

A&O SHEARMAN

UK FCA's PEP talk: clarifying expectations on the treatment of politically exposed persons

24 July 2024

Concerns have been raised in parliament that banks have not been treating politically exposed persons (PEPs) and their families fairly. A recent FCA review found this was generally not the case but has identified a number of steps firms should take to improve transparency and consistency of customer treatment and to ensure customers receive good outcomes.

What are PEPs?

The UK is one of more than 200 countries and jurisdictions committed to international standards that require additional financial checks on individuals who hold significant public functions. The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the **MLR**) defines PEPs as “*an individual who is entrusted with a prominent public function other than as a middle-ranking or more junior official.*”

The reason for conducting additional checks on PEPs, and those connected to them, is that these individuals may be at risk of being targeted for bribery and corruption.

The FCA has published [guidance](#) on the treatment of PEPs for these purposes, which makes clear (amongst other things) that firms should adopt a proportionate and risk-based approach to the application of the MLRs. Further, the FCA expects firms to use information that is reasonably available to them to help identify PEPs. For example: public domain information, public registers such as Companies House, and commercial databases.

De-banking and unfair treatment

Over the last couple of years parliamentarians have periodically expressed concern that UK banks, and other UK regulated financial services firms, appear to be adopting an excessive risk-aversion to dealing with PEPs. Parliament asked the FCA to conduct a review into a selection of firms to: (i) assess the extent to which firms are adhering to the existing guidance on dealing with PEPs; and (ii) evaluate the adequacy of the existing FCA guidance in ensuring a balanced and fair approach to the treatment of PEPs.

The FCA's review was due to be published at the end of June 2024, however, following the dissolution of Parliament and subsequent general election, the [FCA published its findings and further guidance](#) on 18 July 2024. This new guidance aims to clarify the expectations and responsibilities of financial institutions in relation to PEPs.

Expectations

Under current UK legislation, firms are required to conduct additional due diligence on PEPs to comply with the standards set by the International Financial Action Task Force and the MLR. The scope of the anti-money laundering requirements extends beyond the PEPs themselves to include their family members and close associates, collectively referred to as Relatives and Close Associates or “RCAs”.

These controls must be balanced with the need for good customer treatment, starting at account opening and continuing throughout the customer relationship.

In 2017 the FCA issued clarificatory [guidance](#) stating that PEPs domiciled in the UK, along with their RCAs, could be regarded as posing a lower risk of money laundering, unless other high risk indicators were also present.

Results of the FCA review

The FCA’s recent review revealed that the majority of firms have established systems and controls that align with UK legal and regulatory standards and FCA guidance, and that firms do not appear to be subjecting PEPs to excessive or disproportionate checks.

All firms reviewed understood that being a UK PEP or RCA would not, in itself, be a reason to deny services. The review did identify instances where services were had been denied or accounts closed because the firm had identified financial crime concerns that went beyond an individual having been identified as a PEP.

Five points to review and improve

Despite these positive findings, the FCA identified areas where all firms could make improvements to their systems and controls.

- 1. Ensure the definition of a PEP used by the firm is clear and consistent with the 2017 guidance.** The FCA identified that a significant proportion of firms had adopted broader definitions of PEPs and RCAs than that set out in the MLR. Firms should ensure that the definitions used for PEPs and RCAs is aligned with the minimum requirements imposed by law. Having a definition that is broader in scope increases the risk of practices developing where services are unfairly denied to certain groups of customers and prospective customers.
- 2. Conduct ongoing monitoring and status updates.** Firms should regularly reassess the status of individuals designated as PEPs or RCAs, particularly after they exit public office, to ensure that the PEP classification remains appropriate. Where it is no longer appropriate to classify an individual as a PEP or RCA, firms should proactively take the necessary steps to declassify those customers in a timely way.
- 3. Communicate effectively with PEP customers.** Clear, detailed and transparent communication with all customers is essential, particularly those with PEP and RCA status. Customers and prospective customers need to be able to understand why they are being asked to provide or verify information. This is something the FCA will now also be scrutinising through a Consumer Duty lens.

4. **Maintain a risk-based approach.** Firms should effectively consider the actual level of risk posed by individual customers and ensure that information requests are proportionate to those risks. This should be recorded in a well-documented risk assessment methodology that considers all relevant risk factors and individual circumstances. All decisions as to a customer's risk rating should have a clear, documented rationale. Additionally, firms must ensure that they have adopted the changes to Regulation 35 of the MLR, which came into effect on 10 January 2024, which posits that UK PEPs and RCAs generally represent a lower risk than their foreign counterparts, unless other enhanced risk factors are present.
5. **Review and enhance staff training.** The FCA noted deficiencies in staff training across the majority (67%) of firms reviewed. Training programs should incorporate practical scenarios and case studies to better equip staff in handling PEP-related matters. The use of case studies should illustrate both good and poor practice to improve staff proficiency and achieve consistency in customer interactions and treatment.

In response to the FCA's findings, firms are urged to conduct a comprehensive review of their existing policies, procedures and controls. This review should focus on ensuring that risk management practices and the treatment of PEPs and RCAs are in full alignment with the FCA's observations and requirements. Where gaps are identified in their current arrangements, firms should prioritise making necessary improvements and provide more practical staff guidance on the risk-based and proportionate approach to be adopted with regard to PEPs and RCAs.

The FCA noted that some firms continue to operate under global policies and procedures which are not appropriately tailored to reflect UK requirements. The financial crime risks associated with adopting this approach have also been highlighted in a number of recent FCA enforcement notices.

Further consultation

Following its multi-firm review, the FCA has launched a [consultation](#) (GC24/4) on proposed targeted clarifications to its 2017 guidance. The proposed clarifications:

- Reflect the new legal starting point that UK PEPs should be treated as lower risk.
- Make clear that non-executive board members of civil service departments should not be treated as PEPs solely for that reason.
- Give greater flexibility on who can approve or sign off PEP relationships within firms.

The deadline for responses to GC24/4 is 18 October 2024.