



HM Treasury

Financial Services Future Regulatory Framework Review Phase II Consultation

Financial Services Future Regulatory Framework Review Phase II Consultation

Presented to Parliament by the Economic Secretary
to the Treasury by Command of Her Majesty



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Ministerial Foreword

The UK has long been a pioneer in financial services. Financial innovations that were used to fuel economic activity in new ways were instrumental in Britain becoming a great trading nation from the 17th century onwards. Today, the financial services sector remains central to driving economic activity as the UK seeks to build on its global role outside of the EU, a role that will be built on economic vitality, openness and strong trading relationships. From those early days of innovation, the UK financial sector has never ceased to be a world leader. The sector continues to provide essential support to the wider economy, creating jobs, generating tax revenue and driving regional investment and growth. And the sector can help us address some of our biggest public policy challenges. During the Covid-19 pandemic, the sector has been working in partnership with the government to extend credit on an unprecedented scale to businesses across the country, demonstrating the importance of a strong financial services sector in supporting our economy through good times and bad.

Over time, and with the development of the EU's single market, much of our regulatory approach to financial services has been prescribed by EU legislation. Leaving the EU means the UK has the opportunity to take back control of the decisions governing our financial services sector. We can now be guided by what is right for the UK, regulate differently where we need to, and regulate better.

Making the most of this opportunity will be underpinned by this second phase of the Financial Services Future Regulatory Framework (FRF) Review. A review in which we get the opportunity to determine how our financial services rules are made, who is responsible for making them, how stakeholders can have their say and how those making the rules are scrutinised and held accountable.

The proposals put forward in this consultation rightly build on the strengths of the UK's existing regulatory framework and, in particular, the role played by our expert, independent financial services regulators. The approach we propose here is intended to ensure that our regulatory regime has the agility and flexibility needed to respond quickly and effectively to emerging challenges and to help UK firms seize new business opportunities in a rapidly changing global economy.

The proposals set out here will achieve this through a clear cut and coherent allocation of regulatory responsibility. The government and Parliament will set the policy framework for financial services and the strategic direction of financial services policy. Working within this framework, the regulators will design and implement the regulatory requirements that apply to firms, using their expertise and agile rule-making powers to ensure regulation is well-designed and keeps pace with market developments. Enhanced scrutiny and public engagement arrangements will help ensure that the regulators are accountable for their actions and stakeholders are fully engaged in the policy-making process.

I want to take this opportunity to reiterate that the UK remains committed to the highest standards of regulation. Robust regulatory standards are important, not just to ensure a stable and fair financial system here at home, but to ensure that the UK meets its global responsibilities. The importance of the UK as a financial centre, and the role it plays in the global financial system, mean that the success or failure of our regulatory approach can have important consequences far beyond our shores. As the UK seeks to build a global role outside of the EU, it will take its international responsibilities as seriously as ever. The government is also determined to seize opportunities to provide policy leadership in key areas of financial regulation, including on Green Finance and a low carbon future, fintech and payments innovation, financial crime, financial inclusion and the levelling-up agenda.

To help secure economic prosperity at home, and UK policy leadership abroad, we must ensure that we get our framework approach right. I therefore urge Parliamentary colleagues, market participants and other interested stakeholders to engage enthusiastically with the review. This first consultation aims to generate a thorough and wide-ranging debate which will help develop the overall blueprint for our future framework, leading to a full package of proposals for consultation in 2021. As the City Minister responsible for financial services, I have the privilege of overseeing one of the UK's most vibrant, innovative and important business sectors. I look forward to leading the debate on how we develop our overall regulatory approach to ensure the sector continues to thrive well into the future.

A handwritten signature in black ink that reads "John P. Glen" with a stylized flourish underneath.

John Glen MP
Economic Secretary to the Treasury

Executive summary

The Future Regulatory Framework (FRF) Review was established to determine how the overall approach to regulation of financial services needs to adapt to the UK's new position outside the EU and to ensure the regulatory framework is fit for the future. After focusing on the specific issue of coordination between the UK's regulatory authorities in Phase I of the review, the government is now moving to Phase II which will examine the broader regulatory framework for regulation of financial services in the UK.

The government is conducting this phase of the FRF Review in two stages. This first consultation sets out an overall blueprint for financial services regulation, focusing on the split of responsibilities between Parliament, the government and the financial services regulators. In doing so, it highlights the importance of ensuring appropriate and effective arrangements for accountability, scrutiny and public engagement with the policy-making process, particularly in relation to the UK's financial services regulators. The government will carefully consider the responses received and use these to inform a second consultation in 2021, which will set out a final package of proposals and how they will be delivered.

The Financial Services and Markets Act 2000 (FSMA), and the model of regulation introduced by that Act, continue to sit at the centre of the UK's regulatory framework. The government believes that this model, which delegates the setting of regulatory standards to expert, independent regulators that work within an overall policy framework set by government and Parliament, continues to be the most effective way of delivering a stable, fair and prosperous financial services sector. The model maximises the use of expertise in the policy-making process by allowing regulators with day-to-day experience of supervising financial services firms to bring that real-world experience into the design of regulatory standards. It also allows regulators to flex and update those standards efficiently in order to respond quickly to changing market conditions and emerging risks. The FSMA model was readily adapted to address the regulatory failings of the 2007-08 financial crisis and has helped to ensure that the UK remains a global hub for financial services with a world-leading financial sector. The UK's approach to regulation is internationally respected with the UK continuing to be a thought leader in the development of international standards for financial services.

But the UK's membership of the EU has complicated the operation of the FSMA model. The EU approach to regulation of financial services involves detailed regulatory standards being set in legislation applying across Member States in order to facilitate a single market in financial services. Increasing EU competence for financial services regulation has therefore moved the UK's regulatory framework away from the model based on delegation of standard setting to regulators. To a

great extent, the EU approach to regulation is preserved in the 'onshoring' of EU legislation. The vast bulk of EU directly applicable legislation for financial services will now sit on the UK statute book, with amendments made to ensure this legislation works effectively in a UK standalone regime.

There are significant disadvantages to this approach. It means primary responsibility for designing and maintaining regulatory standards is removed from the expertise that is concentrated in UK regulators. And as regulatory standards are set in legislation, it is difficult to flex or update these standards quickly in order to respond to changing conditions. It has led to an unclear allocation of responsibilities across Parliament, HM Treasury and the regulators and resulted in a fragmented rulebook for firms, with regulatory requirements spread across different forms of legislation as well as regulator rules. While the onshored regime for financial services will provide a smooth transition to the UK's new position outside of the EU, minimising disruption for firms and consumers by providing continuity around the regulatory requirements themselves, this structure is not intended to provide the long-term approach for regulation of financial services in the UK.

The government sees the UK's departure from the EU as an important opportunity to review our framework arrangements and ensure that we have an overall approach to regulation of financial services which is right for the UK. The government believes this would be best achieved by building on the strengths of the FSMA model as it was originally intended to operate, making important adaptations that will facilitate appropriate policy input by government and Parliament.

This consultation will therefore propose a blueprint for the future regulatory framework which builds on the strengths of the FSMA model. This blueprint, which is referred to in this consultation as the post-EU framework proposal, has the following key features:

- A clear allocation of responsibilities between Parliament, HM Treasury and the financial services regulators.
- Government and Parliament will be responsible for setting the policy framework for financial services regulation. This will include new policy framework legislation for specific areas of regulated activity which will give the government and Parliament the opportunity to set out the key public policy issues that must be considered when designing and implementing regulatory standards.
- The Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) will be responsible for designing and implementing the regulatory standards that apply to financial services firms and markets using their existing rule-making powers in FSMA. This approach will maximise the use of expertise in the design of regulatory standards and ensure those standards can be flexed and efficiently updated to address changing conditions and emerging risks. As much as possible, this should result in one coherent source of regulatory requirements for firms – the regulators' rulebooks. This will involve the transfer of regulatory requirements in onshored legislation to the regulators. It will also offer an opportunity to review and rationalise some areas of non-EU derived financial services legislation.

- The PRA and FCA will be subject to enhanced transparency requirements obliging them to explain how they have had regard to the public policy issues set out by Parliament in activity-specific policy framework legislation. This will provide Parliament with a clearer basis on which to scrutinise the work of the regulators and will support effective engagement with regulator proposals by firms and members of the public.
- The cooperation and coordination arrangements that exist between HM Treasury and the financial services regulators will include more systematic consultation between these institutions at an early stage in the policy-making process. In particular, this will allow Treasury Ministers, who have overall responsibility for financial services policy in the UK, to consider regulator rule proposals and feed in views to the regulators' policy development process before proposals are finalised for consultation.

The government recognises that this will involve delegating a very substantial level of policy responsibility to the UK financial services regulators. While consulting on the post-EU regulatory framework proposal, it is therefore right to review the framework arrangements for accountability, scrutiny and public engagement in the policy-making process, particularly in relation to the regulators. Chapter 3 of this consultation explains the existing arrangements for accountability, scrutiny and public engagement and identifies areas where these arrangements might be adapted. Parliament will also wish to consider how its scrutiny of financial services regulation may need to adapt, particularly in relation to the financial services regulators.

This consultation proposes an overall approach to the regulation of financial services, built on the existing FSMA model, which the government believes should form the foundation of the future regulatory framework. But it does not, at this stage, present a full package of proposals. This first consultation is intended to generate a thorough and wide-ranging debate in Parliament and among stakeholders that will have an interest in the UK's regulatory approach, including the financial services industry and consumer groups. That debate, and responses made to this consultation, will be used to develop a final package of proposals that will be presented in the second consultation during 2021.

The government would like to thank in advance all those who respond to this first consultation.

Chapter 1

Background and context

1.1 The Future Regulatory Framework (FRF) Review was announced at Mansion House on 20 June 2019 by the then Chancellor of the Exchequer, with the purpose of ensuring that the UK's financial services regulatory framework is fit for the future. The regulatory framework sets the overall approach to regulation of financial services and establishes the institutional architecture needed to operationalise the regulatory regime. While there is no exact definition of what constitutes the regulatory framework, a broad view would include:

- the principles and processes for developing and implementing financial services policy in the UK, including who specifies and defines the activities which are regulated, who sets the standards for regulated activities, and the consequences for failing to adhere to regulatory requirements;
- the institutions that are responsible for developing policy, designing and implementing requirements, and supervising compliance with those requirements;
- the arrangements by which the policy and regulatory institutions are accountable for their work.

1.2 Phase I of the review examined coordination between the UK authorities that have responsibility for regulation of and policy for the financial services sector. The government published its response on 11 March, announcing that it and the financial services regulators were creating the Financial Services Regulatory Initiatives Grid and Financial Services Regulatory Initiatives Forum, to help regulators, firms and consumer stakeholders plan ahead and improve co-ordination and transparency across the regulatory landscape for financial services. The Regulatory Initiatives Forum has now published two iterations of the Regulatory Initiatives Grid, intended to help stakeholders understand how the regulatory pipeline has changed to take into account the impact of the Covid-19 pandemic.

1.3 The government also stated in its response to Phase I that there are a broader set of issues concerning the regulatory framework that need to be addressed. Operation of the UK framework has evolved to accommodate the UK's membership of the EU. Withdrawal from the EU means that aspects of that framework will no longer be optimal and we will need to decide how important policy and regulatory functions carried out at the EU level will be exercised in a standalone UK regime. Leaving the EU means the UK is taking back control of the rules governing our world-leading financial services sector, so it is also an opportunity to adapt our regulatory approach to meet the specific needs of the UK. This second phase of the review will examine how we should adapt our approach to

regulation outside of the EU so that we build on the strengths of existing UK framework arrangements to meet the challenges of the future.

1.4 The UK has always championed, and remains committed to, the highest standards of financial regulation, and this will continue to guide our approach. The government's objectives for Phase II of the review are to ensure our framework:

- Has a clear and coherent division of responsibilities between Parliament, government and the operationally independent financial services regulators;
- Provides for appropriate policy input by democratic institutions;
- Facilitates effective accountability and scrutiny of HM Treasury and the regulators;
- Allows regulation to be agile and responsive to changing conditions, new business opportunities and emerging risks;
- Is coherent and user-friendly for those subject to or affected by financial services regulation;
- Promotes international confidence in the UK regulatory approach; and
- Facilitates effective stakeholder engagement in the policy-making process.

1.5 Whilst this is the first time the government has formally consulted on the overall regulatory framework approach as part of this review, a debate among interested stakeholders is already underway and the Treasury has been proactively engaging with them to understand their views. For example:

- the former House of Lords EU Financial Affairs sub-Committee has launched an Inquiry into financial services after Brexit, which has been examining a variety of issues, including accountability and scrutiny of regulatory authorities under the regulatory framework;
- industry stakeholders (including the International Regulatory Strategy Group (IRSG)) have published papers setting out potential models for the future framework;
- Andrew Bailey, when Chief Executive of the FCA, gave a speech on the future of conduct regulation, including how the regulator views regulating in the public interest in light of its objectives;
- Sam Woods, the Bank of England Deputy Governor for Prudential Regulation, outlined an approach based on the delegation of detailed rule-making powers to the regulators.

Related government action

1.6 The future success of the UK financial services sector will require a world-class regulatory model and an open business environment which continues to attract firms from around the world to conduct a wide range of financial services activity through the UK's well-regulated and highly liquid markets. The government

will be looking to enhance and exploit the existing strengths of the UK regulatory approach and will use all available regulatory tools and mechanisms to deliver on its objectives. The government will continue to drive forward its policy agenda for financial services in a number of specific areas:

- **Innovation:** the UK has pursued a policy approach to foster innovation. This includes a regulatory environment for Fintech which is now internationally regarded as a blueprint for best practice and which has helped the UK Fintech sector become a world-leader. The government will continue to develop new policies to facilitate innovation that serves the users of financial services, including through the Payments Landscape Review, the two consultations relating to the regulation of cryptoassets and stablecoins, and the Access to Cash Review.
- **Stability:** The government will continue to safeguard the UK's financial stability. This includes ensuring prudential standards are updated in line with the international Basel III standards, and conducting a review of certain features of Solvency II to ensure that it is properly tailored to take account of the structural features of the UK insurance sector.
- **Market integrity & consumer protection:** The government is determined to build on existing protections for consumers, and is introducing legislation in the Financial Services Bill to improve the functioning of the Packaged Retail and Insurance-based Investment Products (PRIIPs) regime in the UK and address potential risks of consumer harm. The Bill will also make improvements to the Market Abuse regime. In addition, the government is consulting on a regulatory gateway for authorised firms approving the financial promotions of unauthorised firms.
- **Sound capital markets:** The government remains committed to open and efficient markets and to attracting liquidity into the UK. The government will look to enhance the regulatory approach so that it is clearer, more effective, and more proportionate, whilst maintaining high regulatory standards.
- **Openness:** The UK is retaking full control over its legal and regulatory regime at the end of the Transition Period. We will deploy our regulatory tools to develop closer and more formalised relationships with partner jurisdictions, and seize new opportunities to enhance our openness to global markets. The government plans to maximise the transparency, agility and expertise of our regulatory model and champion our strengths as a safe, open, and global financial centre.

The purpose of the consultation

1.7 This consultation seeks views on proposals and options for adapting the financial services regulatory framework following the UK's departure from the EU. Central to the government's proposed approach is an adaptation of the regulatory model introduced by the Financial Services and Markets Act 2000, which is set out in Chapter 2, along with a discussion in Chapter 3 of accountability, scrutiny and

public engagement arrangements. The proposed approach has the following main features:

- Our expert, operationally independent regulators will be responsible for setting direct regulatory requirements on financial services firms and markets, with Parliament and government responsible for setting the policy framework, through legislation, within which the regulators must operate.
- Accountability and scrutiny arrangements, particularly in relation to the financial services regulators, will need to be reviewed and, where appropriate, enhanced to reflect their expanded responsibilities.
- The consultation will also seek views on how to enhance broader stakeholder and public engagement with the policy making process of financial services, particularly in relation to the financial services regulators.

Chapter 2

The post-EU regulatory framework proposal

2.1 As explained in the previous chapter, the Future Regulatory Framework (FRF) Review was established to determine how the financial services regulatory framework needs to adapt to the UK's new position outside of the EU, and to ensure the framework is fit for the future. The government's view is that the existing framework has significant strengths and it has served the UK well for many years. As such, the government aims to build on those strengths rather than designing a new framework approach from scratch.

2.2 In particular, the government views the Financial Services and Markets Act 2000 (FSMA) architecture, as adapted to address the regulatory failures of the 2007-08 financial crisis, as continuing to be appropriate. This includes the existing regulatory institutions, their overall areas of responsibility and their powers for making rules, supervising firms and enforcing regulatory requirements. And as set out when establishing the FRF Review, the government is of the view that expert, independent regulators should continue to be a central part of the UK's approach to financial services regulation.

2.3 This consultation document therefore focuses on how the FSMA model of regulation can be built on to provide a regulatory framework that makes the most of opportunities provided by the UK's withdrawal from the EU and which will underpin a stable, innovative and internationally competitive UK financial services sector far into the future. This chapter explains the government's proposed blueprint for adapting the FSMA model and how the proposed approach will meet the objectives for the FRF Review as set out in the previous chapter.

The FSMA model

2.4 At the centre of the UK's regulatory framework is the Financial Services and Markets Act 2000 (FSMA). Before FSMA, financial regulation was based on a patchwork of statutes, voluntary codes and regulatory bodies, many of which were industry self-regulation bodies responsible for policing industry standards. The Financial Services Act 1986 (the 1986 Act) started a process to rationalise financial services regulation and move more of the regulatory regime on to a statutory footing. The 1986 Act introduced the first financial services regulator established by statute: the Securities and Investments Board. FSMA extended this process of rationalisation significantly, replacing a number of enactments with one central piece of framework legislation and establishing one statutory regulator with broad

responsibility for financial services regulation and supervision delegated directly from Parliament.

2.5 FSMA was based on an overall model for financial services regulation with the following key features:

- Parliament, through primary legislation, sets the overall approach and institutional architecture for financial services regulation, including the regulators' objectives;
- Parliament establishes the parameters within which HM Treasury sets the 'regulatory perimeter' through secondary legislation, specifying which financial activities should be regulated and the circumstances in which regulation should apply;
- An expert, operationally independent regulator – the Financial Services Authority (FSA) (superseded in 2013 by the Financial Conduct Authority and Prudential Regulation Authority) – with statutory responsibility for setting the detailed requirements that apply to regulated firms and markets. The FSA was also responsible for enforcing requirements applied to firms operating within the perimeter and for taking action against regulatory breaches. Operational independence was underpinned by enabling the FSA to fund itself through a levy on regulated firms; and
- The FSA was tasked with meeting statutory objectives, with requirements set in legislation to ensure appropriate accountability to Parliament, HM Treasury, regulated firms and the general public.

Adaptation of the FSMA model and the broader framework following the financial crisis

2.6 The financial crisis of 2007-08 revealed serious flaws in the UK's system of regulation, particularly in the allocation and co-ordination of responsibilities across the 'tripartite' institutions – HM Treasury, the Bank of England and the FSA. The Bank had inadequate tools to meet its financial stability objective; the FSA's responsibilities were too broad to allow for sufficient focus on the stability of firms; and no part of the framework had responsibility for monitoring the crucial link between the stability of individual firms and the stability of the financial system as a whole.

2.7 The post-crisis framework reforms were therefore focused primarily on institutional design and allocation of responsibilities, with the FSA abolished and replaced with the following institutional arrangements:

- the Financial Policy Committee (FPC) was established within the Bank of England to take on responsibility for the stability of the financial system as a whole, or 'macroprudential' regulation (see below for an explanation of the UK's macroprudential framework);
- the Prudential Regulation Authority (PRA)¹ was established as the prudential regulator of firms which manage significant balance sheet risk as

¹ The PRA was established as a subsidiary of the Bank of England but was 'desubsidiarised' in 2016.

a core part of their business – primarily banks, insurers and the larger, more complex investment firms. The PRA sets regulatory requirements through broad rule-making powers conferred by FSMA (“PRA rules”);

- the Financial Conduct Authority (FCA) was created to focus on conduct of business regulation, with a mandate to promote the right outcomes for consumers and market participants, including through the promotion of competition. It is also responsible for the prudential regulation of firms not within the remit of the PRA. The FCA sets regulatory requirements through broad rule-making powers conferred by FSMA (“FCA rules”);
- In 2013, the Payment Systems Regulator (PSR) was established as the economic regulator of the payment systems industry in the UK; and

FSMA was amended to provide more effective mechanisms for coordination across HM Treasury and the financial regulators.

The continued importance of expert, independent regulators

2.8 As set out above, the delegation of regulatory responsibility to dedicated financial services regulators which operate independently from government has been a core feature of the UK’s regulatory approach for many years. This approach, which is central to the FSMA model, has served the UK well and the government’s view is that it remains the best way of delivering a well-designed, efficiently implemented and effectively supervised regulatory regime. The delegation of responsibility to expert, independent regulators has been adopted by many countries and is supported by the academic literature on financial services regulation, as well as being consistent with the policy approach advocated by the IMF.²

2.9 Dedicated regulators can build up a concentration of policy and technical expertise in financial services regulation that could be more challenging to foster within a government department with its broader range of responsibilities. It is appropriate and accepted practice for quasi-judicial functions like the supervision and enforcement of financial regulation to be exercised independently of government departments and this approach is widely followed in the UK and other jurisdictions. When combined with the valuable experience that comes from the supervision of financial services firms and markets, policy-making and the design of regulatory standards can be informed by the ‘real-world’ conditions and developments closely observed by supervisors. As observed by IMF studies, when regulators make these judgements independently from government, they are likely to deliver more predictable and stable regulatory approaches over time. IMF studies have also found that the response to financial crises has been less effective in countries without independent regulators.³

² Quintyn, M. & Taylor, M.W. 2002. Regulatory and Supervisory Independence and Financial Stability. International Monetary Fund (IMF) Working Paper WP/02/46.

³ Quintyn, M. & Taylor, M.W. 2004. “Should Financial Regulators Be Independent?” International Monetary Fund (IMF) Economic Issues No. 32. This paper cites empirical evidence to demonstrate the effectiveness of regulators independent from political influence, asserting that in every major financial crisis of the decade up to 2004, political interference made both the quality of regulation worse and hindered regulators in their interventions to deal with failing financial institutions.

The UK's macroprudential framework

2.10 As explained in paragraph 2.7 above, an important development in the UK's regulatory approach was introduced by the Financial Services Act 2012. This involved giving the Bank of England responsibility for macroprudential oversight of the UK financial system as a whole, by establishing a new Financial Policy Committee (FPC) within the Bank. The FPC is the UK's macroprudential authority, and is responsible for identifying, monitoring, and taking action to remove or reduce systemic risks with a view to protecting and enhancing the resilience of the UK financial system. In addition to the FPC's statutory primary objective for financial stability, the FPC also has a secondary objective (subject to the primary objective) to support the economic policy of the government.

2.11 The FPC achieves its objectives via its powers of recommendation and direction, as well as its communications. The FPC has a broad power to make non-binding recommendations to anyone regarding macroprudential issues, powers to make recommendations to HM Treasury (for example on the regulatory perimeter or powers of direction made available to the FPC), and powers to make recommendations to the PRA and FCA on a 'comply or explain' basis. The FPC also has the power to direct the PRA and/or the FCA to implement certain macroprudential measures.

2.12 The government's view is that this approach remains appropriate and the government does not propose to alter the macroprudential elements of the UK's regulatory framework.

Operation of the FSMA model within the EU

2.13 The FSMA model was intended to provide a clear-cut division of responsibilities: Parliament sets the legislative framework; HM Treasury, with Parliament's approval, specifies which activities should be regulated; and responsibility for setting regulatory requirements sits with the regulators.

2.14 But this clear split of responsibilities has not always been the case in practice. The expansion of EU competence for financial services regulation has significantly affected the operation of the FSMA model. The development of a single market in financial services, as well as interventions to address regulatory failures of the financial crisis, have resulted in EU legislation covering many key areas of regulation. This includes the prudential regulation of banking, insurance and investment firms as well as wide-ranging regulation covering financial markets activity and infrastructure.

2.15 EU legislation is proposed by the European Commission and negotiated with Member State governments and the European Parliament. HM Treasury, which has led the UK negotiating effort on EU financial services legislation, has therefore taken on responsibility for key areas of regulatory policy. While the UK regulators have worked closely with HM Treasury in influencing the development of EU legislation, HM Treasury has been responsible for negotiating areas of detailed regulatory requirements that would usually have sat with UK regulators under the FSMA model. EU legislation, which increasingly tends to set very prescriptive requirements

on firms in order to underpin the operation of the single market, has constrained the regulators' policy and rule-making discretion. In many areas, UK regulators have been left with little flexibility on how to implement EU standards, even if they are not the right fit for UK firms.

2.16 In areas of financial services regulation not covered by EU legislation, regulators have usually had more policy discretion as originally intended by the FSMA model. But there have been exceptions to this. Domestic regulation to ring-fence banks is an example of setting requirements on firms through the use of more detailed legislation, in this instance constraining the PRA somewhat in designing and calibrating the requirements.

The position now that the UK has left the EU – the 'onshored' regime

2.17 As EU legislation has become a very significant component of UK financial services regulation, the government needed to ensure that there would be no gaps in the UK's regulatory regime following EU withdrawal, and that regulation would continue to operate effectively. The European Union (Withdrawal) Act 2018 saves all EU-derived domestic legislation (for example, legislation implementing EU Directives) and transfers directly applicable EU law (for example, Regulations) onto the UK statute book.

2.18 HM Treasury, supported by the regulators, has been undertaking an unprecedented programme of legislation to ensure the body of retained EU law will operate effectively and will smooth the transition to a UK standalone regime which will take effect from 1 January 2021. This process is often referred to as 'onshoring'. As a result of the European Union (Withdrawal) Act 2018 and this subsequent legislative programme, the bulk of EU financial services legislation will form part of UK law and will continue to apply in the UK after exit, with necessary changes to make sure that it operates effectively. This approach was adopted so that Parliament would play a full role in approving changes needed to ensure onshored legislation works as intended after the transition period ends. It was also designed to ensure that Parliament would take any future decisions on what should happen to the body of onshored legislation as the UK adapts its regulatory approach.

2.19 While the onshoring approach is right for the immediate period after EU exit, it was not designed to provide the optimal, long-term approach for UK regulation of financial services. In fact, there would be significant disadvantages to retaining the onshored regime over the long term:

- **Inflexibility** – The technical detail of financial services regulation needs to flex in response to changing market conditions and new regulatory challenges so that the regulatory regime continues to operate effectively. Having regulatory requirements in legislation can make it difficult to flex requirements and is not conducive to a dynamic and efficient regime. It also means that the responsibility for maintaining regulatory requirements is located in a government department which does not carry out the supervision of firms and markets. The exercise of supervision is the most effective and efficient means of detecting emerging issues and risks that the regulatory regime may need to respond to. Combining responsibility for

the maintenance of regulatory requirements with the supervisory function in the regulators is the most flexible and efficient way of ensuring the regulatory regime can respond to changing conditions.

- **Regulatory requirements maintained separately from the expertise gained through the supervision of firms** – Giving HM Treasury responsibility for the maintenance of a large body of detailed and technical regulation would make it more difficult for the regulatory regime to benefit directly from the resource and expertise that dedicated financial services regulators have. In particular, it would mean that the maintenance of regulatory requirements would be less directly informed by the detailed understanding of financial services activity and business practices that the regulators gain from their day-to-day supervision of regulated firms and markets. As explained above, it is the day-to-day supervisory function which can quickly detect emerging issues and risks that the regulatory regime may need to respond to.
- **Disproportionate demands on Parliamentary time** – Parliament has to consider legislation across the full range of central government responsibilities and use of Parliamentary time must be carefully managed. Ongoing maintenance of detailed financial services regulatory requirements would demand considerable Parliamentary time and it must be questioned whether this would represent good use of Parliamentary attention and resource.
- **A fragmented rulebook** – In the onshored regime, regulatory requirements will continue to be spread across a range of sources, a patchwork of domestic and retained EU legislation, regulator rules made under FMSA and onshored EU technical standards. This fragmented rulebook is challenging for firms and consumers to navigate and is difficult to maintain efficiently. The links and interaction between regulator rules and statute are complex and could quickly become outdated.

2.20 The government's proposed blueprint for the Future Regulatory Framework involves adapting the FSMA model to address the challenges of managing the onshored regime and to create a more coherent and democratically accountable framework for the development and application of future UK financial services regulation.

2.21 The key policy challenge in adapting the FSMA model is how to make the most of independent regulator expertise and flexibility in setting regulatory standards, while at the same time ensuring regulators take full account of broader public policy issues and priorities when designing those standards. Under the approach proposed by this consultation, which envisages a high level of policy responsibility for UK regulators, making sure that the regulators effectively internalise the full range of relevant public policy issues will be essential. If the framework does not provide for this, the regulators' policy-making process risks leading to poor outcomes and could lack credibility and legitimacy. The framework must provide a coherent and effective way for government and Parliament to set out what those broader public policy issues and priorities are. And it must ensure the regulators are open and transparent in explaining how the full range of relevant policy issues have been considered, including where policy trade-offs need to be made. While the current FSMA model has many strengths, the means for government and Parliament to set the key policy issues relevant to specific areas of

regulation and for regulators to take them into consideration, is under-developed and incoherent. The post-EU framework approach set out in this consultation aims to address this central challenge for the future framework.

2.22 This consultation focuses on adapting the FSMA model as it applies to the responsibilities and the operations of the PRA and FCA. As the review progresses, we will need to consider whether, and to what extent, the proposed approach should be extended to other areas of financial services regulation.

The post-EU regulatory framework proposal

2.23 The government thinks that the FSMA model continues to make sense for the UK and will provide a tried and tested foundation for adapting the UK's regulatory approach outside of the EU. Building on the strengths of existing arrangements will provide for a smooth transition to the UK's post-EU regulatory approach and will minimise disruption for affected firms, consumers and other interested stakeholders. The government proposes a blueprint approach which would adapt existing arrangements under FSMA in three key ways.

I: The framework should provide for a clear division of responsibilities as originally envisaged by the FSMA model.

2.24 That division of responsibilities should provide for government and Parliament to set the regulatory framework through legislation, while the financial regulators should, in most instances, be responsible for setting the requirements that apply to financial services firms and markets.

2.25 This would mean that the vast bulk of retained EU provisions would be transferred to regulator rulebooks. The default approach would be for any retained EU law provision that is in scope of the regulators' FSMA rule-making powers to be taken off the statute book to become the responsibility of the appropriate regulator. FSMA already confers broad rule-making powers on the PRA and FCA and therefore no significant reform of regulator powers should be needed for this transfer of responsibility.

2.26 Nonetheless, some elements of legislation would not be appropriate to become the responsibility of regulators and would need to remain on the statute book. This would include the scope of regulated activities where the important question of whether an activity should be subject to regulation is more appropriate for government and Parliament to decide. It would also include provisions that cover the UK's regulatory and trading relationship with other countries, such as equivalence arrangements or mutual recognition agreements. The post-EU framework approach is intended to be flexible and it will be appropriate in some areas of regulation for more detail to be set out in legislation, particularly where there are very important public policy issues involved (such as the UK's regulatory relationship with other countries or where regulation has implications for public funds).

II: FSMA should include policy framework legislation for key areas of regulated activity.

2.27 A gap in the original FSMA model is that, while it set high-level general objectives and principles, it did not provide for government and Parliament to set the policy approach for specific areas of financial services regulation. The government is therefore of the view that new policy framework legislation covering key areas of regulation should be included as part of the adapted regime. This will allow for more strategic policy input by the UK's democratic institutions.

2.28 For example, the proposed approach would involve government and Parliament setting out in legislation the overall purpose and regulatory approach needed for the prudential regulation of insurance business. The legislation would include an explanation of specific policy priorities relevant to insurance prudential regulation, set out in regulatory principles, that the regulator should take into consideration when developing policy and designing regulatory requirements for that particular activity. The approach would need to work for specific markets where participants may be carrying out a range of different activities. For example, in wholesale capital markets different types of participant, often acting in different capacities, may be subject to the same overall set of regulatory requirements.

2.29 In contrast to EU legislation, this activity-specific policy framework legislation would be high-level, focusing on the overall purpose, approach and key policy considerations relevant to each particular regulatory regime. It would not set the requirements that would apply to regulated firms, which would be the responsibility of the relevant regulator(s). In applying this approach to onshored legislation, there would be the opportunity to consider how areas of activity and specific regulatory regimes should be defined. The approach would not need to follow the existing EU legislative file structure and, working with the regulators and industry stakeholders, HM Treasury will explore whether moving away from the EU legislative structure makes more sense in the UK context.

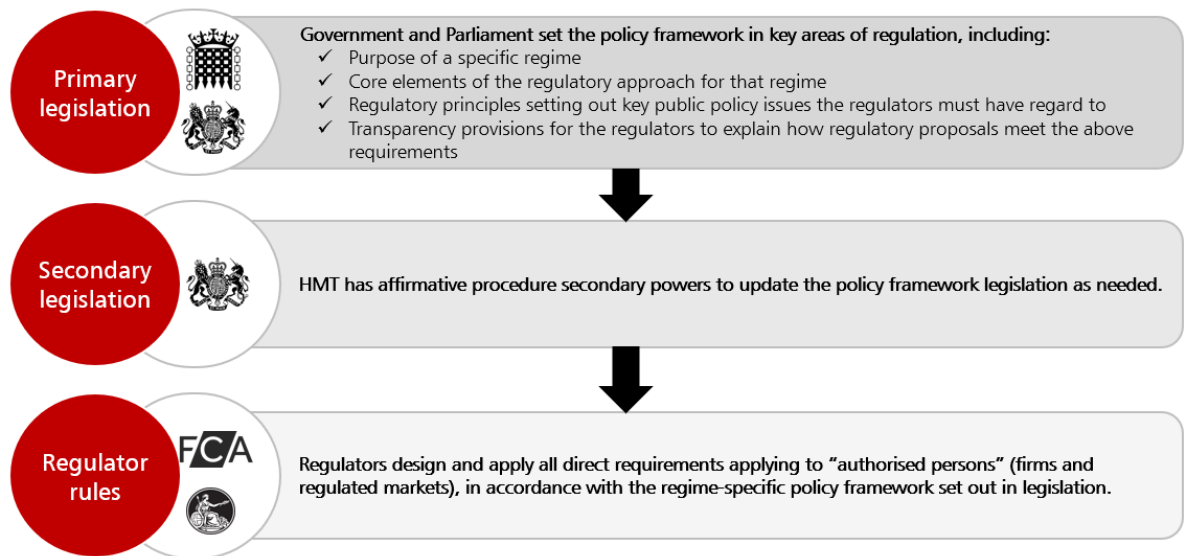
2.30 Such legislation should be designed to set the long-term policy framework for key areas of regulation and should be relatively stable over time. Nevertheless, it should be possible to adapt this legislation to take account of emerging regulatory challenges. As is already provided for in relation to key aspects of the existing FSMA framework which may need updating from time to time, the government envisages the ability to update aspects of activity-specific policy framework legislation, such as the regulatory principles, using the affirmative secondary legislation procedure.

III: Existing FSMA transparency requirements should be updated to reflect new activity-specific policy framework legislation.

2.31 FSMA already sets transparency requirements for the regulators to explain and consult on their policy and rule proposals. These requirements would need to be updated to facilitate transparency around how the regulators meet the obligations set out in new policy framework legislation. Currently the regulators are required to explain how proposals will meet their overarching statutory objectives and how they have had regard to the general FSMA regulatory principles. In addition, we propose that the regulators are required to explain how their proposals

meet the statutory purpose set for a particular regulatory regime and have taken into consideration the activity-specific regulatory principles.

Diagram: the proposed allocation of regulatory responsibilities



Illustrating the post-EU framework approach

2.32 An important theme for this consultation is how policy framework legislation, specific to key areas of regulated activity, should be constructed in order for government and Parliament to give the regulators effective strategic policy steers for each key area of regulation, whilst leaving policy discretion with the regulators on how regulatory requirements should be designed to meet those policy steers.

2.33 The government envisages a legislative approach which will cover five key elements: an obligation for the regulator to maintain a specific regulatory regime; the purpose of the regime; the scope of the regime; any core elements to the regulatory approach that government and Parliament wish to set for the regime; and regulatory principles highlighting specific policy considerations to which the regulators must have regard. How these elements might be set in legislation is illustrated below using a regime for the prudential regulation of insurance business as an example. The example below is to illustrate how the post-EU framework legislative approach might work, but is not at this stage intended to propose the direction of policy for the prudential regulation of insurers. Readers should be aware that the government, working with the PRA, is separately reviewing the prudential rules for insurance business covered by the onshored Solvency II regime.

2.34 **Obligation on the regulator.** This would oblige the PRA to maintain the specified regime. In the exercise of its powers to make regulatory rules under FSMA and in discharging its other general functions, the PRA would be obliged to maintain a regime for the prudential regulation of insurance undertakings, reinsurance undertakings (including groups and third country branches) and the transfer of insurance and reinsurance risk using alternative risk transfer methods.

2.35 Purpose of the regime. Legislation here would be used to set out the overall purpose of the regulatory regime, consistent with the overarching statutory objectives set for the relevant regulator. So for example, under the prudential regime for insurers, the PRA might be required to exercise its general functions in order to:

- a) promote the safety and soundness of PRA regulated insurance undertakings, reinsurance undertakings and insurance special purpose vehicles;
- b) contribute to the securing of an appropriate degree of protection for those who are, or may become, insurance or reinsurance policyholders;
- c) avoid adverse effects that the carrying on of insurance activities may have on the stability of the UK financial system; and
- d) subject to the purposes set out in a) to c) above, facilitate effective competition in the markets for insurance services so that the sector can supply a diverse and affordable range of insurance products and services for UK individuals and businesses.

2.36 Scope of the regime. Currently, there are two regimes for prudential regulation of insurers: one setting EU derived requirements for firms subject to the Solvency II Directive (for example, firms with an annual income of 5 million euros or more); and one based on domestic requirements for all other firms. Application of the post-EU framework approach might be used to rationalise these arrangements and create one coherent regime for the prudential regulation of insurance business in the UK. Such an approach could cover all PRA regulated insurers, reinsurers and insurance special purpose vehicles and would give effect to the overall policy framework set by government and Parliament, but with discretion left to the PRA on the specific regulatory requirements that would apply to firms, with the PRA able to vary requirements based on the size, nature and complexity of firms.

2.37 Core elements of the regulatory approach. Where appropriate, government and Parliament might set out features of the regulatory approach it judges important in order to achieve the purpose it has set for the regime. So, for the prudential regulation of insurance, this might include directing the PRA, when exercising its general functions, to do the following:

- (a) Require undertakings to maintain financial arrangements, including the resources they hold, that enable those undertakings to withstand financial and economic shocks, with the level of resources set to be proportionate to the nature and scale of the risks that individual undertakings are exposed to. The purpose here would be to promote a stable insurance sector, but not to eliminate all risk-taking or the risk of insurance undertaking failure;
- (b) Ensure that the assessment of an undertaking's assets and liabilities is risk-based, reflecting the actual risks that individual undertakings are exposed, making use of relevant financial market information where possible and prudent;

- (c) Require undertakings to have arrangements in place which ensure that those undertakings understand and can manage the risks they are exposed to; and
- (d) Require undertakings to disclose information necessary for the public to understand the current financial condition of undertakings.

2.38 Activity-specific regulatory principles. As explained earlier, the purpose of introducing new activity-specific regulatory principles is to enable government and Parliament to direct the regulators to have regard to specific broader public policy issues that may be relevant to the particular financial services activity being regulated. When proposing new policy or rules in the specified area of regulation, the regulators would be obliged to explain how they have considered the issues set out in these principles. So, for example, when exercising its general functions for the prudential regulation of insurance, the PRA might, among other things, be obliged to have regard to the following principles:

- a) The role of insurance business in facilitating sustainable growth in the UK economy; and in particular, the important role that the insurance, reinsurance and alternative risk-transfer sectors play in providing sustainable finance and a supply of long-term investment to support UK economic growth, including the supply of finance for infrastructure projects.
- b) The socially important role that a viable and sustainable life insurance sector plays in retirement provision for UK citizens.
- c) The desirability of innovation in insurance, reinsurance and alternative insurance risk transfer services in order improve the management of risk for individuals and businesses, and to help maintain the UK's leading position as a centre for excellence in insurance, reinsurance and alternative risk transfer activities.

The approach taken in the 2020 Financial Services Bill

2.39 The forthcoming Financial Services Bill contains important provisions which enable updates to the UK's prudential regime for banks and investment firms, including provisions to meet the UK's international commitments as a member of the Basel Committee and provisions to introduce a new proportionate regime for non-systemic investment firms. The pragmatic legislative approach adopted for these measures is designed to ensure that the UK meets its international obligations on time and the prudential regime keeps pace with international developments, but it has also been designed to be largely consistent with the government's proposed direction of travel for the UK's overall regulatory framework as set out in this consultation. In particular, these Bill measures reflect the split of regulatory responsibilities proposed under the post-EU framework approach and illustrate how new activity-specific policy framework legislation will be developed. The Bill provisions include new regulatory principles which the relevant regulator must have regard to when designing rules to implement either the new Basel standards or the new prudential regime for investment firms. The Bill provisions also provide for

adapted transparency requirements requiring the relevant regulator to explain how it has considered the new regulatory principles. However, the Bill provisions do not represent the full post-EU framework approach. For example, the provisions relating to Basel standards cover specific areas of prudential regulation and do not provide for policy framework legislation covering the whole of the prudential regime. More information on the approach taken in the Bill can be found in the policy statement published by HM Treasury on 23 June 2020 at <https://www.gov.uk/government/publications/prudential-standards-in-the-financial-services-bill-june-update>.

How the post-EU framework proposal meets FRF Review objectives

2.40 The government thinks that the post-EU framework blueprint builds on the strengths of the existing FSMA model and should meet the objectives set for the FRF Review as follows.

- **Clear, coherent and effective allocation of regulatory responsibilities** – The proposed approach will provide for a clearer split of responsibilities than has so far existed under the FSMA model and while the UK has been a member of the EU. This is important to provide for efficient operation of the framework which avoids duplication of effort and also ensures that each of the institutions involved makes the most effective contribution. In the UK system, regulatory expertise is concentrated in the regulators, informed by the day to day supervision of firms and markets they carry out. The proposal makes the most of that expertise in the design and implementation of regulatory requirements. Government and Parliament can make a strategic contribution by setting the overall policy framework in specific areas of financial services regulation, specifying the key policy priorities and considerations that must be taken into account when designing regulatory requirements in each of those specific areas.
- **Appropriate policy input by democratic institutions** – While the FSMA model involves government and Parliament setting the institutional framework, high-level, cross-cutting objectives for the regulators, and the scope of regulated activities, it does not enable them to set out the overall policy approach for specific areas of regulation. The post-EU framework proposal aims to enhance policy input, giving government and Parliament a strategic role in financial services regulation which enables them to set out key policy issues which must be considered in the design of regulatory requirements.
- **Clearer basis for effective accountability and scrutiny** – Parliament will need to consider whether and how it adapts its approach to scrutiny of the work done by HM Treasury and the financial regulators. But regardless of how Parliamentary scrutiny is carried out, the post-EU framework proposal would support more effective accountability and scrutiny, particularly in relation to the work of the regulators. Activity-specific policy framework legislation will provide a clearer set of purposes and policy considerations

by which the performance of the regulators can be assessed in each key area of regulation.

- **Agile regulatory regime** – Activity-specific policy framework legislation should be sufficiently high-level to be durable and require infrequent updating, while specific requirements set through regulator rules can be flexed and updated efficiently in order to take account of changing market conditions, address emerging risks early on and facilitate innovation in financial services provision.
- **Coherent and more user-friendly regime for end-users** – The UK's existing regulatory arrangements have resulted in a complicated and fragmented regulatory rulebook for firms. To some extent this has been unavoidable while the UK has been a member of the EU – all EU countries must work with a combination of EU and domestic legislation and rules. Exit from the EU offers an opportunity to rationalise rulebooks and make them easier to work with. The post-EU framework proposal aims to bring about, as much as possible, a single source of requirements for firms – the regulators' rulebooks. And those regulatory requirements can be designed and expressed in ways best suited to UK circumstances. Rationalising the regime in this way would be delivered gradually over time.
- **Internationally respected approach** – The post-EU framework proposal makes the most of the UK's internationally respected regulators. This delegation of responsibility for regulatory requirements to regulators operating independently from government is supported by the academic literature on financial regulation and by the IMF and OECD. Given the UK's position as a global hub for financial services and the important role it plays in the international financial system, a regulatory approach which commands confidence internationally should be a priority for the UK framework.

Reviewing the FSMA cross-cutting regulatory principles

2.41 In addition to the proposed introduction of new activity-specific regulatory principles, the government will be reviewing the existing cross-cutting regulatory principles set out in FSMA. The regulatory principles were designed to promote regulatory good practice across the range of the regulators' policy-making functions. But some of those principles are now 20 years old and the regulatory landscape has changed considerably. The government will be examining whether these remain the right cross-cutting principles to apply during the regulator's policy-making processes. For example, the government believes EU exit offers an important opportunity to create a more coherent, easier to navigate regulatory regime. The post-EU framework approach is designed to result in, as much as possible, one source of regulatory requirements for firms – the regulator rulebooks and policy documents. The government is interested, for example, in a regulatory principle which requires the regulators to have regard to the importance of accessible, easy to navigate rulebooks, which take advantage of practices and innovations that minimise the compliance burden on firms, such as 'machine-readable' rules.

2.42 It will be important to ensure a sensible balance between cross-cutting and activity-specific regulatory principles. Dealing with a profusion of activity-specific regulatory principles could become a disproportionate resource challenge for the regulators, leading to ineffective outcomes, and could be confusing for stakeholders. If certain policy considerations are relevant to many areas of regulation, it would be more appropriate for these to be reflected in cross-cutting regulatory principles which are designed to inform the regulators' activities across the full range of their responsibilities.

The regulators' overarching statutory objectives

2.43 The overarching statutory objectives for the PRA and FCA set in FSMA are an effective way of ensuring appropriately strong regulatory focus on the policy priorities of financial stability, consumer protection, the integrity of financial markets and competition. Prioritising these policy aims remains vital to ensure a stable and fair financial system in which the British public and the UK's international stakeholders can have confidence.

2.44 In recent years there has been an ongoing debate in Parliament and among industry stakeholders on whether these objectives should be added to or adapted. Much of this debate has centred on whether there should be an objective to support the competitiveness of the UK financial sector. Given the importance of a thriving financial services sector for UK economic growth and prosperity, it is argued that the regulators should have a statutory duty to support the economic viability of financial services and the ability of the sector to compete internationally. Supporters of this view argue that some other countries have, in some way, balanced regulator objectives for financial stability and consumer protection with objectives related to competitiveness. It is also argued that a secondary objective on competitiveness, subordinate to primary objectives around the safety and soundness of firms, market integrity, consumer protection and competition (only the FCA has a primary objective for competition), would deliver appropriate regulator focus on competitiveness issues without undermining the policy priority given to a stable and fair financial sector.

2.45 But, as debated when the Financial Services Act 2012 went through the legislative process, the risk remains that a new competitiveness objective could distract from or dilute the key stability, market integrity and consumer protection objectives. There is an argument that one of the reasons for regulatory failure leading up to the financial crisis was an excessive concern for competitiveness leading to the acceptance of a 'light-touch' approach to regulation and supervision. It could also be argued that a regulatory regime with a sufficiently strong focus on financial stability, consumer protection and competition will promote confidence in UK regulated firms and thereby enhance their ability to compete internationally.

2.46 The new activity-specific regulatory principles proposed in this consultation would be equivalent to the existing general regulatory principles set out in FSMA and would be subordinate to the regulators' statutory objectives. Nevertheless, regulatory principles are important statutory provisions under the FSMA model. They set out policy issues and considerations which the regulators must take into account. Under the post-EU framework proposal, they would enable government and Parliament to be more specific about the policy issues that should be considered

in key areas of regulation, with the aim of instructing the regulators to think about the broader public policy implications that financial services regulation may have. The post-EU framework proposal is also intended to enhance transparency so that regulators are required to explain to Parliament and the public how the regulatory principles have been considered in the policy-making process. The government thinks that these activity-specific regulatory principles could bring about enhanced regulator focus on a broader range of public policy issues, including competitiveness, without needing to change the regulators' overarching objectives.

2.47 The government invites views on this issue, and particularly on how adapting the regulators' statutory objectives would compare with the introduction of new regulatory principles as part of the post-EU framework proposal. Views are also invited on the risks that changing statutory objectives might generate.

Box 2.A: Key questions for consultation respondents

- 1 How do you view the operation of the FSMA model over the last 20 years? Do you agree that the model works well and provides a reliable approach which can be adapted to the UK's position outside of the EU?
- 2 What is your view of the proposed post-EU framework blueprint for adapting the FSMA model? In particular:
 - What are your views on the proposed division of responsibilities between Parliament, HM Treasury and the financial services regulators?
 - What is your view of the proposal for high-level policy framework legislation for government and Parliament to set the overall policy approach in key areas of regulation?
 - Do you have views on how the regulators should be obliged to explain how they have had regard to activity-specific regulatory principles when making policy or rule proposals?
- 3 Do you have views on whether and how the existing general regulatory principles in FSMA should be updated?
- 4 Do you have views on whether the existing statutory objectives for the regulators should be changed or added to? What do you see as the benefits and risks of changing the existing objectives? How would changing the objectives compare with the proposal for new activity-specific regulatory principles?
- 5 Do you think there are alternative models that the government should consider? Are there international examples of alternative models that should be examined?

Chapter 3

Accountability, scrutiny and stakeholder participation

3.1 In a modern democracy, individuals and businesses rightly expect public bodies that exercise important regulatory functions to be accountable for their actions. In many cases, such regulatory functions will be exercised by government departments (usually through the development and implementation of legislation), which are led by elected politicians who are directly accountable to Parliament and ultimately to the electorate. In the UK there are well established mechanisms for Parliament to hold government Ministers to account.

3.2 In many areas of public policy, important regulatory functions are delegated to public bodies which are not led by elected politicians and which operate with some degree of independence from government. Financial services regulation is such an area, where many countries have delegated important responsibilities to regulators that operate independently from government. This approach has been a feature of the UK financial services regulatory framework for almost 40 years.

3.3 While the government thinks this is the most effective approach to the regulation of financial services, for the reasons set out in the previous chapter, it raises important issues around how regulators should be accountable, both to elected politicians and to the general public. The government thinks that existing accountability arrangements for UK financial services regulators have operated effectively for many years. But accountability of the regulators will take on greater importance when their responsibilities expand as a consequence of leaving the EU and under the proposals set out in this consultation. Accountability, scrutiny and public engagement with the work of the regulators is therefore a particularly important theme of this review.

3.4 Before going on to examine the accountability, scrutiny and public engagement arrangements for UK regulation of financial services, it is important to be clear on what the government means by these terms. Accountability can be said to operate in two key ways: to be 'called' to account and to be 'held' to account. The UK's regulatory authorities are called to account in that they are obliged to give an account of their actions to a wide range of stakeholders, including the general public. In addition, the regulatory authorities are subject to arrangements under which they are held to account – that is, their actions can be questioned and challenged by another authority. Who the UK's regulatory bodies are accountable to and the form that accountability takes is explained below.

3.5 **Constitutional accountability.** In the exercise of its legislative powers, Parliament is sovereign. All the UK authorities with responsibility for financial services policy and regulation are therefore ultimately accountable to Parliament in

some way. This involves being called to account and held to account by Parliament. Treasury Ministers are drawn from Parliament and are directly accountable to it. The financial services regulators are for the most part accountable to Parliament through Treasury Ministers. In addition to this, the UK framework includes a specific mechanism for Parliament to directly hold the regulators to account (see the explanation of the select committee system below). The regulators, when exercising the powers delegated to them by Parliament, make regulatory decisions independently from government and Parliament. But Treasury Ministers and Parliament have the right to require the regulators to explain and justify those decisions. The mechanisms by which Ministers and the regulators are held to account by Parliament are explained in paragraphs 3.14 to 3.16 below.

3.6 Accountability under the law. HM Treasury and the regulators must exercise their regulatory functions in accordance with the law. Judicial Review can be used by individuals or organisations to challenge the Treasury or a regulator if the law has not been followed in the way decisions have been reached. This could include how HM Treasury has developed policy or legislation, or how the regulators have developed policy, implemented rules or applied statutory requirements. Readers should be aware that the government has appointed an independent panel of reviewers to examine whether there is a need to reform the judicial review process.

3.7 Accountability to the general public. HM Treasury and the regulators, when making policy or regulatory proposals, are called to account by obligations to give public explanations which make the case for those proposals. For HM Treasury, this requirement flows from government policy to consult the general public. For the regulators, Parliament has set statutory requirements to consult the general public on rule proposals.

3.8 Scrutiny and public engagement. These are the means by which accountability is made effective as well as being essential parts of good policy-making process. It is the ability of interested parties to critically examine policy and the obligation of regulatory institutions to engage with and consider the views of those parties. Various scrutiny and engagement mechanisms exist to facilitate the various forms of accountability which operate in the UK's regulatory framework. These are examined below alongside possible options for enhancing scrutiny and engagement in the UK's post-EU regulatory framework.

The case for reviewing accountability, scrutiny and engagement arrangements

3.9 Adapting the regulatory framework to the UK's new position outside of the EU offers the opportunity to consider whether existing accountability and scrutiny arrangements are appropriate and effective. But there are also two specific reasons for considering whether these arrangements need to be adapted.

3.10 As set out above, HM Treasury and the financial services regulators are accountable to Parliament. But in practice accountability to Parliament has been complicated and limited by increasing EU competence for financial services regulation. Withdrawal from the EU entails a restoration of UK national sovereignty and substantial policy-making responsibility. As Parliamentary sovereignty is central to the UK's constitutional arrangements, examining the role of Parliament in

scrutinising the work of HM Treasury and the regulators will be an important theme for this review. Now that the UK has left the EU, the government wishes to ensure that the UK Parliament has a meaningful and effective role in setting the overall approach for UK financial services policy (see the previous chapter on the post-EU framework proposal) and in scrutinising the work of the authorities responsible for maintaining the UK's regulatory regime.

3.11 Central to the post-EU framework proposal is a clear division of responsibilities under which the financial services regulators become responsible for the great majority of the regulatory requirements that apply directly to financial services firms and markets. This is in line with the approach that Parliament has previously endorsed for some areas of financial regulation that were developed at domestic, rather than European, level, such as the Senior Managers and Certification Regime. The government thinks that this division of responsibilities will meet the objectives it has set for an effective regulatory framework, but it must be acknowledged that in most areas of regulatory policy, this approach will result in greater policy responsibility and discretion for UK regulators than has existed at any time since the early operation of FSMA following its introduction 20 years ago. The review must therefore ensure that this expansion in the regulators' responsibilities is matched by appropriate and effective accountability arrangements which command the confidence of Parliament and the public, and which also deliver real value to the work of the regulators and firms in terms of contributing to the effectiveness of the overall framework.

Review of existing accountability, scrutiny and public engagement arrangements

3.12 In thinking about the accountability, scrutiny and public engagement arrangements relevant to financial services regulation, there are three key relationships that need to be examined:

- The accountability of HM Treasury and the financial services regulators to Parliament and the role that Parliament plays in scrutinising the work of these institutions;
- Engagement on policy between the regulators and HM Treasury in the context of the close working relationship and coordination arrangements that exist between the UK authorities responsible for financial services regulation; and
- Engagement with, and scrutiny by, the range of stakeholders that may be affected by the work of HM Treasury and the financial services regulators, including market participants and consumers.

3.13 For the reasons set out in paragraphs 3.10 and 3.11, this review will need to focus on two key aspects of scrutiny and stakeholder engagement: the role played by Parliament in scrutinising the work of HM Treasury and the financial services regulators; and scrutiny of, or engagement with, the regulators by the full range of public stakeholders.

Existing Parliamentary scrutiny arrangements

3.14 There are long-established scrutiny arrangements in place for Parliament to hold Ministers of the Crown accountable. Government Ministers regularly respond to oral and written questions in both Houses of Parliament; government policy is scrutinised through a range of Parliamentary debates; government legislation is debated and scrutinised according to the procedures for primary and secondary legislation; and both Houses of Parliament are kept informed of policy and regulatory initiatives through the making of ministerial statements and by the laying of important documents before Parliament, including the annual reports of the financial services regulators. These long-standing arrangements will continue to be central to the work of Parliament in holding Ministers to account for the work of HM Treasury and the UK's financial services regulators.

3.15 There is one further aspect of Parliamentary scrutiny which has developed to become particularly important in financial services policy and particularly in relation to the work of the regulators: the system of Parliamentary select committees. Select committees have been a feature of Parliamentary scrutiny for centuries, but the modern select committee system can be traced back to the committee reforms made in 1979, which established a system of departmental select committees to shadow each government department. These reforms included the creation of the Treasury and Civil Service Select Committee, which became the Treasury Select Committee (TSC) in 1995.

3.16 Relevant select committees, and the TSC in particular, provide scrutiny of financial services policy in the following ways:

- **Select committee inquiries** – The committees choose their own subjects of inquiry and decide the duration and approach that will be used for each inquiry. The committees have the power to send for “persons, papers and records” which they decide will be relevant. Witnesses asked to give evidence to an inquiry relating to financial services can include Treasury Ministers and senior officials as well as senior officials from the financial services regulators. The TSC has undertaken many high-profile and influential inquiries, including its examination of the regulatory failures that contributed to the financial crisis. Other committees, such as the former House of Lords EU Financial Affairs Sub Committee and the House of Commons European Scrutiny Committee, have also played a key role in scrutinising aspects of financial services policy.
- **Regular hearings to scrutinise the work of the financial services regulators** – As the regulators are associated public bodies of HM Treasury, the TSC routinely examines the regulators’ approach to policy and administration. As part of this work, senior officials from the regulators attend general accountability hearings - for instance the FCA appears before the TSC biannually and the PRA appears before the TSC after the publication of each annual report.
- **Appointment hearings for key senior leadership positions in the financial services regulators** – It is now established practice for the TSC to use appointment hearings to scrutinise the appointment of individuals to key senior leadership positions in the regulators. For example, the TSC recently

questioned the newly appointed FCA CEO and the Governor of the Bank of England.

Adapting Parliamentary scrutiny

3.17 The government thinks that Parliament should play an important strategic role in interrogating, debating and testing the overall direction of policy for financial services. The proposed post-EU framework approach is intended to ensure Parliament has the opportunity to set out in legislation the overall purpose of key regulatory regimes and to include in that activity-specific legislation a description of the key policy issues that the regulators should have regard to when formulating policy and setting standards. This will give Parliament an enhanced strategic policy role when compared with either the original FSMA model or when compared with the role that Parliament has had in the development of EU financial services regulation. This should be complemented by a strategic approach to Parliamentary scrutiny.

3.18 The government thinks that the long-established scrutiny mechanisms referred to above will continue to be effective in holding Ministers to account for the work of HM Treasury and the financial services regulators. Indeed, the effectiveness of these mechanisms would be enhanced by the role that Parliament will play in setting the overall direction of policy through the proposed post-EU framework approach. Policy framework legislation for specific areas of regulated activity should establish a clear set of policy priorities which Parliament can use to examine the performance of HM Treasury and the regulators against.

3.19 As explained above, the role of select committees, and particularly the contribution made by the TSC, is central to the scrutiny of financial services policy by Parliament. There are two key reasons why Parliament may wish to focus on the select committee system when considering its future approach to Parliamentary scrutiny of financial services policy.

3.20 Firstly, the government thinks that enhanced Parliamentary focus on the key public policy issues related to financial services would improve the overall operation of the UK's regulatory framework. It is, to a great extent, the select committees which provide this strategic policy focus in Parliament, using their inquiries to produce in-depth analysis of significant public policy challenges, drawing on the expertise of a range of interested stakeholders. In recent history, the TSC has had a prominent role in examining the regulatory failures that contributed to the 2007-08 financial crisis and in helping to shape the policy response to the crisis.

3.21 The second reason for focusing on the role of Select Committees is that this Parliamentary scrutiny mechanism already provides for a direct accountability relationship between the regulators and Parliament. The TSC routinely examines the work of the regulators, scrutinises senior regulator appointments and conducts inquiries which are directly relevant to the work of the regulators. The appearance of senior regulator officials before select committees is now a well-established feature of the UK's regulatory framework.

3.22 It is of course for Parliament to decide whether and how it will adapt its approach to scrutiny. The government would like to work with Parliament to explore

how the select committee system will provide effective Parliamentary scrutiny in the future.

Relationship between HM Treasury and the regulators

3.23 As the authorities responsible for UK financial services regulation, the relationship between HM Treasury and the regulators involves wide-ranging collaboration and coordination of regulatory action. As highlighted by Phase I of the FRF Review, effective coordination between regulatory bodies is vital for the smooth and successful operation of our regulatory regime. It should help ensure high-quality policy-making, prevent overlapping initiatives, and avoid overloading firms with new regulatory measures.

3.24 Treasury Ministers have overall responsibility for the UK's financial services regulatory framework. Treasury Ministers can therefore be regarded as having a constitutional duty to scrutinise the work of the regulators as part of their responsibility for ensuring effective operation of the framework. An important feature of that framework, for the reasons set out in the previous chapter, is that the regulators operate independently from government and Parliament. As long as the regulators are acting within their FSMA statutory powers, and in accordance with other relevant financial services legislation, judgements on policy, rule-making and supervision are for the regulators to make.

3.25 However, legislation does provide for certain accountability mechanisms between the regulators and HM Treasury in specific circumstances:

- The Treasury may appoint an independent person to conduct a review of the economy, efficiency and effectiveness of the FCA's use of resources.¹
- The Treasury may direct the PRA or FCA to carry out investigations into regulatory failures and other matters in the public interest.²
- The Treasury may direct the PRA or FCA to take action, or refrain from taking action, necessary in order to ensure that the UK meets its international obligations.³
- The Treasury may require the PRA or FCA to comply with certain statutory provisions on the keeping of accounts and audit.⁴

3.26 In addition, FSMA provides Treasury Ministers with the ability to make recommendations to the regulators on issues related to matters of economic policy through open 'remit' letters.

3.27 As part of their general responsibility for the effective operation of the UK's regulatory framework, it is particularly important that Treasury Ministers are able to assess the implications of regulator proposals for broader government economic and social policy priorities, and to feed in views during the regulators' policy development stage. To achieve this, HM Treasury should be consulted early in the

¹ Section 15 of FSMA.

² Section 77 of the Financial Services Act 2012.

³ Section 410 of FSMA – international obligations, including those related to equivalence assessments. ⁴ Schedules 1ZA and 1ZB of FSMA.

regulators' policy development process, before proposals reach the public consultation stage. It must be emphasised that this should not affect the ability of the regulators to take decisions independently of government when exercising the powers delegated to them in legislation.

3.28 The development of new policy and legislative proposals will continue to benefit from the expertise of the regulators and their day to day experience of supervising regulated activities. In many cases the regulators will be responsible for operationalising or applying new legislative measures, for example when HM Treasury uses legislation to create a new regulated activity. Ensuring such legislation works well in practice will therefore benefit from the input of regulators.

3.29 An example of the importance that coordination arrangements will take on in the framework proposed by this consultation is provided by the equivalence arrangements and mutual recognition agreements the UK is currently putting in place with other countries. Under the proposed post-EU framework approach, regulators will have lead responsibility for setting the regulatory requirements that apply to firms. A significant rule change by a regulator could have material implications for the continued operation of an equivalence decision or mutual recognition agreement. HM Treasury will continue to have overall responsibility for the UK's cooperation and trading relationships with other countries. It is therefore appropriate that Treasury should be consulted if a regulator is developing proposals which may have an impact on the UK's relationship with another country.

Adapting coordination arrangements between HM Treasury and the regulators

3.30 To a great extent, early consultation between the regulators and Treasury on rule or legislative proposals already takes place. But the importance of this aspect of regulatory coordination suggests that such consultation and engagement should be made a more systematic part of the UK framework. This could be achieved by requirements in legislation, arrangements set out in a Memorandum of Understanding (MOU) or a combination of the two. This is in line with existing arrangements for the PRA and FCA to consult with each other on rule proposals. FSMA places an obligation on the regulators to consult each other, which is made operational and effective by an MOU setting out how the obligation should operate in practice.

3.31 The government proposes a general arrangement whereby the regulators consult HM Treasury more systematically on proposed rule changes at an early stage in the policy-making process and before proposals are published for public consultation. The aim here is to give the Treasury sufficient time to consider any broader public policy implications that regulator proposals may have and to allow the opportunity to feed back views to the regulators if necessary. It is important to stress that this policy coordination arrangement would only allow the Treasury to feed in views as regulator policy is being developed. It would not give Ministers a veto over the regulators' rule-making functions or act as a constraint around the regulators' policy discretion when designing rules. As Treasury Ministers have overall responsibility for financial services policy and the regulatory framework, providing for Ministers to contribute views in this way is appropriate. The working arrangements to achieve this will need to be developed by HM Treasury and the

regulators, and they will need to ensure efficient engagement between the three institutions. In particular, it will be important to ensure that such arrangements do not prevent the regulators from introducing rule changes quickly where needed. For example, these arrangements should not prevent the regulators from introducing immediate rule changes necessary to safeguard financial stability or protect consumers, as provided for under FSMA, or minor technical amendments needed to ensure the coherence and consistency of the regime.

3.32 The remit letters that enable Treasury ministers to make recommendations to the regulators related to economic policy will remain in use. While the new regulatory principles in legislation will be the primary means by which HM Treasury and Parliament will direct the regulators to have regard to important economic and competitiveness issues, the remit letters would be used to make recommendations related to particularly topical issues or challenges that would be difficult to reflect in legislation. As such, these letters are expected to be used more frequently than has previously been the case. When these letters are sent, they will be copied to the relevant select committees in Parliament. The government will also consider whether it is appropriate to place an obligation on the regulators to respond and explain how they have taken into account the recommendations made in these letters.

3.33 As explained earlier, HM Treasury, with the approval of Parliament, decides which financial services activities should be regulated. This is usually referred to as setting the regulatory perimeter for financial services. There are of course ongoing discussions with the regulators about maintaining the perimeter and HM Treasury consults the regulators on any changes to the perimeter. The government believes that reviewing the perimeter would benefit from more systematic engagement between HM Treasury and the regulators. The government has therefore committed to holding an annual perimeter review meeting. The next meeting will take place between the City Minister and the Chief Executive of the FCA following publication of the FCA's annual perimeter report on 29 September 2020. To enhance transparency around policy thinking to maintain the perimeter, HM Treasury will publish a record of these meetings.

Engagement with interested stakeholders during the policy-making process

3.34 As set out above, HM Treasury and the regulators are called to give an account of their actions to the general public and are held to account by Parliament. In addition, Treasury and the regulators are required to engage with interested stakeholders as part of the policy-making process and are obliged to carefully consider the views of stakeholders before finalising legislative or regulatory proposals.

3.35 The opportunity for individuals, relevant stakeholders and firms to engage with and scrutinise the development of proposals is essential for two key reasons. First, any policy-making process risks being deficient if it does not draw on the views, experience and expertise of those who may be impacted by regulation. Good policy-making should, as much as possible, be based on evidence and should take into account evidence that external stakeholders may be able to provide. Second, meaningful engagement by stakeholders helps support the policy-making process, making it more likely that finalised proposals are effective, understood and accepted as reasonable by stakeholders.

Existing arrangements for public engagement

3.36 HM Treasury and the regulators are subject to a number of obligations intended to support stakeholder engagement with the policy-making process and to help ensure policy-making is rigorous, evidence-based and open to external challenge. These are explained below.

3.37 As part of the policy-making process, HM Treasury consults on new policy proposals and new legislation. These consultations are conducted in line with the Cabinet Office [Consultation Principles](#).

3.38 HM Treasury's legislative proposals are also subject to the [Better Regulation Framework](#), which provides that Regulatory Impact Assessments (RIA) and Post Implementation Reviews (PIR) are conducted where the equivalent annual net direct cost to business is greater than £5m. These assessments and reviews are subject to independent scrutiny by the Regulatory Policy Committee (RPC). For measures below this threshold the Treasury undertakes a proportionate cost-benefit analysis.

3.39 Engagement with stakeholders is embedded in the regulators' policy-making process through the application of statutory requirements and public law principles. The PRA and FCA are subject to statutory requirements in FSMA which, in general, oblige them to consult on rule or general guidance proposals. These PRA and FCA consultations are generally open for 3 months, although this can change depending on the issue – for example, in case of emergency, consultation periods can be significantly shorter. As part of consultation requirements, the PRA and FCA must explain why a proposed course of action is compatible with their strategic and operational objectives as set by Parliament in FSMA. The regulators must also explain how the proposals are compatible with their obligation to have regard to the FSMA regulatory principles. For rule proposals, a draft of the rules must be included, accompanied by a cost-benefit analysis where practicable to do so. Before making final rules, the regulators are required to give an explanation of the representations received and how they have been taken into account. These requirements are designed to ensure market participants and wider stakeholders have a meaningful opportunity to scrutinise and feed into the development of regulator policy, guidance and rules.

3.40 The regulators also employ other methods of stakeholder engagement which go beyond statutory requirements. For example, the regulators use Discussion Papers and Calls for Input, where appropriate, to gather views on policy issues at an early and formative stage. These help to inform the development of proposals for consultation, especially where policy issues are particularly complex or finely balanced, such as the 2017 Discussion Paper on Distributed Ledger Technology, which helped to develop more detailed thinking and guidance on cryptoassets.

3.41 The Treasury, along with the FCA and the PSR, is required under the Small Business, Enterprise and Employment Act 2015 to publish a Business Impact Target (BIT) Score for any qualifying regulatory provisions (QRPs), as part of reporting under the BIT. The RPC is responsible for verifying all BIT scores.

The role of statutory panels in the regulators' policy-making process

3.42 To contribute to the regulators' policy-making functions, FSMA established a system of panels to represent the interests of consumers and industry practitioners, including smaller regulated firms and financial market participants. Drawing on the experience and expertise of their respective memberships, these panels are intended to provide valuable insight, advice and challenge across all the regulators' regulatory functions. Panel members are appointed by the regulators, and the Chairs are approved by HM Treasury. The regulators consult these panels from a very early stage in policy development to help ensure proposals are designed to meet their policy aims and can be supported by use of available evidence. The FCA and PRA consult these panels on all major policy and regulatory interventions, but the panels also set out their own views publicly and independently, through their Annual Reports, their strategic priorities and responses to regulator consultations.

3.43 The FCA works with five independent panels. Four of these are established by FSMA⁵ with a further non-statutory panel (the Listing Authority Advisory Panel) created by the FCA:

- The Financial Services Consumer Panel represents the interests of consumers using or contemplating using financial services, including SMEs, where relevant.
- The Practitioner Panel represents the interests of regulated firms, and provides input from the industry's view. It also works with the FCA to carry out its annual survey of stakeholder views of the FCA's performance as a regulator.
- The Smaller Business Practitioner Panel represents the interests of smaller regulated firms.
- The Markets Practitioner Panel provides input from the point of view of financial market participants.
- The Listing Authority Advisory Panel advises the FCA on policy issues that affect issuers of securities.

3.44 The PRA works with one statutory industry practitioner panel⁶, which includes an insurance sub-committee. The panel represents the interests of industry practitioners from areas of financial services activity that are subject to PRA regulation: deposit taking, insurance and large or complex investment firms. The Panel considers the PRA's policies and practices and provides input to help it meet its statutory and operational objectives.

3.45 The strategy and policy work of the Payment Systems Regulator (PSR) also benefits from the input of a statutory Panel. The PSR Panel is made up of members drawn from payments system operators, payments service providers, infrastructure and technology providers and service users including consumer, large and small business representatives. While the framework arrangements for the PSR are not covered by this consultation, reviewing the contribution made by the PRA and FCA

⁵ Section 1M of FSMA.

⁶ Section 2M of FSMA.

panels may also be relevant to the PSR panel. In due course the government will consider whether framework arrangements for non-FSMA areas of regulation, including payment systems, should be reviewed and adapted.

Options for adapting stakeholder engagement with policy-making processes

3.46 The review needs to consider whether existing policy-making processes are effective, and the extent to which existing engagement and scrutiny arrangements allow for meaningful participation in the policy-making process by the broad range of stakeholders that may have an interest. This review is, in particular, focussed on the policy and rule-making processes of the regulators, as it is the role of regulators that will be most affected by withdrawal from the EU and the framework approach proposed in this consultation. This review is an important opportunity to ensure the regulators' approach to policy-making is as effective as possible. A wide range of potential options that might be explored is set out below.

3.47 Adapting the contribution made by the existing statutory panels – As explained above, the regulators seek and have regard to the views of these panels, including during the early stages of the policy-making process and through public consultation at the formal proposal stage. The government thinks that the panels can provide effective representation of key stakeholder groups and make a valuable contribution to the regulators' policy-making functions. But the government would be interested in views on whether and how the independent challenge function of the panels might be enhanced and whether the work of the panels could be made more transparent in order to aid the engagement of, and scrutiny by, stakeholders during the policy-making process. How the panel memberships are decided, how their remits are set in legislation and how their work is resourced and supported may be relevant issues to examine. Parliament may also wish to consider whether it wishes to give greater weight to the work of the panels in its scrutiny of the regulators, including holding the chairs of the panels to account for their contribution to policy and rule-making by the regulators.

3.48 Reviewing the regulators' consultation obligations or practices – The statutory requirements for the regulators to consult stakeholders on their rule or guidance proposals are a core scrutiny mechanism in the regulatory framework. FSMA sets requirements for consultation, but in many cases the regulators' practices go beyond these requirements. The government would be grateful for views on whether and how these obligations or practices might be adapted to help improve the policy-making process and the scrutiny of proposals. For example, cost/benefit analysis when required of public bodies is intended to provide a reliable assessment of the likely impact on affected stakeholders and to demonstrate that the benefits delivered will justify the costs involved. The government would be interested in views on whether the regulators' cost-benefit analysis obligations or practices could be improved to better achieve this and to contribute to high-quality, evidence-based policy, while not over-burdening the sector with information requests.

3.49 Introducing more systematic review of regulator rules – In recent years the principle of reviewing regulation after it has been in operation has been embedded in government legislative initiatives. New legislation now routinely includes a requirement for measures to be reviewed after 5 years to check those measures are

achieving their intended aims. The regulators already make use of such reviews in some areas. The FCA, for example, has publicly committed to carrying out such reviews to ensure there is a strong evidence base to guide future decisions, and it has set out its framework for doing so. More routine use of such reviews might be expected to help ensure that regulatory rules are achieving their intended aims and remain effective in the face of changing conditions. But more regular reviews will have resource implications and could divert the regulators' attention from other important tasks as well as potentially introducing greater burden for industry, for example if additional data is required from industry to conduct reviews. The government would be interested in views on the benefits and challenges of making *ex-post* rule reviews a more routine part of the regulators' rule-making functions.

3.50 Independent review of regulator rules - A further option might be to make use of independent, expert reviewers to carry out more significant reviews, such as the review of a whole regulatory regime. The power to appoint an independent reviewer could be conferred on the regulators, or HM Treasury could be responsible for appointments, similar to Treasury's existing responsibility for deciding on the use of independent investigations to examine the outcome of specific regulator policies or interventions. The relevant Parliamentary select committee might also have a role in contributing to, or scrutinising, the review of regulator rules.

3.51 A new external, independent scrutiny function – Some industry stakeholders, including those represented by the International Regulatory Strategy Group (IRSG) have suggested establishing a new external and independent committee to scrutinise the regulators' rule proposals and the evidence on which proposals are based (including cost-benefit analysis where relevant). This committee could have a similar function to the Regulatory Policy Committee (RPC), which provides challenge to government departments (and the FCA in some areas of its rule-making responsibilities) during the policy development stage, with the committee issuing reports to aid public scrutiny of proposals once they have reached the public consultation stage. In theory, such a committee could provide valuable expert, independent challenge to the regulators during the policy development process and could support public scrutiny of regulator proposals by issuing its own reports on whether proposals are likely to meet their intended objectives. But the practical obstacles to be overcome in making such a committee operate effectively are substantial. The government would need to be satisfied that this function would add real value to the policy process and would provide value for money for regulated firms and consumers. It would be important to ensure that such a function does not duplicate the contribution made by the existing statutory panels (which include independent expert members) or the industry trade associations (who already engage with regulatory proposals and provide expert challenge). Securing appropriate membership of the committee, so that it provides impartial expertise without becoming a conduit for any particular stakeholder interest, would be challenging. Ensuring the committee is adequately supported would likely require substantial resource, which would need to be financed through the regulators' levies on regulated firms. And while such a committee would have no power to veto a regulator proposal, its ability to openly challenge regulator proposals might raise issues about the regulators' independence. The government welcomes views on this option and how the challenges set out here might be addressed.

3.52 The government would welcome views from stakeholders on these potential options, as well as any other options to further strengthen the regulators' policy-

making process, or enhance the ability of stakeholders to engage with and scrutinise regulator proposals.

Box 3.A: Key questions for consultation respondents

- 6 Do you think the focus for review and adaptation of key accountability, scrutiny and public engagement mechanisms for the regulators, as set out in the consultation, is the right one? Are there other issues that should be reviewed?
- 7 How do you think the role of Parliament in scrutinising financial services policy and regulation might be adapted?
- 8 What are your views on how the policy work of HM Treasury and the regulators should be coordinated, particularly in the early stages of policy making?
- 9 Do you think there are ways of further improving the regulators' policy-making processes, and in particular, ensuring that stakeholders are sufficiently involved in those processes?

Chapter 4

Responding to this consultation and next steps

Delivering the Future Regulatory Framework

4.1 Applying the Future Regulatory Framework approach set out in this consultation to the vast body of retained EU law will require a significant programme of work by the government and regulators.

4.2 The government's proposed approach involves moving regulatory requirements that apply directly to firms and markets from the UK statute book and into the regulators' rulebooks. HM Treasury expects that this will require a substantial programme of legislation and we are exploring options to achieve the right balance of primary and secondary legislation within the government's wider legislative programme. Parliament will of course have the final say on the approach adopted and how that approach is applied through legislation.

4.3 HM Treasury and the regulators will also need to prioritise the areas of retained EU financial services law which are adapted first to the proposed framework approach. We welcome initial views from stakeholders on priorities. We will bring forward further detail on our approach to implementation, and welcome stakeholder views on this, in due course.

4.4 The government is committed to delivering a coherent and consistent approach across all parts of financial services regulation. Where appropriate, we will look to ensure that our wider programme of regulatory reform draws on the approach for the Future Regulatory Framework as this continues to develop.

Responding to this consultation

4.5 This consultation will remain open for three months, closing on 19 January 2021. We are inviting stakeholders to provide responses to the questions set out above, share their views on our proposed future approach to financial services regulation (the post-EU framework proposal), or to provide views on any issue relevant to the effective operation of the UK's framework for financial services regulation.

Who should respond?

4.6 A wide range of stakeholders will be interested in the important issues presented in this document. Responses are welcome from all stakeholders, including:

- Financial services institutions and firms
- Other businesses impacted by financial services regulation
- Trade associations and representative bodies
- Consumer groups

How to submit responses

4.7 Please submit your responses to FRF.Review@hmtreasury.gov.uk, or post to:

Future Regulatory Framework Review

Financial Services Strategy

HM Treasury

1 Horse Guards Road

SW1A 2HQ

4.8 More information on how HM Treasury will use your personal data for the purposes of this consultation is available on the FRF Review webpage.

Next steps

4.9 The important and wide-ranging issues raised by a review of the UK's financial services regulatory framework, combined with the broad range of stakeholders that will be affected, make a long-term, in-depth review process appropriate. The government is therefore conducting this phase of the FRF Review in two stages.

4.10 This first consultation sets out an overall blueprint for financial services regulation in the future, focusing on the split of responsibilities between Parliament, the government and the financial services regulators, and the approach to use of legislation for financial services. Alongside this, the consultation highlights the importance of ensuring appropriate and effective arrangements for accountability, scrutiny and public engagement with regulatory bodies, particularly the UK's financial services regulators given the breadth of responsibility they will take on under the proposed approach. The government will carefully consider the responses received and use these to inform a second consultation, setting out more detail on the proposed approach in the first half of 2021.

4.11 As part of this consultation, the government will also undertake a programme of stakeholder engagement. This will include a series of roundtables and workshops, to maximise opportunities for stakeholders to share their views with the government.

HM Treasury contacts

This document can be downloaded from
www.gov.uk

If you require this information in an alternative format or have
general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gov.uk