of issues which should be disclosed to the appropriate regulator in accordance with Principle 11. These include any significant failure in the firm's systems and controls, including those reported to the firm by its auditor.

Here, the guidance states that the period of notice given to the appropriate regulator "will depend on the event", although it expects a firm to discuss relevant matters with it "at an early stage" and before making any "internal or external commitments", SUP 15.3.9R. This may imply some degree of flexibility in notification timescales, although the guidance emphasises the need to provide important information "promptly". Many larger firms will have an individual who is responsible for the FCA relationship and who will have a view on consistency and methodology of communication with the FCA. The content of a notification should be drafted carefully and clearly, and where appropriate with advice from external legal counsel.

Compliance Tip:

In practice, the decision if, and when, to make a notification to the FCA/PRA is a vital and difficult judgement that must be made at an appropriate level, usually by the Board or other governing body within a firm or senior compliance personnel.

Except for matters that have a serious regulatory impact or the matters specified in SUP 15.3.11R, notifications in accordance with Principle 11 may, in theory, be deferred for a short time to allow the firm to conduct initial enquiries to assess the impact and understand the nature and scale of the issue, so that clear information can be provided to the FCA. This timing will be a careful balance in many cases.

A firm is likely to enhance its position in the eyes of the relevant regulator by ensuring that any notification clearly outlines the issue identified and proposes a resolution, or a particular course of action.

Any decision to delay a notification under Principle 11 must, however, be taken on grounds which can be justified and should be fully documented. Relevant enquiries should obviously be taken within the shortest possible timescale. In particularly difficult cases, a firm may consider taking external professional advice on the need to make a notification.

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PRA Fundamental Rule 7 notifications

The Compliance Handbook 964552409

Fundamental Rule 11 mirrors the FCA's Principle 11 in its wording: "A firm must deal with its regulators in an open and cooperative way and must disclose to the PRA appropriately anything relating to the firm of which the PRA would reasonably expect notice." PRA regulated firms will need to consider whether this obligation is triggered by any events which prompt them notify the FCA, and cannot assume that the PRA would be content to receive information second hand from the FCA.

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PRA Notifications Chapters

The Compliance Handbook 964552408

There are separate notification requirements in the Notifications Chapter of each part of the PRA Rulebook applicable to different types of PRA regulate firm. These should be consulted whenever a PRA firm identifies an issue which may be notifiable.

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Notifying the appropriate regulator: What should a firm disclose?

The Compliance Handbook 000000026

An initial notification to a regulator about an identified issue should be drafted carefully to include relevant information and to identify the firm's planned response. The content will vary depending on the issue.

If a firm presents a report of its investigation to the appropriate regulator the report should usually include the following information:

- the nature and extent of the problem;
- how the problem arose;
- any breaches of policies and procedures identified or systems and control failings;
- the remedial action that has been taken; and
- the steps the firm has taken towards preventing any recurrence.

As a precaution, before presenting the report, a firm may wish to consider the issue of legal privilege (which is discussed in more detail below), and consider whether to share a non-privileged version of the Report (for example a short summary) to retain the option of retaining privilege over the detailed report; or to sharing the report on a limited waiver of privilege basis. Wherever possible, the firm should seek to distinguish between problems that have been identified as representing isolated events and those that may suggest systemic control weaknesses. In general the report should emphasise the firm's compliance effort and senior management commitment to promoting a compliant and ethical culture throughout the firm as well as its fact investigations and conclusions on the matters at hand.

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External reporting to other regulators

The Compliance Handbook 000000027

The requirements to notify the FCA and PRA are set out in detail above, but the firm must also identify any other regulators or third parties that may either require notice of an internal investigation or the issues arising from such an investigation or that may give credit for self-reporting. These may include:

- NCA;
- the relevant UK Listing Authority;
- the Information Commissioner;
- HM Revenue & Customs;
- the SFO;
- The Office of Financial Sanctions Implementation;
- overseas regulators or enforcement authorities;
- a market or an exchange; and
- the firm's insurers.

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Intervention by the regulator

The Compliance Handbook 000000029

The FCA and PRA have wide-ranging and significant powers of intervention and enforcement. These include a range of investigative powers which it can delegate to an "investigator" who may, or may not be a member of the relevant regulator's staff. The regulators' enforcement and investigation powers are considered in detail in a separate chapter.

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Avoiding regulatory intervention

The Compliance Handbook 000000030

One way that a firm might avoid regulatory intervention or enforcement is for the firm to persuade the FCA/PRA of the following:

- that the internal investigation was thorough and was conducted impartially and properly;
- that the firm has identified all of the issues and is taking immediate action to correct areas of weakness;
- that the firm has drawn up a plan offering redress or to take remedial action to correct any deficiencies which have been identified.

One of the principal aims of an internal investigation will be to seek to persuade the FCA/PRA that there is no need for it to undertake, or to commission, an additional investigation of the matter. Whether this is successful will of course depend on a range of fact-specific circumstances including the severity of the issues, the compliance history of the firm, and the enforcement priorities of the regulator.

If, however, the internal report raises significant senior management or systems and controls deficiencies, or any issue having a serious regulatory impact, then the FCA/PRA can instigate its own investigation, notwithstanding the fact that an internal investigation has already been carried out.

In these circumstances, even where the FCA/PRA is minded to commission a further investigation, it may still be possible for the firm to propose an alternative course of action in an effort to retain an element of control over the process. This could include:

- a second internal investigation with different or wider terms of reference;
- a report by the firm's external professional advisers; and
- nomination of a firm to carry out a s.166 FSMA skilled persons report.

In many cases, the firm may offer, and/or the FCA/PRA may instruct the firm, to carry out a past business review ("PBR") by way of remediation. This is where a firm is required to review all customer files, or a specified sample, in respect of a specific part(s) of its business (e.g., sale of investment products or loans), identify sales which are not compliant and proactively offer redress to those customers. The costs to a business of carrying out a PBR can be significant, in terms of loss of management time, in developing systems to record and analyse the data and in producing a report. If the firm lacks the resources to conduct such a review, a range of law firms and other professional services firms are able to do so. Where litigation is a risk, the firm may want to consider the value of legal privilege and the ability to advise on both the PBR and the litigation as relevant to who it chooses to appoint.

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Follow up task list

The Compliance Handbook 000000032

In case the regulator takes further action, and in any event to address issues identified during the investigation, the firm should consider taking some of the following steps:

- the position of individuals: is the conduct of any certified persons, conduct rules staff or SMF Managers implicated in the matters investigated and if so are any updates to regulatory references, fitness and propriety/conduct rule breach findings, reports to the regulator, or internal disciplinary measures appropriate?
- A plan should be devised to ensure that the action points identified during the investigation are implemented.
- A team (or an individual) should be made responsible for checking that the specific action points have been addressed and, where necessary, new procedures have been implemented.
- If the action points are not being addressed, the team should ensure that remedial action is taken. If necessary, the team should seek the support of senior management. Appropriate timescales should be agreed and monitored.
- There must be active follow up and record keeping. It is advisable to document the action taken so that the firm can demonstrate to the regulator that it took steps to rectify any problems.
- Progress with remedial action should be monitored by the Board (or other governing body) and/or by the senior management team and any action plan re-assessed and revised if necessary.
- Appoint someone responsible for managing any updates to the regulators which have been agreed or offered.
- If the investigation reveals systemic problems with wider ramifications or systemic failures, further action may be required. A firm should consider the bigger picture: for example, did the problem arise because the compliance department is under-resourced? Is the firm's senior management view of compliance sufficiently supportive, or are there problems with the firm's compliance culture - for example, are there systemic rule breaches indicating an absence of a compliance culture?

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Record keeping

The Compliance Handbook 000000033

It is essential to record the conclusions of the investigation, the remedial steps taken or required and the process of reviewing the progress of remedial actions. Even if the information is not to be made immediately available to the regulator, it is important to establish an audit trail for the work undertaken, in case the problem recurs or becomes relevant at some later stage. The firm should also keep an audit trail demonstrating how its risk assessments, policies and procedures have been recalibrated as a result of the incident and subsequent investigation and remediation. Under certain legislation such as The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 the FCA has a right to demand risk-assessments in relation to money laundering.

Documents created and collected during the investigation should be carefully reviewed at the conclusion and copied and retained where appropriate. The need to retain documentary evidence should be considered against the requirements under data protection legislation. Documents that may be legally privileged, should be separated and identified to ensure that they are not disclosed at some later stage. This process can be particularly useful in preparing for an FCA/PRA supervision visit or even a dawn raid.

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De-brief staff and other stakeholders

The Compliance Handbook 000000034

The firm should consider if, and how, the findings of an investigation should be communicated to staff and other stakeholders. Producing different documents tailored to different stakeholder audiences, rather than a single investigation report, will help to preserve legal privilege in detailed work, but enable high level feedback for other stakeholders. The need to de-brief staff, and to communicate with other stakeholders, will depend upon the extent to which the investigation has been made known; its findings; and whether the matter has reached the public domain. The firm may wish to consider using a specialist public relations firm for this task.

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Review policies and procedures

The Compliance Handbook 000000035

At the conclusion of an investigation, it may be necessary not only to deal with the immediate issues raised by the investigation, but also to consider whether any of the firm's risk identification and risk management policies could be improved.

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Whistleblowing

The Compliance Handbook 964552407

An internal investigation may be prompted by the disclosure of a reportable concern - a whistleblowing report. In such circumstances the firm will need to give careful thought to demonstrating ongoing compliance with the regulators' whistleblowing rules, and may also need to take employment law advice. Where, as is often the case, a whistleblowing report has occurred in conjunction with an employment dispute or disciplinary, careful coordination will be needed between the employment and investigation advisers and workstreams to ensure consistency and avoid repetition, or interacting with the whistleblower which is inappropriate in light of the wider context.

The EU Whistleblower Directive, which was enacted in December 2021, introduces, among other things, a requirement for organisations with 50 or more employees in the private sector irrespective of the nature of their activities. Despite the UK's departure from the EU, the Directive will still remain relevant for firms with wider EU operations. Consideration should be given to how the Directive is implemented in local jurisdictions within the EU.

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Why whistleblowing policies are necessary

The Compliance Handbook 000000037

Since 1999, the Public Interest Disclosure Act ("PIDA") has afforded statutory protection for workers who make "protected disclosures" (that is, "blow the whistle"). The FCA rules on whistleblowing are contained in SYSC 18 and the PRA's rules are in "General Organisational Requirements" (for banks) and "Whistleblowing" (for Solvency II firms) chapters of the PRA handbook. The PRA has also issued an explanatory supervisory statement (SS39/15). The rules are binding on deposit-takers with over £250m in assets, PRA-designated investment firms and to Solvency II insurers. For other firms, they act as non-binding guidance.

SYSC 18 of the FCA handbook reminds firms of the provisions of PIDA and contains additional requirements regarding internal whistleblowing procedures, conduct of whistleblowing investigations, and the appointment of a whistleblowers' champion.

These rules apply to protect whistleblowers who raise "reportable concerns", which is not identical in scope to the definition of those who qualify for protection under PIDA. A whistleblower covers any person that has disclosed or intends to disclose a reportable concern to a firm, to the FCA or the PRA or in accordance with Part 4A (Protected Disclosures) of the Employment Rights Act 1996. A reportable concern covers a concern held by any person in relation to the activities of a firm, including: (a) anything that would be the subject matter of a protected disclosure, including breaches of rules; (b) a breach of the firm's policies and procedures; and (c) behaviour that harms or is likely to harm the reputation and financial well-being of the firm.

The FCA has stated that it would regard as a serious matter any evidence that a firm had acted to the detriment of a whistleblower. Such evidence could lead the FCA to question the fitness and propriety of the firm, or relevant members of staff, and could lead to authorisation or approval being withdrawn) (SYSC 18.3.9R). In essence, the absence of an effective policy could ultimately lead to loss of a firm's business or an individual's ability to work in the industry

Firms therefore need to give careful thought to their obligations, and the rights of whistleblowers, when conducting an internal investigation arising from a reportable concern.

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Nature of whistleblowing arrangements

The Compliance Handbook 000000038

For larger firms covered by the FCA and PRA whistleblowing rules, appropriate and effective UK internal procedures must include the following:

- arrangements to handle disclosures of reportable concerns where the whistleblower has requested confidentiality or has chosen not to reveal their identity;
- an ability for disclosures to be made through a range of communication methods;
- arrangements to ensure the effective assessment and escalation of reportable concerns by whistleblowers including to the FCA or the PRA. The Firm's employee handbook or other equivalent document must explain that (a) reporting to the PRA or to the FCA is not conditional on a report first being made internally; (b) it is possible to report using the firm's internal arrangements and also to the PRA or to the FCA (these routes can be used simultaneously or consecutively); (c) it is not necessary for a disclosure to be made to the firm first.
- an assurance that, where a reportable concern has been made, the firm will take steps to ensure that no person under its control engages in victimisation against that person for making that disclosure;
- the provision of feedback to a whistleblower about a reportable concern made to the firm, where this is feasible and appropriate;
- the retention of appropriate records of reportable concerns by whistleblowers, the firm's treatment of these reports and the outcome;
- the preparation of an annual report to the firm's governing body on the operation and effectiveness of its systems and controls in relation to whistleblowing, which report must maintain the confidentiality of individual whistleblowers;
- prompt reports to the FCA about each case the firm contested but lost before an Employment Tribunal where the claimant successfully based all or part of their claim on whistleblowing detriment or dismissal;
- appropriate training for UK-based employees, managers of UK-based employees (wherever the manager is based) and employees responsible for operating the firm's internal arrangements.

  training for UK-based employees must include: (a) a statement that the firm takes the making of reportable concerns seriously; (b) a reference to the ability to make reportable concerns and the methods for doing so; (c) examples of events that might prompt the making of a reportable concern; (d) examples of the action that might be taken by the firm after receiving a reportable concern, including measures to protect the whistleblower's confidentiality; and (e) information about sources of external support such as whistleblowing charities.

  training for managers of UK-based employees must include: (a) how to recognize when there has been a disclosure of a reportable concern; (b) how to protect whistleblowers and ensure confidentiality is preserved; (c) how to provide feedback to a whistleblower where appropriate; (d) steps to ensure fair treatment of any person accused of wrongdoing by a whistleblower; and (e) sources of internal and external advice and support on such matters;

  training for employees responsible for operating the firm's whistleblowing procedures must include how to: (a) protect a whistleblower's confidentiality; (b) assess and grade the significance of information provided by whistleblowers; and (c) assist the whistleblowers' champion.
- written procedures in accordance with SYSC 18.3.1R(e)(ii).

The procedures may also include:

- a clear statement that the firm takes failures seriously;
- an indication of what is regarded as a failure;
- clarification that there may be other appropriate routes for some issues, such as grievances or consumer complaints, but the internal arrangements can be used to blow the whistle after alternative routes have been exhausted in relation to the effectiveness or efficiency of the routes;

- the opportunity to raise concerns outside the line management structure, such as with the compliance director, internal auditor or company secretary;
- provision of access to an external body such as an independent charity for advice;
- making whistleblowing procedures accessible to staff of key contractors (as the definition of a whistleblower is not limited to the firm's workers);
- a statement that nothing prevents the firm from taking action against those who have made false and malicious disclosures.

The Whistleblowers' Champion

It is also necessary to allocate senior management responsibility for acting as the firm's whistleblowers' champion (SYSC 18.4.1G). The whistleblowers' champion is responsible for ensuring and overseeing the integrity, independent and effectiveness of the firm's whistleblowing policies and procedures, including those intended to protect whistleblowers from being victimized because they have disclosed reportable concerns (SYSC 18.4.4R).

The whistleblowers' champion should have the level of authority and independence and access to resources (including legal advice and training) and information sufficient to enable him or her to carry out that responsibility. They need not have a day-to-day operational role handling disclosures from whistleblowers (SYSC 18.4.5)

Thought will need to be given to the level of oversight the whistleblowers' champion has of an internal investigation, and any related employment action, arising from the disclosure of a reportable concern, and that person's interaction with the whistleblower.

Settlement Agreements

A firm must include a term in any settlement agreement which states that nothing in the agreement prevents a worker from disclosing a reportable concer. Firms must not ask workers to enter into warranties which require them to disclose to the firm that they have made a protected disclosure or that they know of no information which could form the basis of a protected disclosure. Firms must not use measures intended to prevent workers from making protected disclosures (SYSC 18.5R).

The PRA rules also make it clear that wording in employment contracts should not deter staff from whistleblowing.

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Efficacy of arrangements

The Compliance Handbook 000000039

Many firms will have existing whistleblowing policies in place, but the key is to ensure that the policy is effective. If, for example, no calls have ever been made to a "whistleblowers' hotline", a firm may wish to consider whether its existence has been properly communicated to staff. To be effective, whistleblowing procedures must be communicated to staff in a positive way and reinforced by regular reminder, and firms must be able to identify "reportable concerns" effectively. The Board (or other governing body) must commit to the policy and staff must see the culture of the organisation as being conducive to supporting such a policy. It is important for the firm to act with due skill, care and diligence when dealing with whistleblower allegations including ensuring that the investigation team has proper control of the investigation process, does not have a conflict of interest and is impartial.

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Claiming privilege

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The purpose behind the doctrine of legal professional privilege is that clients must be able to consult their lawyer openly and in confidence, without fear that such communications may subsequently be used against them in legal proceedings.

Communications between in-house or external lawyers and any staff or their clients for the dominant purpose of seeking legal advice, may benefit from legal professional privilege, and where litigation is reasonably in contemplation, certain communications with third parties may also be protected. It should, however, be noted that in continental European countries privilege may not be available to in-house lawyers, and may also have a limited application over documents, so care should be exercised outside the UK. Documents covered by legal professional privilege are protected from disclosure. Privilege is, therefore, a very important issue to consider when handling an internal investigation, in particular where it appears that the matters under investigation give rise to potential regulatory, complaints, or litigation risk. The law on privilege is currently evolving and is complex and careful expert legal advice should be taken both on what communications are likely to be privileged and on what documents can be withheld from disclosure as privileged.

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Types of legal privilege

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There are two types of privilege: legal advice privilege and litigation privilege:

- legal advice privilege protects communications or other documents, made or provided confidentially, between a client and his or her lawyer for the dominant purpose of giving or receiving legal advice.
- litigation privilege protects communications or other documents, made or provided confidentially, between a client and a lawyer, or either of them and a third party, the dominant purpose of which is for use in litigation, either for the purpose of giving or receiving advice in relation to it, or for obtaining evidence to be used in it. For litigation privilege, litigation must be in reasonable contemplation. In an internal investigation, it will often be difficult to argue that litigation is already in reasonable contemplation, and even then it will be difficult to show the internal investigation is for the dominant purpose of the litigation as opposed to, for example, complying with regulatory obligations - but this will depend on the circumstances.

The concept of legal professional privilege is recognised through the broadly analogous provisions of section 413 FSMA, which deems certain communications to be "protected" from the any disclosure to the PRA or FCA. In considering the scope of privilege s413 should always be consulted in addition to common law case law, particularly as that case law continues to evolve and could potentially depart from the specific provisions of s413.

A separate chapter deals with the details regarding the current law and that is not repeated here.

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Status of documents produced for an internal investigation

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Even where privilege may be legitimately claimed in respect of an internal investigation report, it may not extend to ancillary documentation, such as transcripts of interviews with witnesses, or the minutes of the meeting at which the report was discussed, unless the communications are within the client team or litigation privilege can be claimed. Where external lawyers are tasked to conduct an internal investigation, the report they produce will generally attract legal professional privilege. If, however, the internal investigation is intended to deflect the regulator from carrying out its own investigation, the firm may choose to waive the right to claim privilege on a limited basis, or to provide the regulator with a summary report which it is comfortable not claiming privilege over (at least in the first instance). This will depend on the circumstances, the findings and the risk of collateral use by third parties such as potential future litigants.

Firms should seek professional advice on the question of whether a report issued by an in-house legal department attracts privilege in all the circumstances.

In any event, where a firm claims privilege over certain documents, it is important that those documents are separated from non-privileged material, labelled clearly (so that they can be easily identified and extracted in any future disclosure process) and that staff are clear about what to do in the event that a regulator challenges them. Some firms have established processes for dealing with circumstances where regulators and others challenge claims of privilege. These include sealing the documents and delivering them to a third party until the issue can be resolved. This process can be particularly useful in the event of a "dawn raid" or even in the context of regulatory supervision visits.

Compliance Tip:

In the context of claiming privilege, a firm must give serious consideration to who should handle the internal investigation and report to the board. A report written by an in-house lawyer may be legally privileged, whereas a report written by a member of the compliance department or an external party that is not a law firm will not be. Communications should be routed through in-house, or external, counsel and marked "do not forward" to reduce the risk of privilege being lost by transmission of the communication beyond those treated as part of the "client team". Set out below is a checklist of some other key points to consider in increasing the likelihood communications benefit from the doctrine of legal privilege:

- An in-house lawyer must be acting in a legal capacity, not a business advisory capacity, in order to claim privilege for any advice given.
- If engaging external advisers to investigate a matter, it should be noted that accountants or compliance consultants would not be able to benefit from legal professional privilege. However, where such parties are instructed by lawyers for the dominant purpose of litigation which is in contemplation (i.e. where litigation privilege applies), privilege may be extended.
- Consideration should be given as to which specified individuals are to be deemed part of "the client team" for legal advice privilege. Only these people should communicate with the external lawyers and receive privileged communications.
- The creation and distribution of "raw material" for the investigation should be strictly controlled.
- Privileged communications should be circulated on a limited basis, unamended and unaltered, and should not be distributed unnecessarily to a wider audience. Consider using "limited waiver of privilege" language for the purpose of transmission outside the "client group".
- Individuals should avoid the creation of further copies of potentially relevant documentation and avoid making manuscript notes on any potentially relevant documents/copy documents.
- Individuals should also avoid rearranging or editing relevant files and approaching third parties for documents or copy documents.
- Where a firm is voluntarily disclosing privileged material it should be careful to ensure that no other parties have a right to claim joint privilege over that material.

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