MANX INSURANCE ASSOCIATION
INTERNATIONAL LIFE ASSURANCE

Please reply to:

Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

12 October 2010

Dear Sir/Madam

Re: Cm 7874: A new approach to financial regulation: judgement, focus and stability

I am writing to respond to the above paper on behalf of the Manx Insurance Association (MIA), the trade body which represents authorised life assurance companies based on the Isle of Man (IOM).

All MIA members are prudentially regulated by the Isle of Man Government Insurance and Pensions Authority.

The products of MIA members can be marketed into the UK under the FSMA 2000 (Financial Promotion) Order 2001. Some member firms also choose to be regulated by the FSA for the conduct of business.

IOM firms have been authorised by UK regulators since the introduction of the Financial Services Act in 1986; by LAUTRO, the PIA and the FSA respectively. Under the PIA rules, Isle of Man firms were classified as category four members, i.e. that were jointly regulated or supervised. This classification recognised that such firms do effect and carry out contracts of insurance whilst not being subject to the prudential regulation of the UK regulator.

The FSA rules made no such allowance for the unique circumstances of IOM firms and thus the permissions of such firms had to be 'engineered' to some degree, with IOM firms being subject to the rules relating to investment firms. These rules are, at times, irrelevant to the activities of a life assurer.

We read the recent paper with interest and welcome the opportunity of commenting on the issues that relate directly to our members at this early stage. Our views are based on the experience that PIA category four membership reflected more accurately than current FSA permissions the unique situation of IOM firms.

We would welcome the establishment of a single conduct regulator in the form of the Consumer Protection and Markets Authority (CPMA); this would appear to facilitate the regulation of IOM firms for conduct of business without the need for the duplication of prudential regulation by the Prudential Regulation Authority (PRA).

We would be more than happy to discuss the issues raised in this response if it is felt that this would be useful.

Yours faithfully

John Hollis
Chairman

SUBMISSION BY MICHAEL McKEE TO HM TREASURY

RESPONSE TO CP: "A NEW APPROACH TO FINANCIAL REGULATION"

I am a Partner in DLA Piper, the international law firm, and lead the advisory side of the Financial Services Regulatory practice in the UK. This submission is made in a personal capacity.

It is based upon my experience of having worked for the London Stock Exchange, Citigroup, the British Bankers' Association (BBA) and DLA Piper over the past 15 years.

Over that period I participated in the policy discussions and the implementation which led to the creation of the FSA and the development of its role. I was also involved, working at a senior level for the BBA and as a member of the Financial Markets Committee of the European Banking Federation, in the negotiations leading to the development of key pieces of legislation forming the EU's Financial Services Action Plan including MIFID, the Market Abuse Directive, the Prospectus Directive, the Transparency Directive and the Takeover Directive.

My experience in relation to these regulatory issues has been recognised in the past by CESR selecting me to become a member of the Committee of European Securities' Regulators' Market Abuse Directive Practitioner Panel and by my selection as a member of the European Commission's forum group on the future of European capital markets. I have also given evidence to the Economic and Monetary Affairs Committee of the European Parliament with regard to the extension of the roles of CESR, CEBS and CEIOPS. I have also served on many HM Treasury and FSA working groups involving industry practitioners and focused on financial services regulatory matters.

I set out below my answers to the questions asked in the CP.

1. **Should the FPC have a single, clear, unconstrained objective relating to financial stability and its macro-prudential role, or should its objective be supplemented with secondary factors?**

   Some secondary factors should be taken into consideration.

2. **If you support the idea of secondary factors, what types of factors should be applied to the FPC?**

   The FPC should have regard to the impact of their decisions on the United Kingdom's attractiveness as a location for non-UK financial services institutions and, in consequence, the strength of international wholesale financial services business in the UK. The FPC should also have regard to the impact of their decisions on UK retail customers of financial institutions and seek, so far as practicable, to minimise loss to retail customers as a consequence of any financial stability decisions. The FPC should also have regard to the financial costs of any financial stability decisions and the likely impact on tax revenues, the Financial Services Compensation Scheme and other sources of funding.

3. **How should these factors be formulated in legislation – for example, as a list of "have regards" as is currently the case in the Financial Services and Markets Act 2000 (FSMA), or as a set of secondary statutory objectives which the FPC must balance?**

As a list of “have regards”.

4. **The Government welcomes respondents’ views on:**

   Whether the PRA should have regard to the primary objectives of the CPMA and FPC;

   Whether some or all of the principles for good regulation currently set out in section 2 of FSMA, particularly those relating to good regulatory practice, should be retained for the PRA;

   Whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and

   Whether there are any additional broader public interest considerations to which the PRA should have regard.

   There should be a hierarchy with regard to the objectives of the three bodies. Each should have regard to the objectives of the other but the FPC’s objectives should take precedence over the objective of the other two bodies and the PRA’s objectives should take precedence over the objectives of the CPMA.

   The principles for good regulation have generally worked well and should be retained for the PRA.

   The requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should definitely be retained.

   The PRA’s objective should be focused upon micro-prudential issues and those macro-prudential issues which relate to financial stability. Consequently the PRA should not be subject to any broader public interest objectives unless these are objectives that have been given also to the FPC and are suitable for it’s financial stability role.

5. **Is the model proposed in paragraph 3.16 – with each authority responsible for all decisions within their remit subject to financial stability considerations – appropriate, or would an integrated model (for example, giving one authority responsibility for authorisation and removal of permissions) be preferable?**

   In view of the decision to create the PRA and the CPMA the model proposed in paragraph 3.16 appears to be the correct one.

6. **Is the approach outlined in paragraph 3.17 to 3.23 for transfer of regulatory functions and rule making sufficient to enable the PRA to take a more risk-based judgement-focussed approach to supervision?**

   The key to making good risk-based judgements is the quality of staff and the quality of the information flowing to those staff. Consequently while the approach outlined may assist in enabling the PRA to take a more risk-based judgement focussed approach it will not be sufficient in itself.

   The implementation of the changes in the institutional framework and the creation of the PRA will lead to staff uncertainty and staff will leave. It will be important, therefore, to focus on staff retention and the training of staff in developing a more judgement based approach.

   Consideration also needs to be given to how the existing FSA ARROW framework and the IT supporting it will be used. It is suggested that, in the first instance, ARROW and the supporting IT, should continue to be the basis for supervising firms in both the PRA and the CPMA. It is inevitable, however, that there will need to be a separation out of the supervisory framework for CPMA firms from the supervisory framework for PRA firms – and that is likely to require a divergence in approach between the PRA (which will need a more sophisticated framework for prudential supervision) and the CPMA (which will needs a less sophisticated prudential supervision framework – but will also need a sophisticated conduct of business supervision framework).

7. **Are safeguards on the PRA's rule-making function required?**

   Yes.

8. **If safeguards are required how should the current FSMA safeguards be streamlined?**

   Most of the safeguards should continue in place and are a necessary protection. In particular consultation is necessary and a proper timescale before rules come into force. There is probably scope for streamlining aspects of the cost-benefit analysis process. This appears to have been overengineered.

9. **The Government welcomes views on the measures proposed in paragraphs 3.28 to 3.41, which are designed to ensure that the operation of the PRA is transparent, operationally independent and accountable.**

   The measures proposed seem appropriate. However, there does not appear to be any provision for an equivalent to the FSA's Practitioner Panel or Consumer Panel. There is a need for regular dialogue between the PRA and its external stakeholders. The question is whether this should be institutionalised e.g. through one or more Panels or whether it should be more informal e.g. through meetings with trade associations and their members. My own preference would be for formalised informality i.e. for there to be regular and consistent arrangements with bodies such as the BBA and the Association of British Insurers – and their members – but that these would not necessarily need to be underpinned by statutory provisions. It would be important, however, to ensure that the new arrangements do not inadvertently preclude some arrangements. For example, FSMA made it difficult for the FSA to endorse or support industry guidance of which they approved.

10. **The Government welcomes respondents' views on:**

    Whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and the FPC;

    Whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which;

    Whether, specifically, the requirement to have regard to potential adverse impacts on innovation or competitiveness of the UK financial services sector of regulatory action should be retained; and

    Whether there are any additional broader public interest considerations to which the CPMA should have regard.

    Answer to Question 4 applies to this question.

11. **Are the accountability mechanisms proposed for the CPMA appropriate and sufficient for its role as an independent conduct regulator?**

    Yes.

12. **The Government welcomes views on the role and membership of the three proposed statutory panels for the CPMA.**

    I support the proposal to put the Small Business Practitioner Panel on a statutory footing.

13. **The Government welcomes views on the proposed funding arrangements, in particular, the proposal that the CPMA will be the fee- and levy-collecting body for all regulatory authorities and associated bodies.**

    The proposed fee arrangements and the levy-collection arrangements appear appropriate. In particular the CPMA is the natural candidate to collect the fees on behalf of all bodies. One concern, however, is that the creation of additional institutions such as the PRA and CPMA will lead, overall, to an increase in the amounts levied and the overall cost of regulation to the financial services industry – both initially and increasingly over time.

14. **The Government welcomes views on the proposed alternative options for operating models for the FSCS.**

    The existing compensation scheme arrangements have, since their inception, created concerns within the financial services sector about the extent of cross-subsidy. Even if alternative arrangements are put in place there could still be some degree of cross-subsidy between entities. On balance it would, however, seem to be preferable to separate the compensation schemes but have them administered by one common body – the FSCS – with a view to minimising administration costs. This approach would also mean that it would be simpler to map European laws relating to compensation schemes to the particular scheme to which they relate.

15. **The Government welcomes views on the proposed division of responsibilities for markets and infrastructure regulation.**

It is important that the Markets Division of the CPMA should be a strong and well resourced part of the CPMA. This will be important (1) in order to ensure that the CPMA is not too heavily dominated by purely retail conduct considerations (2) to ensure that wholesale markets are well-understood and well-regulated and (3) to ensure that the CPMA has a strong and influential voice in European policy decisions. Reasons (2) and (3) are also reasons why the UKLA should be part of the Markets Division and should not be split out into a separate body together with FRC. Primary and secondary equities markets should be regulated out of the same body – which is the approach taken by all other countries in Europe. Moreover, the Markets Division of CPMA is to be the spokesperson in Europe on primary and secondary markets at CESR and its successor – so it makes sense that they should be responsible not just for secondary markets but also for listing.

16. **The Government welcomes views on the possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses**

The proposed division of responsibilities appears sensible. Supervision of exchanges should definitely be within the Markets Division of CPMA as there is a significant overlap with issues relating to the firms who trade on these exchanges. The Bank of England has always been responsible for payment systems because of their systemic implications. Similar systemic implications exist for clearing houses and, consequently, it appears sensible to give responsibility for them to the Bank of England.

17. **The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.**

For the reasons given in answer to question 15 the UKLA should not be merged with the FRC. The UKLA's overlaps and obligations sit more appropriately with CPMA.

18. **The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.**

Moving aspects of financial market regulation into a companies regulator is likely to make the regulation of those aspects less, rather than more, effective – particularly if this also involves transferring departmental responsibility to BIS since BIS, while having expertise in company law, has limited knowledge and experience with regard to financial markets.

No answer is provided to questions 19 to 21.

25 August 2010

A RESPONSE

This submission relates only to the retail section of Financial Regulation as outlined in the Discussion Document A new approach to financial regulation: judgement, focus and stability.

Introduction

One has to assume that the title of the document "A New Approach" is meant to be ironic, since I can find no originality in the discussion document at all. It's strictly a case of more of the same, but with a slightly different cover. Indeed most of the thinking is based around the FMSA 2000 and its development under the FSA, which could account for the reference to stability.

After 25 years of regulations, 10 of which were under the FSA, we suffered a near catastrophic financial collapse, so I suspect that this type of stability is suspect.

During the course of the the last 10 years we have had more financial problems than in any other similar time period in the last 200 years. It is arguable that the Regulatory System in place was a strong factor in the severity of the collapse because it provide artificial underpins that created artificial confidence in the strength of the market.

Does that not trigger any sense of doubt about the current process of ritualistic regulation?

The analogy that initially springs to mind is that of King Cnut trying to control water. The financial markets are probably even more fluid than water. Trying to erect barriers is more likely to create a damming situation, with the consequence that when, not if, the barriers are by-passed the result is disaster.

I would not argue against regulation, but I would question whether the type of regulation currently under consideration has any other effect that providing jobs for people. It has certainly not created a healthy financial industry.

I would submit that the retail sector of that industry serves the rich very well, the middle class reasonably well, and the poor not at all. Why? Because the sheer cost, in all its forms, of regulation, as currently structured, makes it an economic impossibility to offer services across the board. This was not the case when I came into the finance industry 40 years ago. It may have had its weaknesses, but it did operate at all levels of the market, and there were relatively few scandals.

Competition and innovation were strong.

An Incorrect Perception

Implicit in the consultation document is an assumption that many parts of the retail financial system are seriously defective.

It is not, was not, and never will be without fault. That is a fact of life. We have a civilization that is over 5,000 old, and we still need policemen on the street. And if we are to believe the media things are worse now than they have ever been - so have the policemen have failed, and need replacing? I think a better answer is that the media need stories to sell, the police do a reason job, and the morality of Society has changed little.

We used to believe that deportation or hanging would be deterrent enough to stop crime. It never did. But that does not stop the FSA thinking along similar lines.

So let's look at regulation using a more realistic approach.

To use an old proverb, a door lock is to keep honest people honest. In crude terms, 90% of a population will be law abiding, 5% will be incorrigibly deviant, and 5% will sway. The lock is to persuade that 5% to go with the 90%. The deviant 5% will never be deterred by locks, and need to be treated differently.

The FSA act on the basis that 100% of the retail market is incorrigibly deviant, and that is not cost effective.

Is there any evidence that the deviancy rate within the financial industry is seriously out of line with deviancy rates in similar industries. If it isn't then whatever regulatory system you put in place will appear to fail if it is given the wrong brief - even if the industry, in the main, runs well.

I would suggest that the available evidence actually points towards a reasonably well run retail sector. The deviancy rate is remarkably small, especially in an industry that deals with significant temptation. There are things that can be done better, but that will always be the case.

Although the level of real information is remarkably low the statistics coming out of the FOS and the FSA indicate a deviancy level well below 1% of transactions. Whilst this can amount to a lot of money, it does not suggest endemic problems. A large part of the statistics also point to the majority of the complaints being in particular areas of business, which can be addressed specifically.

Without being complacent, the information available does not suggest massive problems, contrary to the impression that the FSA like to portray.

A consequence of this mis-portrayal by the FSA is a fall off in consumer confidence. If there is a motorway or aircraft crash, there will be statement put out reminding people that these are still safe ways to travel. If the statistics mentioned above are reasonable it may be more beneficial for the FSA to remind people that 99% of financial transactions are quite satisfactory. But, of course, that would undermine the rational for further growth in that institution.

Enforcement

Outright fraud, such as that committed by Mr Madoff, has been with us for centuries. Obviously there should be laws covering that, but it is not as clear whether that should be an area for the Financial Regulator.

Just as you have identified a tension between macro and micro management in the financial sector, so I believe there is a tension between Regulation and Enforcement.

Firstly the two mindsets are entirely different. The problem is that the right/wrong mentality of the enforcement section becomes part of the regulatory process in which concepts of right and wrong are restricting, in that changes in the market can change perceptions overnight. Regulation needs a far more flexible viewpoint.

Secondly, and perhaps more importantly, the current enforcement process by the FSA stands outside the Common and Statute Law in this country. In many cases it is quite arbitrary, and not subject to proper, second line scrutiny. In practice it is tantamount to the police force being able to convict and sentence. As we have seen in the past the police force is not perfect in its judgement, even when it has to prove its case before an impartial authority. Is the FSA likely to be an exemption?

The FSA has just been given additional powers to force companies to behave in a manner acceptable to the FSA. There appear to be no controlling aspects to this. In other words we have to accept that the FSA are absolutely right in all their judgements, they are infallible. Given their record over the last10 years this is not a good assumption. Even Lord Turner and Mr Sants have acknowledged mistakes. The process is becoming remarkably similar to Fundamentalist Clergy who wish to control every aspect of their followers life.

Therefore Enforcement should be handled by an independent agency.

Revenue Collection

It seems very odd to give the revenue raising authority to the very people who run the industry.

It’s a little like saying to judges that they will get a bonus for every person they fine. There would be four consequences:-

1) the number of people sentence to imprisonment would fall;

2) the number of people fined would increase;

3) the number of people found guilty would increase, and

4) the Judges would be very wealthy.

In many ways that it what is happening with the FSA at the present. They are creating more and more regulations in order that they can legitimately fine more people so they can create a bigger empire. (As an aside I would also suggest that the regulation they create is specifically designed to increase their chances of being able to find people guilty, in order to be able to demonstrate they are doing their job. There is little, if any, evidence that the majority of regulations are actually beneficial to the service provided to the consumer. I would suggest that the evidence is actually to the contrary.)

There is no method of analyzing whether those offenses have any practical relevance to running an effective financial industry. Actually, I would content that it doing the exact opposite. The retail finance industry is now significantly less effective than it has ever been because it is more concerned with not inadvertently breaking a rule, than in providing quality service. I have personally seen instances of this.

I would also consider it odd because it creates no sense of effectiveness or efficiency. For example, in a time when the Government is talking about increasing efficiency in order to reduce expenditure by 25%, the FSA are talking about raising expenditure by the same amount.

Given their recent failures this appears to be rewarding failure. Hopefully there will be a review committee of some form to continuously monitor the cost effectiveness of the new Authority, and that it is done with clarity and openness.

Checks & Balances

It is bizarre that the nation that inadvertently created the concept of checks & balances in Government have proposed a structure that has only nominal controls.

There are committees associated with the new organisation, but just because you hear someone does not mean you have to listen to or take any notice of that person. Indeed the process of avid hearing can be used to disguise total practical indifference to the opinions expressed.

The FSA is not answerable to Parliament (yes, legislation can be enacted to change things, but that is not being answerable); the FSA is not even answerable to the Treasury, its nominal masters.

The nearest the FSA comes to being answerable to any authority is the Office of Fair Trading, in case there are questions of trade distortion arising from actions of the FSA. But there has been no reference on this point, notwithstanding the dramatic decrease in insurance companies; in the concentration of advisory services at the high end of the market (again a bizarre consequence of FSA actions - in practice it spends a lot of its retail resources protecting the rich!); or in the charging structures of fund managers (the FSA imply that commissions are distorting - but not if you run an investment fund?).

The regulation introduced by the FSA has created enormous market distortions, not the least of which is that consumers no longer understand the status of their adviser, or what it may imply. RDR will exacerbate the position to the level of total incomprehensibility. But no-one it going to change that, notwithstanding that there is not one shred of evidence that any part of the change will create any benefit to consumers. The majority of applicable research either points in the opposite direction, or, in the main, suggests that the changes are neutral. Not bad for a process that will cost millions.

There is no body that can impartially view these effects and require changes in FSA direction when necessary. Most people refine their ideas through discussion and debate. The FSA is not required to discuss or debate. Certainly the debate over RDR has changed the initial Review so little it will be implemented pretty much as originally presented. That there is not one sustainable fact, or any method of measuring/quantifying the “achievement” of the RDR , appears to mean nothing.

There must be such a controlling facility alongside the new Authority. It might just generate the CPMA a little respect, something the FSA has signally failed to do in the retail market.

The market changes so fast, and Regulators only react to what has been, not what is to come, so it is imperative that a body of authority stands alongside the new Authority to ensure it thinks through what it is doing.

Without that safeguard history demonstrates that catastrophes will happen.

A Flawed Process

A fundamental problem with the current regulatory process is that it is process based. The discussion document goes through the process requirements as though process were the solution to every problem. The FSA handbook is 3,000 pages thick, and based on history. It even manages to specify the font sizes to be used in documents. It is process personified.

When the FSA started the comment was made that the Authority would move away from tick box regulation of the PIA; when London Turner was appointed 10 years later he again made the comment that the FSA would move away from tick box regulation. So nothing has changed in 10 years. Does that not speak volumes about the current management - who will probably stay in place for the new Authority.

The FSA have a process mentality - if all the boxes are ticked then the job is well done. And they can monitor the process easily.

Some years ago I heard, on a number of occasions the comment that if an Adviser were following FSA rules it would be impossible to provide Best Advice. I came across a number of occasions where this proved to be the case.

Ticking boxes does not provide good advice for clients. It can just as easily hide poor advice.

The FSA have a penchant for copious paperwork. Someone once said “A specification that will not fit on one page of 8.5x11 inch paper cannot be understood.” There is research that demonstrates that people will readily read short documents but not long. Yet the result of FSA regulation is to produce overlong and complex documents that clients do not read.   I have seen Key Feature documents 30 and 40 pages long, filled with dense type - does any one really believe they do anything other than denude forests.

Yet your discussion document promises more of the same. This is not beneficial for the consumer.

When Milton Friedman suggested that inflation could be controlled by the simple expedient of changing interest rates, he create a revolution in simple management of the economy. It may not be perfect, but it is clear and simple.

I would tentatively suggest that a similar change in thought patterns should be required by the new Authority. Competition is more likely to create a better retail environment, and that is more likely to arise through lower costs and a good deal less red tape. The current level of control is positively reducing competition and innovation. In some ways the FSA is now having to act like the Monopolies Commission because competition has been reduced so much. Genuine innovation is now exceedingly rare.

In 25 years the nature of the market has changed dramatically; even in the last 10 years there have been enormous changes in the way that Society operates. None of this is reflected in the current rule book, or thinking, of the FSA.

It is quite possible that a contributory factor to the financial crisis was that the FSA’s detail numbing approach blinded them to the wider picture - they couldn’t see the wood for the trees.

Consequently, I would hope to see a different emphasis for the new authority, concentrating more on the overview, than the specifics. Let Professional Indemnity Insurance cope with the detail. Let the CPMA lay down clear guidelines, insist on PII and let the Insurers ensure that rules are followed, or no payouts. Having worked with Accountants for a number of years I am quite aware of the power that the PI Insure holds in maintaining quality standards. Hit people were it hurts, in their pockets. It does concentrate the mind, and positively rewards good habits, a factor that is currently absent from regulation.

As Prof Gower put in his original report “no system can perform the impossible task of protecting fools from their own folly”. If the new Authority moves away from the impossible to the manageable the consumer may be better served, and at significantly less cost. On this point do not just look at the costs of the FSA or the proposed CPMA, but at the compliance departments within every financial institution. This add layers of cost to everything. That the consumer will pay.

Whilst there are problem areas in the retail sector, it is not the disaster area that many would like to consider it. Heavy handed regulation has had a greater negative than positive effect. Consumers should be encouraged to use a relatively effective sector. People will not use financial services if the only news is bad news.

If the CPMA continues in the negative vein of the FSA most problems will be solved - because there will be no practical retail market remaining, other than that provided by the Government. Nationalizing the retail finance market, by default is not likely to sit well on the Curriculum Vitae of the first Conservative Government for 15 years.

Glen McKeown

Dear Sirs

In response to your consultation document please note:

We are a small insurance broker, giving advice and selling insurance policies mainly to SME's.

The amount of the FSCS levy we are required to pay, has rocketed, due primarily to the latest mis-selling scandal, in the area of Payment Protection Insurance, (PPI).

We have been established 17 years, and have never sold a single PPI policy.

The funds formed from the FSCS levy, should be specific to the risks associated with the firms, that produce the levy and transact that class of business.

It cannot be right and is certainly neither sustainable or equitable, to expect that; firms who have never been involved with selling or providing advice to consumers on PPI, are then expected to contribute to the fund subsequently needed, to pay compensation to consumers who have been mis-sold this category of product.

It is very simple to segregate and accurately allocate the funds by each class of business, every insurer is required to do this all the time, so that they know for example, the value of their private car or home insurance books of business.

The mechanism already exists, it is tried and tested, simple and fair.

For example; if we, as the professional advisers for, and sellers of, a "Shop Package" insurance policy; are held to have been professionally negligent and no other line of compensation to the consumer is available, (assuming for this example, that our mandatory Professional Indemnity, policy and/or own funds/assets, are not able to provide the compensation).

Then the other professional advisers and sellers of "Shop Package" insurance policies should provide the levy funding to compensate.

This approach precisely mirrors the way the insurance industry assesses and funds risk.

When we, as professional advisers, complete our Professional Indemnity forms every year, we are required to indicate on the form, the split of classes of business transacted, with percentage proportions applying to each class of business, e.g. 10% home insurance, 20% private car, 30% shop, 40% business combined, etc.

Insurers then charge us the appropriate Professional Indemnity premium, based on this split of business.

To try and effectively "reinvent the wheel" with a different system to this, seems complex and unnecessary as well as expensive and inaccurate.

The Financial Ombudsman Service and the FSCS can tell you, in a moment; how many and at what cost, were the consumer compensation claims made to them, involving private car insurance, this year.

Insurers can tell you, in a moment; the total value of their private car insurance premiums, this year.

Professional advisers can tell you, in a moment; the value of private car insurance commissions, this year.

All of this is simple, accurate, equitable and efficient - best of all, cheap to administer, since the statistics are so readily available, as the figures are routinely produced within the insurance industry already.

So please, please, please, save money, keep it simple, use the systems already in place and draw compensation funding from the sectors responsible for generating it.

Thanks

Phillip Middleton

Foundation insurance

Blue Band

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First of all I believe that all Insurers who grant an intermediary an agency should be prepared to grant risk transfer.They should also have control over whom Underwriting Agencies use and cascade risk transfer fully down the line.this will mean that all consumers would be protected when using an intermediary and financial regulation could be a lot lighter.

I understood that one of the cornerstones of the FSA remit was a stable market.Insurance is far from a stable market with various Insurers constantly under cutting the market and losing money as they do so to obtain "market share".I believe each year an Insurer on each class of business it operates must show that it is making an underwriting profit.If it makes a loss then it has to show how it is going to rectify it.

Another aspect is comparison sites where intermediaries are quoting 7% or more below the cost to themselves,so making a loss and then charging high credit fees admin charges,legal protection cover etc to recoup.We have found that Mr Average switches off when he hears how much the policy is and doesn't appreciate the full cost of what he is paying.

Treating Customers Fairly should have an avenue of complaint to the Regulator of Insurers where a Broker can complain about Insurer practices and receive a quick response.For example a client has a non fault accident and wants to add a credit hire vehicle to his policy.There is clearly an Insurable Interest as the hire Company make him liable for any damage and he is liable for any injury/damage he causes to other people/property.Because insurers don't think a client should have alternative transport they either refuse cover or say they will only provide cover up to the grouping of his own car.This isn't fair and is not in the interest of the client but it is the Insurer trying to keep him out of an alternative vehicle.There are weekly examples of Insurers high handed attitude and trying to steam roller or rail road clients where the complaints procedures take too long and a speedier independent appeals process is needed together with a fine if Insurers are found guilty that Brokers can appeal to.Clients very often just accept the position as they don't want the bother of complaining so Insurers don't improve.

David Miller.

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Dear Head of Financial and Regulation Strategy

Please find our response to your consultation: *Cm 7874 A new approach to financial regulation: judgement, focus and stability*

I am responding on behalf of an organisation: Morton Michel a medium sized, family insurance intermediary in Croydon that employs 30+ people and specialises in providing insurance products to the childcare sector.

Not all of the consultation questions are applicable to ourselves and we have therefore responded to a selection of the points.

Consumer protection and markets authority (CPMA)

10 The Government welcomes respondents' views on:

- whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and FPC;

  We would like to see the CPMA have regard to the financial stability of firms and as much as possible we would like to deal with the CPMA as a 'one-stop shop' in much the same way as we currently interact with FSA.

- whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which;

  We would like to see the CPMA adhere to all the principles for good regulation currently set out in section 2 of FSMA

- whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and

  In this area, our concern is that the CPMA should pursue a proportionate response to regulation – one that is both outcomes focussed and aware of the individual requirements and resources of the company being regulated.

- whether there are any additional broader public interest considerations to which the CPMA should have regard.

  We believe it to be in the public interest to keep the regulatory regime as straightforward and comprehensible as possible as a more complicated regulatory regime will inevitably lead to higher costs for the consumer.

11. Are the accountability mechanisms proposed for the CPMA appropriate and sufficient for its role as an independent conduct regulator?

We would like to see industry figures on the board of the CPMA to ensure that the interests of regulated firms (and particularly the smaller non-relationship managed ones) are taken into account.

13 The Government welcomes views on the proposed funding arrangements, in particular, the proposal that the CPMA will be the fee- and levy-collecting body
for all regulatory authorities and associated bodies.

We believe the CPMA should continue to be a fee and levy collecting body for all regulatory authorities. We would expect fees to be broadly comparable to or lower than the levels at which they are now. We have for a number of years paid consistently higher fees, year on year and had no regulatory interaction whatsoever or any return of value by the regulator. We would suggest that *companies that have been subject to regulatory sanction or investigation should be paying higher fees – in much the same way FOS fees are levied by case.*

14 The Government welcomes views on the proposed alternative options for operating models for the FSCS.

We continue to be concerned that, as a medium sized insurance intermediary, we are paying for or being penalised for the failures of other companies in our area in the FSCS fees we are paying, which have gone up dramatically over the last year in our fee-block.

Markets and Infrastructure

16 The Government welcomes views on the possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses.

The FSMA regime could definitely be rationalised and simplified, but we would like to see fewer, not more regulatory bodies.

Other Points

- Ideally we would like our interactions with and reporting to the CPMA to be in a similar format to what we are familiar with currently with FSA as significant alterations will add complexity and cost to our business.
- We would like to see more 'preventative regulation': i.e. industry training and road shows with the emphasis on helping companies to understand their regulatory responsibilities and to avoid problems before they occur.
- As a medium-sized company we would like to be able to obtain straightforward and individualised advice from the CPMA, or FSA's successors, when we need it. Traditionally we have found FSA's contact centre reluctant to offer direct regulatory advice.

We hope these thoughts are of assistance.

Kind regards

Paul

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Response to CM 7874

I have been invited to respond presumably because I have responded to previous related Treasury and FSA Consultations.

Overall I think the proposals are a big step in the right direction. My response relates to general principles enunciated previously.

1) The insurer of liquidity and financial stability has the incentive to protect the insurance fund against abuse (deal with moral hazard). Hence it is correct that the Bank (of England) should be responsible for financial stability and have the necessary additional tools (beyond short term interest rate setting), to engage in asset price inflation offsetting policy.

   a) In order to protect the taxpayers, the Bank should also oversee the bank deposit insurance scheme (separated from other financial services compensation schemes). AND the bank DI Scheme should be prefunded with risk-related premia in order to 'tax' bank risk taking.

   b) Monetary policy has effectively moved beyond short (nominal) interest rate setting to long term interest rate setting and yield curve considerations. Inflation targeting may need to be downgraded.

2) An attempt should be made (I am working on a paper) to replicate the US FDIC approach (risk related DI and prompt resolution) toward small and medium sized banks. If 'living wills' and 'special resolution regimes' for TBTF (in terms of size/complexity etc) are not

really credible (and I doubt they are) then TBTF banks must be broken up.

3) Any break up of TBTF banks should follow a thorough Competition Commission review (covering alleged economics of scale and scope). Note US banks (relative to the US market) are much smaller than UK banks. But if UK banks were restricted to (say) 10% of the market (as ostensibly in the US) they would be relatively small internationally. What is the relevant market for UK banks (UK or EU?).

4) In other papers I have argued (as have others) that retail banking is essentially a utility and should be regulated as such (and the utility regulator should be funded in the same way as other utility regulators). To my mind the retail finance (utility) regulator (RFR) would regulate banking and insurance services provided to consumers and SMEs, including the payments system (Cruickshank Report) and credits (taking over from the OFT). The Competition Commission and OFT would then be released from almost continuous post Cruickshank investigation of retail banking activities, but would liaise with the RFR as they do with other utility regulators.

5) The FSA would be left with wholesale and investments market regulation and would fund itself by charging fees to participants. To have authority it would also need to be able to prosecute fraud (using the re-invigorated SEC in the US as a model). It could be argued that the New York Attorney General has helped keep the SEC on its toes, however, and so perhaps a division of the Fraud Squad could play a similar role.

6) CFEB is a good idea and it should be funded by a levy on financial firms, although some thought might be given to passing the financial education role to the proposed RFR (utility) regulator.

7) The Regulators should have no role to promote or protect at 'the City', as the FSA had (and the Bank had before it). The focus should be on effective regulation to promote financial stability and protect depositors and taxpayers. The relevant government department, the Corporation of London and the Mayor of London can promote the City and fight its corner if they so wish as long as regulatory independence is assured (idealistic I know!).

Andy Mullineux
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NAPF Response

HM Treasury Consultation 'A new approach to financial regulation'

1 About NAPF

The NAPF is the leading voice of workplace pensions in the UK. We speak for 1,200 pension schemes with some 15 million members and assets of around £800 billion. NAPF members also include over 400 businesses providing essential services to the pensions sector. UK pension schemes directly own around 13 per cent of the UK equity market, a figure which is considerably increased once indirect holdings through insurance policies and unitised products are taken into account. They are also major investors in international equities, in gilts and in corporate bonds.

As major institutional investors dedicated to the provision of occupational pensions for millions of workers and pensioners, our pension scheme members have a particular interest in the integrity and efficient functioning of the capital markets. We are grateful for the opportunity to reply to the Treasury's consultation on its proposed approach to financial regulation.

2 Summary

Our response is restricted to Questions 17 and 18. We argue that primary and secondary market regulation must be undertaken within the same regulator. In the model proposed in the consultation document this would be the Consumer Protection and Markets Authority (CPMA).

3 NAPF response

3.1 *Question 17. The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under the BIS.*

3.1.1 Primary markets regulation is essentially a matter of financial and securities regulation rather than of company law. Little more than one twentieth of the 20,000 securities admitted to the Official List are equity securities issued by UK companies, the bulk of the remainder being UK and international corporate bonds and sovereign debt. The UK Listing Authority (UKLA), as the UK's primary markets regulator, thus sits more logically with financial markets regulation than with company law. In the model proposed in the Treasury's consultation document, this would be the markets division of the Consumer Protection and Markets Authority (CPMA).

3.1.2 Practical considerations also point to the need for UKLA to be considered a part of financial markets regulation:

i issues relating to market conduct, particularly market abuse, cut across primary and secondary markets. Primary and secondary markets regulation thus needs to be closely integrated. It is difficult to see how this can be done effectively if it is not only the responsibility of different regulators but subject to a different legislative regime.

ii Operationally, similar skills are required for primary and secondary markets regulation. In particular, both require real-time monitoring and response. This is very different from the work of the Financial Reporting Council (FRC) and calls for a different approach and culture which will not mesh easily within the same organisation. Indeed, one of the main reasons behind the government's proposed new regulatory architecture was the difficulty of combining the cultures required for financial supervision and conduct of business regulation within the Financial Services Authority.

iii securities and markets regulation is very largely driven by EU legislation. The UK accounts for 60-80 per cent of EU securities trading and is a truly international centre for new issuance. Yet it will have only seat on the Board of the European Securities and Markets Authority (ESMA), which will be held by the CPMA. It is essential that the interests of both the UK's primary and secondary markets be directly represented in ESMA.

3.2 *Question 18. The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.*

We cannot think of other aspects of financial regulation that could be made effective by being moved into the proposed companies regulator. We would however like to put on record our belief in the effectiveness of the Panel on Takeovers and Mergers. We believe that its current structure enables it to operate with a speed and authority that would be difficult to replicate in another way.

October 2010

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Steve C B Lucas
Finance Director

12 October 2010

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Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London SW1A 2HQ

Dear Sir or Madam,

I would like to respond on behalf of National Grid to specific questions in the consultation document: ***A new approach to financial regulation*** (Cm 7874).

17. ***The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.***

We do not support this proposal for a number of reasons:

- There is no logic in having separate regulators (CPMA and UKLA/FRC) which are independent of each other for the primary and secondary markets in a security.
- It must be possible to achieve synergies, and hence a lower cost, from having a single body regulate these activities that occur in the same market.
- The role of the UKLA is to regulate the issuance of and the continuing market in securities, not companies per se. In addition, only a tiny proportion of these securities are equities issued by UK companies.
- If the UKLA were to be part of a companies regulator then a share issue would be regulated by two separate regulators: the UKLA would regulate (inter alia) the prospectus with the CPMA regulating (inter alia) the sponsor and the operation of the Greenshoe.
- It is vital that the UKLA has a strong voice in Europe. If it is separated from CPMA, which will be the voting member of ESMA, then the only way that the UKLA can influence the direction of European regulation is via CPMA.

18. ***The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.***

We can not envisage the need to move other parts of financial market regulation in to a companies regulator. There does not seem to be a need for a companies regulator – a combination of existing legislation and regulation (including the FRC and the Takeover Panel) already provides a robust framework. To place responsibility for this framework in a new regulatory body runs the risk of confusing who has primacy, for example in company law.

I hope you find these comments useful. If you have any queries, please do not hesitate to contact me.

Yours faithfully,

Steve Lucas

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18 October 2010

Dear Sirs

NATIONWIDE BUILDING SOCIETY'S RESPONSE TO 'A NEW APPROACH TO FINANCIAL REGULATION: JUDGEMENT, FOCUS AND STABILITY'

Nationwide Building Society welcomes the opportunity to respond to the Treasury's consultation on a new approach to financial regulation. We are the UK's third largest mortgage lender and savings provider and as the UK's largest building society we are different from many of our competitors. Unlike banks that are run for shareholder benefit and to maximise profit, we are owned by and run for the benefit of our 15 million members. We are a member of the Building Societies Association and support its response to the consultation.

We recognise the need for reform regarding the regulatory regime governing financial services. We understand the Government's rationale for the creation of the Financial Policy Committee (FPC), Prudential Regulatory Authority (PRA) and the Consumer Protection and Markets Authority (CPMA) and, broadly, believe that the proposed new system with its focus on ensuring financial stability is the right approach.

However, there are a number of issues that we wish to highlight as priorities for the Government and the new regulators to address as the new structure is developed and begins its work in earnest:

- **There should be strong coordination and alignment of objectives between the new regulators.** Given the nature of its business, Nationwide will be subject to both the PRA and the CPMA. Therefore, the new regulators must ensure they are coordinated and aligned in terms of their statutory objectives, rule-making and approach to oversight so that the financial services industry has one consistent standard to follow. It is evident that there are areas where prudential matters overlap with conduct risk and consumer protection, or where the distinction is not clear, as stated recently by Lord Turner. A close working relationship between the PRA and CPMA is vital, despite the fact that this has been difficult to achieve even when under the same FSA umbrella. The regulators should be legally separate and, in practice, independent from the Government with the power to operate without political obstruction.

- **Supporting diversity should be an objective of the FPC, PRA and CPMA.** The more diversified a financial system in terms of ownership, governance structures and portfolio make-up, the better able it is to weather the strains produced by the normal business cycle. There is a lack of diversity within retail financial services, which has had a negative impact on competition and choice for consumers. The Coalition has recognised the need to address this issue through its 'Programme for Government' commitment to "foster diversity in financial services, promote mutuals and create a more competitive banking industry". It will be vital that this is reinforced through the remits of all three new regulatory authorities, together with a requirement for them to publish an annual 'diversity report' on the sector.

- **In this vein, the new regulatory authorities should ensure their rule-making and enforcement has a proportionate impact on institutions within the sector operating different business models than those of the plc banks.** Nationwide and, in general, the wider building society sector (with a number of obvious exceptions) have emerged from the financial crisis in relatively good shape, requiring little direct taxpayer support. To support a sector in which diversity can thrive, the regulators should ensure the impact on firms is proportionate to risks they represent to the stability of the sector and that their approach is suitable for building societies, as well as plcs, which have a fundamentally different, and inherently lower risk, business model. Regulation must recognise and be tailored to encourage a diversity of models, not solely to the default setting of the plcs. The FSA's current approach to the development of a new wholesale capital instrument for building societies that meets their requirements, is suitably attractive to investors and does not compromise the principles of mutuality is a case in point, as is HM Treasury's rationale for applying the forthcoming bank levy to building societies.

- **The CPMA should focus on its role as a regulator and not act as a 'consumer champion'.** The CPMA should be responsible for ensuring balance, clarity and fairness within the market, allowing consumers to make sound decisions. It should protect consumers in the sense that its rules should ensure the market is characterised by these factors through acting impartially. It is the role of consumer groups to act as 'champions', with recourse to the Financial Ombudsman Service, not the regulator, which would create a conflict of interest. It will also be important that the CPMA balances the responsibilities of lenders and borrowers, consumer protection and choice, and the need for simple products and innovation, to ensure that productivity and growth in the sector is not stifled, potentially creating greater cost for consumers.

- **The Bank of England should be subject to a strong accountability and transparency framework.** The Bank will have significant powers, with regard to macro-prudential policy, interest rate setting, individual firm supervision and its membership of the FPC and PRA. Ensuring the Bank does not become excessively powerful will be important and the consultation document recognises the need for "robust mechanisms that ensure transparency and a high degree of accountability of the central bank's actions in safeguarding financial stability". Whilst ensuring that the FPC is able to focus on its financial stability objective, the Government should consider strengthening these mechanisms through exploring whether all the FSA's accountability provisions should be applicable to the FPC.

- **Regulators should continue to be obliged to consult with industry over rule changes.** The consultation document implies that the Government would be open to the possibility of watering down the obligations of the regulator(s) to consult with industry. HM Treasury states that it wants to avoid a situation where the rule-making process becomes overly bureaucratic. We would like to ensure the revised architecture continues to include a robust statutory mechanism requiring interaction with industry. This would include – and should not be limited to – pre-consultation with industry expert groups (e.g. Credit Risk Standing Group) and performing considered cost benefit analyses to gauge both whether proposed rules will actually address the risks identified and that the costs of implementation are proportionate to the behaviour they seek to control. We would go further and request that regulators consult jointly wherever possible.

In addition to these important issues, we have also responded, where appropriate, to the specific questions raised in the consultation document. Please find these attached.

My colleagues and I would be happy to discuss any aspect of our response with you.

Yours faithfully,

Graham Beale

Graham Beale
Chief Executive

Responses to the consultation questions

The Bank of England and the Financial Policy Committee

Q1: Should the FPC have a single, clear, unconstrained objective relating to financial stability and its macro-prudential role, or should its objective be supplemented with secondary factors?

It is right that the primary objective of the FPC should be to deliver financial stability. This should ensure the problems arising from the FSA's numerous statutory objectives are not repeated under the new regulatory structure. However, we believe that this primary objective should be supplemented by secondary factors that do not undermine the FPC's pursuit of financial stability.

We believe that it is difficult to identify 'bubbles' and therefore set appropriate restrictions on areas such as credit to avoid financial instability. Nothing could illustrate this better than banks being encouraged to lend at high LTVs in a period of a falling House Price Index and to borrowers who, on average, are likely to face increasing financial constraints. Whilst this may make macroeconomic sense, it ignores the impact on individuals. On balance, however, it is clear following the financial crisis, that maintaining macro stability should have primacy.

Q2: If you support the idea of secondary factors, what types of factors should be applied to the FPC?

The secondary factors that should be applied are:
- Ensuring it has regard to the objectives of the PRA and the CPMA to provide for a consistent approach to regulation and manage effectively any overlap in responsibilities.
- Ensuring the continuing competitiveness of the UK financial services industry. The FPC should take into account the cumulative impact of new and existing regulation on the competitiveness and profitability of firms, including mutuals.
- Ensuring that any restriction or action is proportionate to the expected benefits.
- Ensuring it takes into account diversity of institutions within the financial services sector.

Focusing on this last point, a plurality of different business models in any sector is important as it offers different ways of combining economic, social and political priorities, thereby maximising their potential benefit. The more diversified a financial system in terms of ownership, governance structures and portfolio make-up, the better able it is to weather the strains produced by the normal business cycle.

The recovering UK economy needs a more 'socially useful' retail financial services industry. The long-term focus of the mutual model provides a useful and necessary counter-balance to the short-term pressures of the public companies.

There is a lack of diversity within retail financial services, which has had a negative impact on competition and choice for consumers. This is not only true amongst the large national banks that dominate the marketplace but also between banks and mutuals. Whilst new entrants to the market should be encouraged and efforts made to facilitate this, the experience of one new entrant, which has taken approximately two years to open just one branch, clearly proves that banking is an extremely complex business and requires time and experience to build a meaningful presence. In the short and medium term, new entrants will have minimal impact on competition. Supporting the 'challenger' brands already operating successfully on the high street is necessary to achieving the goal of a more competitive and diverse sector.

We believe that the FPC, working with the PRA and CPMA, should be required to publish an annual diversity report on the sector, ensuring that their actions promote, rather than inhibit, a range of business models operating within financial services.

Q3: How should these factors be formulated in legislation – for example, as a list of 'have regards' as is currently the case in the FSMA 2000, or as a set of secondary statutory objectives which the FPC must balance?

Given the importance of these secondary factors, we believe that these factors should be established as a set of secondary statutory objectives. Requiring these factors as secondary statutory objectives, rather than factors to 'have regard' to, would give them greater legal force. We do not believe that the pursuit of these factors would compromise the primary financial stability objective of the FPC.

They should also be consistent with those of the PRA and the CPMA to ensure the alignment of their approach and a single view from the regulators. The three elements of the future regulators' roles must be co-ordinated to avoid duplication and any increase in requests for information from individual firms, but still ensuring clarity of responsibility where overlaps occur.

It will be vital that the Bank of England should be subject to a strong accountability and transparency framework. The Bank will have significant powers, with regard to macro-prudential policy, interest rate setting, individual firm supervision and its membership of the FPC and PRA. Ensuring the Bank does not become excessively powerful will be important and the consultation document recognises the need for "robust mechanisms that ensure transparency and a high degree of accountability of the central bank's actions in safeguarding financial stability". Whilst ensuring that the FPC is able to focus on its financial stability objective, the Government should consider strengthening these mechanisms through exploring whether all the FSA's accountability provisions should be applicable to the FPC.

The Prudential Regulatory Authority

Q4: The Government welcomes views on:

- ***whether the PRA should have regard to the primary objectives of the CPMA and FPC.***

It is important that all three regulatory bodies have statutory objectives to have regard to the objectives of each other to ensure a consistent and coordinated approach to regulation both for the industry and for the consumer.

- ***whether some or all of the principles for good regulation currently set out in section 2 of FSMA, particularly those relating to good regulatory practice, should be retained for the PRA.***

We believe that all of the FSMA principles for good regulation should be retained for the PRA. We do not believe that they should necessarily hinder the achievement of the PRA's primary objective "to promote the stable and prudent operation of the financial system through the effective regulation of financial firms, in a way which minimises the disruption caused by any firms which do fail".

The principles should ensure that a standard benchmark on proposed regulation is applied by the PRA when making rules as is currently the case with the FSA.

- ***whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained.***

We understand the Government's rationale for considering whether this requirement should be applicable to the PRA, given the argument that one of the reasons for regulatory failure was excessive concern for competitiveness and innovation, to the detriment of financial stability.

However, both the requirement to have regard to potential adverse impacts on innovation and the competitiveness of the UK financial services sector must be retained to allow the UK's financial institutions to bring new products to market. A super equivalent, even protectionist, UK regime must not be allowed to develop.

- ***whether there are any additional broader public interest considerations to which the PRA should have regard.***

Given the potential increase in capital to be held and also the capital held against specific types of lending, there should be additional considerations of barriers to entry, diversity in financial services provision and consumers' access to financial services. Ultimately, the result may be the consumer paying more or having restricted access to areas of financial services.

Q5: Is the model proposed in paragraph 3.16 – with each authority responsible for all decisions within their remit subject to financial stability considerations – appropriate, or would an integrated model (for example, giving one authority responsibility for authorisation and removal of permissions) be preferable?

An integrated model for granting and amending permissions would be preferable. As preserving financial stability is the basis of the regulatory reform, it would be appropriate to have the PRA act as the body for granting permissions. This would ensure, at outset, that all new financial services firms have adequate financial resources. The on-going supervision of retail intermediaries should be the responsibility of the CPMA.

Q6: Is the approach outlined in paragraph 3.17 to 3.23 for transfer of regulatory functions and rule making sufficient to enable the PRA to take a more risk-based, judgement-focussed approach to supervision?

The key functions of the PRA as described in paragraph 3.20 appear appropriate. However, the approach of any regulator to its rule-making must continue to be subject to statutory process including industry consultation and a cost benefit analysis to ensure the rules address the risks and the costs of implementation are proportionate to those risks.

As noted in paragraph 3.18, all rule-making must be co-ordinated between the authorities to ensure there is clarity and consistency in the rules so, whilst there may be two authorities, the rules should reflect a common view.

Q7: Are safeguards on the PRA's rule-making function required?

Yes, the current FSMA safeguards should remain in place for the PRA.

Q8: If safeguards are required, how should the current FSMA safeguards be streamlined?

We believe that the current FSMA safeguards remain appropriate. They should be maintained and not streamlined for the reasons set out in the first paragraph in answer to Q6 above.

Q9: The Government welcomes views on the measures proposed in paragraphs 3.28 to 3.41, which are designed to ensure that the operation of the PRA is transparent, operationally independent and accountable.

The measures proposed are appropriate. However, the PRA's operational independence must not prevent it consulting with the FPC and CPMA to ensure there is alignment and consistency in the regulators' approach.

<u>The Consumer Protection and Markets Authority</u>

Q10: The Government welcomes views on:

- ***whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and FPC.***

The CPMA should have financial stability as one of its objectives, rather than just a 'have regard' to ensure it is aligned with and also supports the PRA and FPC agendas and ensures consistency.

Businesses make decisions with their stability in mind and the regulator should recognise that businesses do consider the implications for their financial stability when making decisions.

Ensuring the CPMA's and PRA's objectives are aligned and their activities are coordinated will be essential in ensuring that both regulators do not seek to address the same issue through their own mechanisms.

With regard to the mortgage market in particular, we retain a strong preference for prudential regulation. Changes to the conduct of business rules should be limited and proportionate given that poor practice emerged from a limited number of outliers within the market. We believe that the FSA is at risk of over-regulating the market and that the current proposals will result, through design and unintended consequences, in a market that is lacking in innovation and where the needs of certain consumer segments are no longer met. Big losers will be the self-employed and the credit impaired, but other groups including first time buyers, self builders and the low cost home ownership market will also find their plans constrained. We believe that the proposals will result in a loss of customer empowerment that will deny many potential borrowers access to the market.

- ***whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which.***

All of the principles of good regulation should be retained, particularly the requirement of 'proportionality'. In our case, as a building society, regulators should ensure that the impact of proposed regulation on certain firms is proportionate to the risks they represent to the stability of the financial sector.

However, we have concerns with the proposed role of the CPMA as a 'consumer champion'. We do not believe it to be appropriate for a conduct of business regulator to also take on this function as it would create a conflict of interest.

The CPMA should be responsible for ensuring balance, clarity and fairness within the market, allowing consumers to make sound decisions. It should protect consumers in the sense that its rules should ensure the market is characterised by these factors through acting impartially. It is the role of consumer groups to act as 'champions' with recourse to the Financial Ombudsman Service, not the regulator.

- ***whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained.***

As described in the response to question 4 consideration of innovation and the competitiveness of the UK financial services industry must be retained.

- ***whether there are any additional broader public interest considerations to which the CPMA should have regard.***

The CPMA should have regard to consumers' access to affordable, simple, understandable products. Preventing innovation will inhibit development of products; excessive regulation will ultimately increase the costs to firms who in turn will have to pass those costs on to consumers through the pricing of the product.

The Government needs to accept that the more responsibility it layers on business the less responsible individual consumers will become. Consumers should be encouraged to take responsibility for their actions and the binding nature of the agreements they enter into.

It will be important, therefore, that the CPMA balances the responsibilities of lenders and borrowers, consumer protection and choice, and the need for simple products and innovation, to ensure that productivity and growth in the sector is not stifled, potentially creating greater cost for consumers.

In addition, as with the FPC and PRA, diversity within financial services should also be a factor which the CPMA takes into account.

Q11: Are the accountability mechanisms proposed for the CPMA appropriate and sufficient for its role as an independent conduct regulator?

The measures outlined in paragraph 4.36 are appropriate. We would, however, question the extent of the CPMA's independence from government given that its governing board is to be appointed by the Treasury with "strong interest" from the Department for Business, Innovation and Skills.

Q12: The Government welcomes views on the role and membership of the three proposed statutory panels for the CPMA.

Given the proposed composition of the CPMA, all mechanisms that provide for external challenge and accountability are vital and would be welcomed. Membership should be representative of all affected parties.

Q13: The Government welcomes views on the proposed funding arrangements, in particular, the proposal that the CPMA will be the fee- and levy-collecting body for all regulatory authorities and associated bodies.

We agree with the proposal that a single authority should be responsible for collecting fees and levy payments. However, it may be more appropriate for the collecting authority to be the Bank of England, possibly via a vehicle that is separate to both the PRA and CPMA. We believe the Bank of England should direct resources to regulatory priorities and ultimately institutions.

We recommend that levies are co-ordinated such that they are raised concurrently and relate to aligned periods of account, streamlining the collection process and avoiding a fragmented process for the receiver.

In our view, fee-setting should have regard not only to the size of the organisation, but also the level of its inherent risk. We would prefer fee calculations to take account of the level of risk as assessed by the PRA and by the CPMA, taking account of the two bodies' respective remits. Where there is any cross-over in the activities of the two bodies, synergies should be explored and reflected in the fee structure, thereby avoiding an organisation effectively paying twice for the same regulatory coverage.

Q14: The Government welcomes views on the proposed alternative options for operating models for the FSCS.

The FSCS should remain the single body for administering compensation scheme. The separation of cross-funding is preferred.

Any future compensation scheme levy must be based on the risk of the entity. Building societies have an inherently lower risk business model than banks and this should be recognised in the funding model for any future scheme.

The Government must also consider the potential impact of proposed changes to the deposit guarantee scheme directive by the European Commission and ensure this is appropriately considered within the new regulatory architecture. Whilst there are still many unknowns, current proposals would have a hugely significant impact on the profitability of the building societies and, therefore, their ability to accumulate capital reserves.

Markets and infrastructure

Q15: The Government welcomes views on the proposed division of responsibilities for markets and infrastructure regulation.

We have no comment to make on this issue.

Q16: The Government welcomes views on the possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses.

We have no comment to make on this issue.

Q17: The Government would welcome views on whether the UKLA should be merged with FRC, as a first step towards creating a companies regulator under BIS.

We do not have any strong views on this issue as we have less interaction with the UKLA than a plc. We can, however, see there could be benefits from a merger with the FRC. This must be explored carefully given the impact this would have on institutions' interaction with the FRC and its various subsidiary bodies.

Q18: The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.

We have no comment to make on this issue.

Crisis management

Q19: Do you have any overall comments on the arrangements for crisis management?

We believe that the new regulatory structure as described – with an emphasis on alignment and coordination of the authorities – together with the tools introduced as a result of the recent financial crisis, should represent a more effective regime to deal with any future crises.

Q20: What further powers of heightened supervision should be made available to the PRA and the CPMA, and in particular would there be advantages to mandatory intervention, as described in paragraph 6.17?

We do not believe that there is a strong case for further powers/tools to be made available in a time of crisis over and above those outlined in the consultation document.

Q21: What are your views about changes that may be required to enhance accountability within the SRR, as described in paragraphs 6.21 to 6.24?

Whilst we understand the point made in the consultation document regarding avoiding a conflict of interest between the Bank of England exercising its new responsibilities in relation to the PRA and its powers in exercising the stabilisation powers under the SRR, there needs to be close co-operation and communication between all regulatory bodies or functions within the new regulatory framework to ensure their respective powers are exercised effectively. Commentary to date has been that the former tripartite structure was ineffective as no one body took the lead – the consultation document makes this argument strongly. The new regulatory regime should ensure that it is clearly visible which body/function is taking the lead.

One way in which the new regulatory framework could be used to enhance the accountability of the SRR would be for Bank of England (both through the PRA and as the lead resolution authority) to be subject to greater reporting obligations on the rationale and explanation of any actions taken under the SRR. Such reports should be made not just to Parliament but also to the public to ensure both the creditors of a failed institution and the industry (which effectively pays for the failures through the FSCS) understand how and why the SRR is being used.

Furthermore, in order to enhance the effectiveness of the SRR, the Bank of England (as the lead resolution authority) should be responsible for leading the formal processes required to assist the failed institution and the transferee of their business(es) with the implementation of the transfer of business(es), as this is, in practice, where many difficulties can arise with the SRR.

Impact assessment

Q22: Annex B contains a preliminary impact assessment for the Government's proposals. As set out in that document, the Government welcomes comments from respondents on the assumptions made about transitional and ongoing costs for all types of firm. In particular, comments are sought from all types and size of deposit-taking, insurance and investment banking firms (including credit unions and friendly societies), and from groups containing such firms.

It is not possible to comment extensively on the impact of the proposals as the regulatory reporting regimes have not been set out in sufficient detail. However, we anticipate that there would be inherent on-going additional costs involved in dealing with two separate regulatory bodies. In addition, there would be one-off costs incurred through changes arising from amended reporting requirements. Costs and a time delay would also be incurred in updating the B2B direct information link which currently exists between the FSA and Nationwide, which historically we have not found to be quick to amend.

nef
economics as if people and the planet mattered

A new approach to financial regulation: judgement, focus and stability

Response by nef (the new economics foundation) to HM Treasury consultation (July 2010)

By Greg Ford and Tony Greenham, 18 October 2010

I Financial Policy Committee (FPC)

1 ***Should the FPC have a single, clear, unconstrained objective relating to financial stability and its macro-prudential role, or should its objective be supplemented with secondary factors?***

The FPC should have secondary factors.

2 ***If you support the idea of secondary factors, what types of factors should be applied to the FPC?***

Secondary factors for the FPC should include:

- promoting the public interest; as a secondary objective to financial stability, the FPC should have a duty to use its long list of macro-prudential tools to promote other public interest goals as determined by the government, to the extent that they do not conflict with the primary objective of financial stability. Examples might include promoting employment or long-term savings, or sector-specific goals such as green investment or control of house price inflation;

- promoting a balanced economy; the government has said it wishes to rebalance the economy so that it is no longer over-dependent on finance. The FPC can help to restore the balance by (i) ensuring that macro policies and regulatory strategy are designed primarily for the productive, rather than the financial economy, and (ii) applying macro-prudential tools on a sectoral basis to achieve and maintain that balance, for example by lowering capital rules or risk weightings against lending in certain sectors or regions and raising it for others (similar to the proposal in paragraph 3.11 for the PRA to have regard for wider factors including consumer and business lending)

Secondary factors for the FPC should NOT include facilitating innovation, the international character of financial services, or maintaining the competitive position of the UK.

3 ***How should these factors be formulated in legislation – for example, as a list of 'have regards' as is currently the case in the Financial Services and Markets Act 2000 (FSMA), or as a set of secondary statutory objectives which the FPC must balance?***

We prefer secondary factors to be implemented as secondary statutory objectives. The "have regard to" formulation would require only consideration, while the statutory approach would require balanced actions and so hold the FPC to a higher standard in delivering its secondary objectives.

Additional comments on the FPC

(i) Governance (paragraphs 2.39-2.45)

The paper proposes to appoint four external FPC members with experience of banking, insurance and investment banking to challenge group-think without conflicts of interest. Given the need for City experience, there is a danger that external members will favour City interests over the public's interest for reasons of personal loyalty and outlook, even if obvious conflicts of interest such as board directorships and financial firm pension pots are absent.

We therefore propose that external members have, in addition to financial experience, an interest in the public good. The restriction on conflicts of interest should be extended to several years before and after their tenure on the FPC. External members should share the same outlook as that proposed for non-executive board members of the CPMA, who are "expected to have the necessary skills and background to bring the viewpoint of all relevant stakeholder groups to the board" (paragraph 4.33). External members with this outlook would help the FPC to deliver the secondary factors outlined above.

(ii) Macro-prudential tools (Box 2.C)

The FPC's tool-box of macro-prudential policies, described in Box 2.C, should be as broad as possible.

Variable risk-weightings should be encouraged as a way for the FPC to challenge the assumptions of ratings agencies. By applying its own risk-weightings on different sectors or asset types, such as real-estate backed securities or private equity leverage loans, the FPC could target asset bubbles and help implement the government's industrial policies. This would create the possibility to influence the lending policies of commercial banks directly according to public policy goals, instead of leaving it to the interaction of ratings agencies and capital adequacy rules, which are not set with such goals in mind (which gave us an oversupply of credit for asset backed securities and undersupply to SMEs).

The FPC should have flexibility to deviate from Basel 3 standards, especially concerning risk-weightings. Should the FPC decide to increase risk weightings against assets perceived as not risky (such as sovereign bonds) in excess of the Basel level, it may need to reduce risk weightings for riskier assets during a transitionary implementation period[1].

Quantitative credit controls and reserve requirements should remain available, since they give regulators more options in a crisis and could facilitate future changes to monetary policy aimed at democratising money creation[2].

We would also like the FPC to have a more formal role in assessing the contribution to financial stability of financial sector taxes including balance sheet levies, financial activities taxes and financial transaction taxes. While fiscal policy is the treasury's remit, the FPC should have a voice to the extent that financial taxes impact stability and the secondary factors in its remit.

II Prudential regulation authority (PRA)

4 ***The Government welcomes respondents' views on:***

4.1 ***whether the PRA should have regard to the primary objectives of the CPMA and FPC;***

Yes, the PRA should have regard to the primary objectives of the FPC: systemic considerations should outweigh the interests of individual firms.

4.2 ***whether some or all of the principles for good regulation currently set out in section 2 of FSMA, particularly those relating to good regulatory practice, should be retained for the PRA;***

We would retain only facilitating competition.

4.3 ***whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained;***

No. These requirements allowed systemically dangerous innovations to go unchallenged and required the regulator to promote the interests of firms it was policing. These factors should be dropped.

Arguments for their re-introduction, including those based on the contribution of finance to the UK economy, should be seen in the context of the bail-out and finance-led recession. As regulators including the Bank of England have noted, unilateral regulation does not need to be a disaster for the UK's competitiveness as it would improve long-term stability and encourage higher standards from overseas regulators.

4.4 ***whether there are any additional broader public interest considerations to which the PRA should have regard.***

A new objective of "functionally effective markets" should be added to the regulatory objectives in FMSA section 2(2).

The PRA could then hold financial institutions accountable for delivering their core economic purpose, such as maturity transformation, capital formation or whatever it is. As Lord Turner said, some financial activity contributes little social value, but many activities impose social costs through excess intermediation and systemic risk. By putting the idea of "purpose" at the centre of the regulator's objectives, the PRA could help to reform the financial sector in a positive way.

We accept that this would mean the regulator making uncomfortable value judgments about some controversial activities, such as high frequency trading. However, the level of dysfunction that the market has achieved under laissez-faire and the inability of the industry to reshape itself mean the regulator must intervene if we are to have functionally effective financial markets that serve society's interests.

As a statutory objective, "effectiveness" would help the PRA to tackle some of the core problems in finance, such as principal/agent, institutional short-termism and excessive intermediation.

It could be supplemented with "have regard to" factors including, for example, social utility (enabling the regulator to ask who benefits from an activity, and at who's expense), informational symmetry (for example in reporting private equity or other fund returns), transparency on risk and pricing (so agents inform principals of the full costs) and appropriate pay structures (that avoid moral hazard and appropriation).

5 ***Is the model proposed in paragraph 3.16 – with each authority responsible for all decisions within their remit subject to financial stability considerations – appropriate, or would an integrated model (for example, giving one authority responsibility for authorisation and removal of permissions) be preferable?***

The PRA and CPCA should have clear individual responsibility for their areas so firms cannot exploit differences between them.

6-9 ***No specific comments on these questions.***

Additional comments on the PRA

(i) The intended primary objective of the PRA (para 3.5) should be amended to read: "to promote the stable, prudent and functionally effective operation of the financial system through the effective regulation of financial firms, in a way which minimises the disruption caused by any firms which do fail."

(ii) The PRA should consider requiring firms, as part of their licensing conditions, to state their economic function or purpose, and later to demonstrate to the PRA or CPMA that their activities conform with it [link to Statements of Purpose paper when ready]

(iii) The PRA and CPMA should jointly establish a high pay commission to investigate excessive remuneration in financial services. As well as monitoring compliance with FSA guidelines on pay, the PRA could use investigations of specific pay awards to uncover cases of market dysfunction or lack of competition.

(iv) On governance, the PRA board is proposed to include a majority of non-executive members appointed by the Treasury free from conflicts of interest (3.32). The same exclusion of finance professionals should apply as with the FPC.

III Consumer protection and markets authority (CPMA)

10 ***The Government welcomes respondents' views on:***

10.1 ***whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and FPC;***

Yes, as systemic stability comes before individual firms and their stakeholders.

10.2 ***whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which;***

We would retain only the last one, facilitating competition.

10.3 ***whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained;***

No, these should be dropped.

10.4 ***whether there are any additional broader public interest considerations to which the CPMA should have regard.***

The CPMA should have regard for a wide and evolving range of public interest factors. As with the PRA above, these should be assessed partly by functional outcome.

11-14 ***No specific comments on these questions.***

Additional comments on the CPMA

(i) We support the proposal in paragraph para 4.24 for the CPMA to have a more interventionist and pre-emptive approach to retail conduct regulation and hope this helps it to develop a strong focus on beneficial economic function, as for the PRA.

(ii) We agree that the CPMA should protect so-called sophisticated investors to the same level as retail investors, although in different ways (para 5.6). Wholesale markets have grown highly complex in both their structure and in the products offered. This makes vested interests and informational asymmetries commonplace and more damaging than in the retail markets, since the effects of wholesale market failure are greater.

IV Markets and infrastructure

15 ***The Government welcomes views on the proposed division of responsibilities for markets and infrastructure regulation.***

We note that the CPMA will have an explicit requirement to promote market efficiency and integrity (5.9). We hope that “efficiency” here will mean requiring exchanges to serve users with legitimate economic functions and not simply add profitable new trading services for speculators. The increase in short-term trading volumes in recent years has accompanied increased spending by exchanges on innovations that bring little economic benefit such as dark pools and high frequency trading. We would like to replace “market efficiency” with “market effectiveness”.

We would also like to see consideration given to the idea of market infrastructure being regulated as utilities, with controls on pricing and investment that reflect the public good.

16-22 ***No specific comments on these questions***

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[1] For example as proposed by former World Bank director Per Kurowski, accessed at http://subprimeregulations.blogspot.com/2009/10/my-voice-and-noise-on-regulatory-reform.html

[2] For a fuller discussion of democratising money creation see http://neweconomics.org/blog/2010/09/28/democratizing-money

HM Treasury consultation A new approach to financial regulation: judgement, focus and stability

A response by Norton Rose LLP

Introduction

Norton Rose Group is a leading international legal practice offering a full business law service from offices across Europe, the Middle East and Asia Pacific. The Group comprises Norton Rose LLP and its affiliates and Norton Rose Australia.

Our financial services practice provides an integrated transactional and advisory service for clients active in the financial markets, combined with expertise from the banking, investment funds, insurance and international securities practices.

We have consulted with our clients very widely within the financial services industry on the Government's proposals contained within the HM Treasury consultation paper „A new approach to financial regulation: judgement, focus and stability' (the Consultation).

Issues

Given our membership of the relevant Law Society committees, we are not submitting a full response to the Government's proposals. However, we would like to take this opportunity to comment on the following which are of particular concern to our clients:

1. The position of the markets division within the Consumer Protection and Markets Authority (CPMA).

2. The position concerning the separation of the UKLA primary listing role from the secondary market regulatory role.

Position of the markets division with the CPMA

We support the creation of a twin peaks regulatory structure in which the regulation of conduct of business and macro-prudential activity are separated by two bodies. However, it is crucial for financial stability that a strong markets division is created within the CPMA to ensure the proper and orderly regulation of the UK's capital markets.

Many of our clients have noted that the CPMA has been described as "a strong consumer champion" and there is a concern that it will not be able to differentiate proportionately between retail and wholesale business regulation because of its strong consumerist overlay.

It is essential that the integrity and experience of the markets division is safeguarded in the CPMA. It is therefore important that two equally strong and operationally distinct divisions within the CPMA are created for retail and markets business. Each division should be well resourced, having its own budget and run by separate managing directors.

We think that in order to give confidence to the market that the role of markets regulation will be properly recognised we think that the integrity of the markets division should be entrenched in the legislation. We recognise that there are various ways in which this might be achieved and would urge HM Treasury to consider some or all of the following types of provisions:-

- Appointment and removal of the managing director of the markets division directly by the Chancellor;
- Separate general duties on the CPMA when exercising its markets related functions akin to those currently in Section 73 FSMA in relation to the Listing Authority function in the new legislation;
- Consultation by the chief executive of the CPMA with the managing director of the markets division on all senior appointments;
- Requirement for the Board of the CPMA to have a certain number of representatives of the wholesale markets or their advisers;
- Requirement for the Board of the CPMA to set a separate budget for the markets division each year and to disclose this in the annual report;
- Ability for the managing director of the markets division to request resource from the CPMA Board or in extreme cases to write an open letter to the Chancellor for separate advisory functions, legal and enforcement support, for the division if at any point he or she believes that this is required in order for the CPMA to fulfil its functions;
- A separate market practitioner panel should be created which will be consulted in the same way as the existing panels;
- A requirement for markets issues to be dealt with in the CPMA annual report specifically.

Separation of the UKLA primary listing role from the secondary market regulatory role

A strong and cohesive markets division within the CPMA should maintain a strong link between the primary market (where companies raise capital) and the secondary market (where shares in companies are traded). This is necessary to maintain investor protection, ensure effective real time market supervision, tackle market abuse and execute enforcement activities.

We would support the broad-based industry view that the UKLA should remain within the markets division of the CPMA rather than be transferred to the Financial Reporting Council (FRC).

We have had the benefit of seeing the City of London Law Society's Company Law-Sub-Committee response to the Consultation and agree with the points made in relation to this issue. We particularly agree with the sub-committee's assertion that the proposed merger of the UKLA with the FRC offers little by way of synergies and would only serve to fragment the regulation and supervision of primary and secondary markets, to the detriment of investors and issuers.

It is important that a strong and cohesive markets division exists within the CPMA which maintains a strong link between the primary market and secondary market.

The UKLA has a crucial role in market regulation given its responsibility for overseeing consistency in disclosures and processes for listed securities. In light of this the UKLA should remain within the markets division of the CPMA as its functions are integral to the regulation of the markets on which securities are admitted to trading. We believe that this would keep primary markets regulation and secondary markets regulation in the same place and assist in the transition to the new regulatory arrangements.

There are concerns that the proposed separation will lead to regulatory and supervisory fragmentation which would ultimately be more costly for issuers. In addition, the proposals create the potential for two different rule books which possibly could contain conflicting rules which would result in inconsistent approaches being adopted.

The CPMA markets division will represent the UK at the new European Securities and Markets Authority (ESMA). In light of this it is important that the responsibilities of the CPMA mirror those of the ESMA. The transfer of responsibility for the UKLA from the markets division to the FRC would mean that the UK would only be directly represented at the European level on secondary markets issues. It is important that on securities issues both primary and secondary markets are equally represented at the European level.

Response from Norton Rose LLP

We welcome the opportunity to respond to the proposals for reform set out in the Treasury paper „A new approach to regulation: judgement, focus and stability'. We do not propose to address each of the questions posed in this paper but to provide our general views on the proposals as they may affect our clients in the insurance industry. Out main concerns are the following:

Adequate insurance representation at the FPC
Whilst we support the creation of a body with responsibility for macro-prudential oversight we have concerns that, without suitable representation from the insurance sector, the Financial Policy Committee (FPC) will only consider the macro-prudential issues facing banks. Any developing crisis within the insurance sector could potentially fail to reach the attention of the FPC as a significant systemic risk until it was too late to be addressed.

Lack of detail as to how the proposals will affect the insurance industry
We are concerned that the proposals fail to provide adequate detail of how the insurance sector will be regulated. We would hope that adequate consideration is given towards the benefit of these proposals to a sector worth billions of pounds to the UK economy. The paper addresses failings in the regulation of banks but does not explain how the proposals will benefit other financial sectors. In the Government's view, the financial crisis in the UK was exacerbated by the fact that no single institution had responsibility or power to take concerted action in response to emerging negative trends. The upheaval of the proposals may in fact, we believe, create a significant risk of regulatory „underlap' if insufficient consideration is given to how the Prudential Regulatory Authority (PRA) and Consumer Protection and Markets Authority (CPMA) will take over the current remit of the FSA.

In particular, we believe that the current proposals do not adequately explain how moving towards a dual regulatory system will benefit the insurance sector. We are concerned that for a number of insurers with both a broking or investment arm, the new system will impose increased costs and administration. The proposals fail to set out the extent to which firms might have to seek authorisation from both the PRA and the CPMA. Furthermore, it is not clear whether the new system will require individuals to seek approval from different regulatory bodies depending on whether the controlled function which they seek approval for fell within the remit of the PRA or CPMA.

There is a risk that a system with two regulators rather than one will be more burdensome and expensive for firms than the current FSA regime. Under the FSA regime, firms currently have the benefit of centralised supervision where a relationship manager can coordinate ARROW visits and supervisory issues with the firm. With the fragmentation of the regulatory system, many firms are concerned that there will be an inevitable rise in regulatory administration and a subsequent increase in costs.

The need for insurance specialists in the PRA and the impact on European policy
The government must ensure that the new authorities have suitable insurance expertise and we would wish to see the PRA established with a team of insurance specialists. Furthermore, we would expect this team to be given suitable resources with which to undertake their supervisory obligations. This will be of considerable importance in light of the role the PRA must play in the new European regulatory architecture. When EIOPA comes into existence in the New Year it is vital to ensure that the UK insurance sector is suitably represented in discussions concerning Solvency II and other new legislation or supervisory requirements at a pan-European level.

We are concerned that the CPMA should not be seen as the „poor relation' of the PRA in terms of staffing, budget and authority. The division of the FSA into two regulatory work streams, with the PRA within the Bank of England and the CPMA outside, risks creating a regulatory hierarchy with consumer protection and conduct issues being pushed out of the spotlight.

Lloyd's of London
The consultation paper states that the Government will consider how best to regulate Lloyd's of London. The Society of Lloyd's itself, as well as managing and members' agents, are currently regulated by the FSA. The proposal states that the Government, in consultation with both the FSA and the Bank of England, will consider how best to allocate the various regulated activities at Lloyd's between the PRA and CPMA. Lloyd's is a unique market and maintains this distinction in the

regulatory approach taken to its participants. Lloyd's itself has statutory obligations to regulate its own market. Under the Lloyd's Act 1982, the Council of Lloyd's is given "the management and superintendence of the affairs of the Society" and is empowered to "regulate and direct the business of insurance at Lloyd's". We are concerned about how a tripartite system comprising Lloyd's, the PRA as well as the CPMA may affect the administrative operation of the market.

The impact of the proposals on preparations for Solvency II

The timing of these upheavals could not be more challenging for the insurance industry. The change to a new financial regulatory regime in the UK will coincide with preparations for Solvency II as well as the Retail Distribution Review. The FSA is already facing the complex administrative burden of implementing Solvency II by the beginning of 2013. This challenge can only be made harder by the uncertainty and disruption that will result from the break-up of the FSA. For firms the changes will be no less challenging.

NYSE Euronext

NYSE Euronext's Response to HM Treasury's Consultation Document Entitled "A New Approach to Financial Regulation"

1. NYSE Euronext

1.1 NYSE Euronext is a leading global operator of financial markets and a provider of innovative trading technologies. NYSE Euronext's exchanges in Europe (Amsterdam, Brussels, Lisbon, London and Paris) and the United States provide for the trading of cash equities, bonds, futures, options, and other Exchange-traded products. NYSE Liffe is the name of NYSE Euronext's European derivatives business and is the world's second largest derivatives business by value of trading. It includes LIFFE Administration and Management, which is a self-clearing Recognised Investment Exchange pursuant to the Financial Services and Markets Act 2000 ("FSMA").

1.2 Furthermore, NYSE Euronext is building two new clearing houses, to be located in London and Paris. The former will be a Recognised Clearing House under FSMA.

2. Executive Summary

2.1 NYSE Euronext welcomes the opportunity to comment on the Government's plans to reform the system of financial regulation in the UK. NYSE Euronext has focussed its comments on those aspects of the reforms which will have a direct impact on markets and infrastructure (i.e. those matters set out in Chapter 5 of the Consultation Document).

2.2 NYSE Euronext recommends that the Government take action in the following four areas, in order of priority:

(a) **Recognised Body Regime:** rather than taking precipitous action, either maintain the status quo or conduct a meaningful consultation about the future of the Recognised Body regime, which will acknowledge the unique position of the Recognised Bodies, for example as front-line regulators rather than quasi-firms, and which will allow for a full exposition of the facts and a comprehensive explanation and consideration of the potential options.

(b) **Wholesale Markets Regulation:** ensure that the proposed conduct regulator, the Consumer Protection and Markets Authority ("CPMA"), is able – notwithstanding any retail investor focus – to regulate conduct in wholesale financial markets in a manner which reflects the needs of the professional users of those markets, recognising that such needs often differ significantly from those of retail investors.

(c) **Co-ordination Among the New Regulators:** ensure that the Bank of England and CPMA avoid overlap and gaps in the regulatory oversight of trading, clearing and settlement systems; ensure that the UK is represented effectively in the crucial negotiations within ESMA which lie ahead.

(d) **Listing:** make the UK Listing Authority ("UKLA") part of CPMA (rather than merge it with the Financial Reporting Council ("FRC")) in order to maintain the synergies between primary and secondary markets regulation.

3. Recognised Body Regime

3.1 The Consultation Document notes, briefly and almost in passing, that “the Government proposes also to consider whether there is any scope for rationalising the two regimes contained in the Financial Services and Markets Act 2000 or FSMA (authorisation under Part 4 and recognition under Part 18) under which trading platforms and CCPs are regulated”. The Consultation Document provides no explanation as to what this means in practice and cites no rationale for such an exercise. Nor does it set out the options that are being considered or the advantages and disadvantages which each would entail.

3.2 NYSE Euronext has discussed this matter with other Recognised Bodies, and in a joint meeting with the UK authorities it transpired that the Government is contemplating dismantling or significantly amending the regime under which Recognised Investment Exchanges (“RIEs”) and Recognised Clearing Houses (“RCHs”) (collectively, “Recognised Bodies”) are regulated. It is surprising that a matter of such significance was not explored more fully in the Consultation Document.

3.3 The regime for Recognised Bodies was established by the Conservative Government through enactment of the Financial Services Act 1986 and was carried forward into the present FSMA regime. As such, there has been over two decades of experience with the operation of the Recognised Bodies regime. In NYSE Euronext’s view, that experience has demonstrated the following:

(a) The structure of the current regime is correct in recognising, and continuing to recognise, the unique position of Recognised Bodies as front-line regulators of the member firms which use their facilities. As such, the Recognised Bodies are partners in regulation with the FSA (as they were with the Securities and Investments Board before it). This has provided an effective framework for the maintenance of fair and orderly markets. The changes which NYSE Euronext understands are being contemplated would radically alter the nature of the relationship between the Recognised Bodies and the statutory regulator, to the detriment of the efficacy of the regulatory system as a whole.

(b) The regime proved effective during the financial crisis. No Recognised Body was in distress – or in receipt of government funding – during the period of financial turmoil. On the contrary, the Recognised Bodies played an important part in managing the consequences of the default of major financial institutions, such as Lehman Brothers; and their markets continued to operate effectively and in an orderly and transparent manner, whilst liquidity in many other fora dried up.

(c) The legislative framework in most jurisdictions with major financial centres distinguishes exchanges and clearing houses on the one hand from users of their facilities (e.g. investment firms and banks) on the other, and subjects them to appropriately tailored regulatory obligations. Subjecting exchanges and clearing houses in the UK to a regime designed for investment firms and banks would run counter to those established international standards and would raise a question mark over the continued ability of UK-based exchanges and clearing houses to provide their facilities to their many users based outside the UK.

3.4 In light of these considerations, NYSE Euronext would strongly urge the Government to retain the status quo or to conduct a substantive consultation about the future of the Recognised Body regime, which will allow for a full exposition of the facts, a comprehensive explanation of the potential options and the advantages and disadvantages of each. This would facilitate an open and informed debate which would lend itself to an enhanced decision-making process about the way forward.

4. Wholesale Markets Regulation

4.1 The Government will be aware that concern has been expressed that the regulation of conduct in the wholesale financial markets will be the responsibility of a body which has been given the working title of "**Consumer** Protection and Markets Authority" (emphasis added).

4.2 Against this background, the Consultation Document recognises that the regulation of conduct in wholesale financial markets and of the infrastructure that supports those markets is a key area of financial regulation. It goes on to explain that the Government acknowledges the crucial role of these markets, both to the operation of the financial system as a whole and to London's position as a major financial centre. Furthermore, the Consultation Document recognises that the activities that are the focus of wholesale market conduct regulation are, in a number of important respects, considerably different from other types of financial services, particularly those provided to retail customers.

4.3 NYSE Euronext welcomes these acknowledgements and stresses that it is vital that the proposed conduct regulator, the CPMA, is guided by them in the manner in which it regulates the wholesale financial markets. NYSE Euronext therefore supports the Government's proposal that, in recognition of the differences between retail financial services and wholesale financial markets, responsibility for all market conduct regulation – including the oversight of exchanges - will be located within an operationally distinct division (i.e. the "markets division") of the CPMA.

4.4 It is important that these distinctions are drawn clearly, not just in relation to the operational organisation of the CPMA, but also in the legislation which underpins it and in its governance structure, rules, guidance and supervisory processes. Each of these must be appropriately calibrated in order to ensure that the CPMA undertakes the appropriate form and style of regulatory oversight for the type of business concerned, rather than having a perspective solely focussed on the interests (notwithstanding their worthiness) of the provision of retail-oriented services.

5. Co-ordination Among the New Regulators

5.1 The Government proposes to make the markets division of the CPMA responsible for regulating exchanges and other trading platforms and the Bank of England responsible for overseeing clearing houses and settlement systems. NYSE Euronext understands the underlying rationale for a bifurcated approach of this nature. However, it notes that trading, clearing and settlement cannot each be regulated in complete isolation as they are each a link in the same business chain. Activity in one link can and does have an impact on activity in the others.

5.2 For example, in the case of on-exchange derivatives markets, like NYSE Liffe's, where contracts are held open for months if not years, regulation of the market must encapsulate both trading activity (i.e. the flow of transactions on a daily basis) and open positions (i.e. the stock of outstanding transactions). Trading takes place on the regulated market, while resultant positions are held with the clearing house. Such positions can and do have an impact on future activity on the market and issues concerning them are, in many cases, the key factors which must be managed actively in respect of the maintenance of contract and market integrity. The legitimate interest that the CPMA should have in relevant areas of post-trade activity must therefore be explicitly acknowledged in its remit and responsibilities.

5.3 Any regulatory structure involving more than one agency is potentially prone to a lack of coordination and the resultant development of overlap or gaps in regulatory oversight. NYSE Euronext would therefore urge the Government to ensure that an operational framework is put into place which will enable the Bank of England and the CPMA to operate in a coordinated fashion in the interests of minimising the costs and promoting the effectiveness of the regulatory system.

5.4 Furthermore, the Government has announced that the CPMA will represent the UK on all matters within the European Securities and Markets Authority ("ESMA"). However, unlike the remit of the CPMA, ESMA's remit will not be confined to conduct regulation, but will also include.prudential regulation. Indeed, one of ESMA's first tasks will be to develop binding technical standards which will underpin the European Market Infrastructure Regulation ("EMIR"). EMIR will, amongst other things, promulgate standards for central counterparties, which at national level within the UK will be an area of regulation led by the Bank of England rather than the CPMA. As such, a concern must arise as to how key aspects of clearing and other areas of prudential regulation can be effectively handled, in the ESMA context, by a body which does not have primary responsibility for such matters at national level.

5.5 In such circumstances, there is a real danger that the UK's voice will not carry sufficient weight, or will not be informed by adequate expertise, in the crucial negotiations which lay ahead on these matters within ESMA. NYSE Euronext would therefore urge the Government to consider pragmatic means by which those responsible for clearing/prudential regulation in a national context can be properly engaged in the relevant ESMA negotiations. In any event, it is crucial that the CPMA is able to point to explicit responsibilities (and therefore its general credibility to opine in related matters) in those areas of post-trade activity in which it has a direct interest.

6. Listing

6.1 UKLA has an important role to play in the development of the London capital markets and, more generally, in facilitating capital formation in a robust but efficient manner. NYSE Euronext believes that the best way to ensure that UKLA continues to perform this role effectively is for it to remain within the CPMA markets division. This conclusion is based on several important factors:

(a) It is important for primary and secondary markets to be considered together, both in terms of policy formulation and in the implementation of that policy. Dividing regulatory functions in the way proposed between the CPMA and the merged FRC and UKLA increases complexity and may result in differences in the regulatory approach to particular problems. There is also a danger that knowledge about market participants will be held more disparately, thereby potentially increasing oversight risk.

(b) As the CPMA will be the UK's representative in ESMA and, more generally, in European debates, it may be less effective in addressing primary market issues if it has no direct involvement in such matters.

(c) It is not obvious that the FRC is a natural partner for the UKLA other than the fact that both have an interest in the corporate sector. In particular, UKLA has a far greater involvement in real-time monitoring and supervision than the FRC and greater interest in international matters (the FRC having little exposure to non-UK matters). Merging the two could dilute the effectiveness of the UKLA to address such matters, to the detriment of the development of London as an international centre for capital raising.

7. Next Steps

7.1 NYSE Euronext would welcome the opportunity to discuss further the contents of its response to the Consultation Document with HM Treasury, the Bank of England and the FSA.

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Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
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14 October 2010

Dear Sirs,

A new approach to financial regulation: judgement, focus and stability

On behalf of Old Mutual plc, a financial conglomerate with its primary listing in London, I welcome the opportunity to respond to the above consultation. Although the Government has a number of options available to it in relation to the regulatory framework, we have accepted that the HM Treasury paper reflects a structural decision that has been taken so have not responded on other options that may have been available to it in this regard. The attached document therefore contains our detailed response to the questions raised, albeit there are some issues of fundamental importance which I have brought to your attention below:

1) A key theme in the paper is the continued use of secondary factors and other considerations by regulators and there is a sense that there is a desire for these to fall away or be significantly reduced. This may be a question of language, but I do wish to make it clear that I would be very concerned if these secondary factors were in any way diluted as these are part of the key checks and balances of the current system. I am sure they can be made to work better and be more tailored, but it is important that they are there.

2) It is of significant importance that all three regulatory bodies work closely together to ensure consistency of approach and a level playing field across the different sectors and in the EU. Related to this point is the question of how the regulators will resolve internal differences on policy areas. The paper gives the impression that it will be possible for the regulators to operate independently with the main cross reference being cross directorships at the executive level. I think this is insufficient.

3) The new regulatory system should not just address the recent macroeconomic issues but must also be focused on the level of financial services activity in the UK. A regulator's success cannot simply be considered in the context of no major firm failures or 100% compliance to rules. The level of activity in the market and whether consumers are actively investing for the future and insuring against risks must also be a key metric and we suggest this should be a prominent feature of the new regime.

4) It seems to us that intuitively, a regulatory regime change of this scale will lead to significant industry costs by small and large firms alike. Having examined the preliminary impact assessment we are not persuaded by some of the underlying assumptions and are concerned to ensure that the Government does not underestimate the impact of its proposals.

I trust that this letter and our detailed comments will be of assistance to you in the development of the new regime.

Yours sincerely

Philip Broadley
Group Finance Director
Old Mutual plc

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Response to questions

Question 1: Should the FPC have a single, clear, unconstrained objective relating to financial stability and its macro-prudential role, or should its objective be supplemented with secondary factors?

Whilst it is important that the FPC is not constrained in its principle role, it cannot operate in complete isolation to the broader regulatory framework. We believe therefore that its objectives must include the need to have regard to specified secondary factors as these will serve to balance its activities and place them in a broader context. It is important however that these secondary factors are not too internally focused but contain reference to external success factors. An example here could concern the impact of macro-prudential policy on consumer lending. If the objective stops at the need for financial stability, then this could result in decisions that harm consumers.

Question 2: If you support the idea of secondary factors, what types of factors should be applied to the FPC?

1. Economic and fiscal impact
2. The Statutory objectives of the other regulatory authorities
3. The regulatory regime in general should support the maintenance of a vibrant, competitive and growing financial services market where impact on end consumers is given prominence in decision taking.
4. The broader legal framework in the UK and Europe
5. International developments and initiatives concerning macroeconomic policy and developments (it is important that the UK does not go out on a limb on macroeconomic issues)

Question 3: How should these factors be formulated in legislation – for example, as a list of "have regards" as is currently the case in the Financial Services and Markets Act 2000 (FSMA), or as a set of secondary statutory objectives which the FPC must balance?

There are pros and cons of each route. In view of the Treasury's concern that the FPC must have the freedom to act, then "have regards" may provide more flexibility. It is important however that whatever route is chosen, the FPC is subject to sufficient external scrutiny on how it exercises its powers in the context of these secondary requirements.

Question 4: Whether the PRA should have regard to the primary objectives of the CPMA and FPC?

Yes. Even with separate regulatory bodies there still needs to be "joined up" regulation. An important component of the new regime needs to be close cooperation and awareness between regulators of their mutual objectives and activities. Joint awareness will limit the likelihood of the regulators pulling in different directions.

This point is particularly important in relation to the potential over time for firms subject to prudential regulation by the PRA to be subject to different requirements than firms subject to prudential regulation by the CPMA as this will result in an unlevel playing field. The policy approach in relation to European developments of both the PRA and CPMA must also be aligned to avoid diverging standards. Both of these points imply a working relationship between the two regulators that is prescribed as part of the regulatory structure.

- ***Whether some or all of the principles for good regulations currently set out in Section 2 of FSMA, particularly those relating to good regulatory practice should be retained for the PRA?***

We believe all the principles should be retained and should apply to the FPC, CPMA and the PRA in the context of their respective activities. Although the core objectives of each regulator may be different, (i.e., macro-prudential, micro-prudential and customers and markets), all of them impact the financial sector so should be required to consider the impact of their activities on it.

- ***Whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained?***

The purpose of the principles of global competitiveness and innovation as part of the FSA's remit are derived from the risk that without such considerations regulation could develop in a vacuum and without sufficient regard to the broader environment. It is our view that in the absence of such considerations, the financial sector in the UK could be placed at a disadvantage relative to its international peers. These requirements should therefore be retained.

- ***Whether there are any additional broader public interest considerations to which the PRA should have regard.***

We believe that all three regulators should also be required to consider the volume of financial services activity in the UK market and in particular the level of take-up of financial products (i.e., not just lending). In this respect, increased regulation may have the potential to reduce client disadvantage, but it can also markedly reduce the level of sales and take-up of products by clients. In our view the level of take-up of financial services products must surely be a key public interest consideration and the correlation between increased regulatory requirements and falling client take-up should therefore be defined and monitored on an ongoing basis. With an increasingly aging population many of whom have little pension provision any factors that could inhibit the availability of financial products should be taken seriously.

Question 5: Is the model proposed in paragraphs 3.16 – with each authority responsible for all decisions within their remit subject to financial stability considerations – appropriate, or would an integrated model (for example, giving one authority responsibility for authorisation and removal of permissions) be preferable?

In our view, there is a case for the establishment of distinct departments dealing with functional areas that work across the regulators. Authorisation, permissions, approved persons and fees are the most obvious, albeit a case could be made that the specialist skills required for enforcement could also warrant a distinct cross regulatory function. This would facilitate an easy lift out from the FSA, consistency, reduction in duplication and allow for the development of appropriate skills that can serve the PRA and CPMA.

The challenge here would be the level at which decisions could be taken by the department under an SLA and what would be reserved to the regulator. A service arrangement could not work however if too much was reserved.

Question 6: Is the approach outlined in paragraph 3.17 to 3.23 for transfer of regulatory functions and rule making sufficient to enable the PRA to take a more risk-based, judgement-focused approach to supervision?

It is important that the new regime is established with minimal change, so we support the use of existing FSMA rules where this is possible. It is understood that in some areas the rules will cover both the PRA and CPMA and overlap and underlap will need to be considered. As a principle we suggest that new rules are kept to a minimum.

We believe a bigger question concerns an assessment of the structure of rules and whether these are delivering a proportional regulatory benefit. There is reference in the paper to moving to a more "judgment focused" model and in this light it would be a good opportunity to review the rules when transitioning to the new model. A point that I believe needs to be made when considering a judgment focused model is whether the regulator has staff with the relevant skills and experience and can make the balanced judgments necessary for such a regime to be effective. This is an issue that has been raised in relation to the current regime, but in my view has not been fully addressed.

Question 7: Are safeguards on the PRA's rule-making function required?

Yes. We see no reason for the current safeguards not continuing in the new regime. These safeguards were there for a reason and we would caution against taking them away in the absence of certainty that adequate safeguards exist elsewhere.

Question 8: If safeguards are required, how should the current FSMA safeguards be streamlined?

We see no reason why they should be streamlined and are not clear why this is considered necessary. We are conscious that in other jurisdictions, the involvement of the industry in the rule making process is far greater than in the UK and in many respects the net position is better for it. Certainly significant consultation with industry feedback taken seriously, can result in greater alignment and support on new rules and better outcomes. With this in mind we would argue for more involvement and greater consideration to industry views rather than a removal of this part of the process or any reductions in its scope. We would also argue for greater external scrutiny of decisions taken by the regulators where they differ markedly from industry views.

Question 9: The Government welcomes views on the measures proposed in paragraphs 3.28 to 3.41, which are designed to ensure that the operation of the PRA is transparent, operationally independent and accountable.

Besides PRA being audited by the National Audit Office, there should be a mechanism in place for the industry to submit either annually or bi-annually their views on PRA and what needs to be changed or improved. The regulated firms should be in a position to challenge PRA on issues that they feel strongly about. In essence the challenge mechanism should be the same as that for the CPMA as described in para 4.36.

Question 10: The Government welcomes respondents' views on:

- ***Whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and FPC?***

Yes, but further clarification is needed from the Government on how conflicting issues and judgement between PRA, CPMA, the regulated firms, politicians and wider public issues should be addressed.

We also think the language used in the paper of "consumer champion" with its supporting rhetoric of "tougher, proactive and focussed approach to regulating conduct" should be avoided as this continues to portray the industry in a negative light to the general public. We believe this type of messaging can have the unintended consequence of hindering the take-up of financial products at a time when there is a significant need for more provision in a wide range of sectors. Additionally we are not convinced that consumers need to see messaging that informs them that the regulator is "on their side" (if that is the intention). Surely a regulatory title that includes reference to "Consumer Protection" is already clear enough in terms of its purpose. It is also important to consider that if the consumer protection role of the regulator is overplayed, this will undermine the intention of being more balanced between supervision of firms and consumer responsibility (as commented in section 4.25 of your paper).

- ***Whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which?***

Yes, we believe these should all be retained.

- ***Whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained?***

As mentioned above, this is a principle that can apply proportionately to the activities of all regulators.

➢ ***Whether there are any additional broader public interest considerations to which the CPMA should have regard?***

Yes. Please see comments in relation to the PRA as applying here as well.

Question 11: Are the accountability mechanisms proposed for the CPMA appropriate and sufficient for its role as an independent conduct regulator?

Yes, but it is important that accountability considerations concern the impact of CPMA's activities in a broader sense and not just the narrower question of whether confidence in the markets has been achieved.

Question 12: The Government welcomes views on the role and membership of the three proposed statutory panels for the CPMA.

The Consumer Panel, Practitioner Panel and Small business Practitioner Panel should continue on similar lines to today. A point of note however is that consumers, practitioners and small businesses will be influenced by decisions taken by the PRA (Prudential implications on the large retail firms) and also to a lesser extent by macro prudential requirements impacting firms as required by the FPC. There needs to be a mechanism therefore to ensure that the panels can consider and provide feedback and input on the regulatory system as a whole and not just on the activities of the CPMA

Question 13: The Government welcomes views on the proposed funding arrangements, in particular, the proposal that the CPMA will be the fee- and levy-collecting body for all regulatory authorities and associated bodies.

A central fee collecting body would minimise duplication, albeit this does not need to be any single regulator. A service company working on behalf of the regulators is another model for doing this.

We believe a more important issue the Government needs to tackle is the continuing increase in regulatory costs. Already the industry believes fees and levies are too high and with the new structure resulting in more regulatory bodies the expectation must be that fees and levies will increase still further (we are not persuaded at this stage that costs will be broadly neutral). We believe an analysis is required of the value for money to UK plc of costs expended on UK regulation compared for example to other regimes which have more proportional structures and whose experience in recent times has fared at least as well as the UK. Regulatory costs have increased significantly since the late 80's when the Financial Services Act came into force and notwithstanding increasingly complex requirements on firms and often intensive scrutiny; this was not enough to prevent the recent banking failures. It is absolutely critical therefore that the regulatory restructure does not simply concern organisational change as mooted by this paper but is also concerned with an assessment of the right regulatory approach with a willingness to drop rules, systems and procedures that have not worked, may be of negligible regulatory benefit and yet consume significant industry cost.

A related point is the need for consideration of how the UK regulator approaches its European role and whether it is right for UK plc, its firms and consumers for the UK regulator to act as "lead" in relation to European regulatory developments. This often results in UK firms incurring costs that result in them being subject to regulatory requirements that are super equivalent to the directives leaving them at a disadvantage to their EU peers.

Question 14: The Government welcomes views on the proposed alternative options for operating models for the FSCS.

We support separate levies for different classes of business under the auspices of one body that would collect the levies and administer the scheme across the complete industry. We suspect however that the lack of cross subsidy may be an issue for some sectors and in such circumstances a proportionate loading may be relevant.

Question 15: The Government welcomes views on the proposed division of responsibilities for markets and infrastructure regulation.

We have no concerns with these proposals.

Question 16: The Government welcomes views on the possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses.

We have no strong views on this issue.

Question 17: The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.

This would be a logical step.

Question 18: The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.

Consideration could be given to whether the Takeover Panel should also come under the auspices of the markets division of the CPMA or even part of a merged UKLA/FRC body.

Question 19: Do you have any overall comments on the arrangements for crisis management?

No.

Question 20: What further powers of heightened supervision should be made available to the PRA and the CPMA, and in particular would there be advantages to mandatory intervention, as described in paragraph 6.17?

No strong views.

Question 21: What are your views about changes that may be required to enhance accountability within the SRR, as described in paragraphs 6.21 to 6.24?

No strong views.

Question 22: Annex B contains a preliminary impact assessment for the Government's proposals. As set out in that document, the Government welcomes comments from respondents on the assumptions made about transitional and ongoing costs for all types of firm. In particular, comments are sought from all types and size of deposit-taking, insurance and investment banking firms (including credit unions and friendly societies), and from groups containing such firms.

Having reviewed the preliminary impact assessment we are not convinced that the assumptions in terms of cost (minimal costs in general) will be borne out in practice. I cannot see that regulatory regime change of this nature can be anything other than a material undertaking for the majority of financial services firms. It should be appreciated that firms will need to track changes to FSMA, the FSA rules and in some cases those of other bodies, conduct an impact assessment, advise management and then implement changes to procedural documents and in some instances systems and controls. I believe this will concern significant cost for major groups and most large firms and would be surprised if even smaller firms did not incur material cost in this area. This will be at a time when other changes are being implemented, for example Solvency II, RDR, CRD changes and PRIPS. Of course if a regime change is the Governments intention then this will be necessary, but I am concerned that there is not an underestimate of the cost and impact of doing so.

Other factors that should be considered:

We have answered the questioned set out in the paper, but also have some additional points we would like to make now. We trust these will be of use as work develops on the more detailed policy considerations of the new regulatory framework. These concern:

- The difficulties that may arise for firms in dealing with two regulators. In this respect, will the PRA be the senior regulator for firm interactions and overrule the CPMA in the event of a conflict of views? If so, what impact will this have on the ability of the CPMA to meet is regulatory obligations? Although the previous regime had a number of different regulators (PIA, IMRO etc), these were covering discrete areas. We believe the proposed regime has the potential for difficulties here which need to be considered.
- How will regulatory interaction operate at a Major Retail Group level? i.e., Close and Continuous (C&C) meetings with the Supervisory team from PRA, or will a team from the CPMA also want C&C meetings?
- How will notification and escalation work, particularly under Principle 11 (or its equivalent). Will one regulator inform the other or will both regulators need to be informed?
- How will Enforcement be handled? One team across both regulators or two teams. How will there be consistency? If the need for significant legal/regulatory skills are taken into account we believe this gives strong support for an enforcement division that is outside of the regulators and works for them.
- How will ARROW reviews be handled? PRA, CPMA or joint.
- The need for consistency and one contact point on Approved Persons, Permissions, Change in Control and similar broad areas.
- How will contact with international regulators be handled. How many touch points with the UK.

I would like to respond to the current review of Financial Services within the timescale allotted.

It is my view that the FSA has failed miserably in regulating the financial activities in the UK. They seem to allow the Banks to get away with whatever they wish with impunity, the complaints against banks are running at astronomical levels but again nothing is ever done to curtail their activities. I see clients daily who tell me of the experiences they have had with their banks but they are never brought to task by the FSA. Where were they when we had the banking crisis. Not one banker/executive has been prosecuted while it appears that IFA's are fined/suspended for much lesser minor infringements. The cost of regulation is ever going upward while at the same time FSA are rewarding themselves with huge bonuses. For failure! The introduction of the RDR will cause much disruption to advisers and consumers alike. Many advisers who for years have provided quality advice to their clients will now leave the industry because of the costs/qualification requirement imposed without consultation on the IFA community.

And who now will those clients turn to for advice. Heaven forbid, they will have to go to the banks. The % of complaints against the banks is running in excess of 50% at present but after the RDR, when many IFA's will not be around to advise these same clients, these complaints levels will rise to astronomical proportions. Are MP's ready for the fall out? I think not. Additionally they (FSA) act as judge, jury and executioner without the right of appeal. Wherefore the Human Rights Act - they ride roughshod over it with impunity!

What kind of a society is that? I strongly believe that we need regulation but I also feel that it needs to be proportionate, cost effective and fair. The FSA are none of these things. In my view, after 20 years in the industry, the FSA are the most draconian of all of the regulators, yet they have achieved far less than their predecessors. The costs cannot possibly continue and will eventually lead to the demise of Independent Financial Advice in the UK which will suit the banks in their voracious appetite to take it all but by allowing the banks their largesse will only lead to the detriment to the consumers in society which in turn will lead to unfairness and hostility towards the establishment will undoubtedly result.

Thank you for allowing me my response.

Colin Palmer

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Response

PanaceaIFA.com submission in connection with the formation of the Consumer protection and markets authority (CPMA)

Contact: Derek Bradley, ceo, PanaceaIFA.com

PanacaealFA.com, Rotterdam House, 116 Quayside, Newcastle upon Tyne, NE1 3DY

Date: 22 September 2010

Introduction

PanaceaIFA.com is an online community representing 3,000 smaller, directly regulated Independent Financial Advisers (IFAs). Our members' annual premium income from sales represents £639.9 million. PanaceaIFA.com aims to give a voice to smaller, directly regulated IFAs and help ensure their concerns are not overlooked by policy makers.

PanaceaIFA.com welcomes the opportunity to contribute written evidence to the Treasury Select Committee's inquiry.

Key Points

- The formation of the CPMA should take into account the five key principles of the Better Regulation Executive.
- Legislators should consider the unintended consequences of regulation on smaller businesses in the financial services sector, while addressing the failures which lead to the financial crisis.

- The CPMA should take a risk-based, transparent, consistent and proportionate approach in its dealings with IFAs, something the Financial Services Authority (FSA) has often failed to do.

Submission & Recommendations

1. When constituting upon the formation of the CPMA, and with the smaller IFA firm in mind, HM Treasury should build on the principles of the Regulators' Compliance Code.

2. The Regulators' Compliance Code is a central part of the Government's better regulation agenda. Its aim is to embed a risk-based, proportionate and targeted approach to regulatory inspection and enforcement among the regulators it applies to.

3. PanaceaIFA.com's members see the government's review of Financial Services Regulation as a much needed opportunity to ensure these principles are applied to the CPMA.

4. While protecting the consumer, such an approach would deliver significant benefits to low risk and compliant businesses within the IFA sector through better-focused inspection activity, better advice for businesses and lower compliance costs.

5. **Transparency** - The FSA has often failed to be transparent. Rules are often unclear, change frequently and are applied retrospectively. This makes compliance extremely difficult for smaller IFA firms.

6. **Accountable** - The CPMA should be accountable for its actions. Currently the FSA cannot be sued for any failures and has a record of being neither fair nor reasonable to the small businesses it has

PanaceaIFA .com Empowering small IFA firms

regulatory authority over.

7. **Proportionate** - **T**he regulatory costs of resources, reporting, disciplinary action and qualification levels should reflect fairly and proportionately on small IFA firms, by giving consideration to the size of the regulated firm and the nature of its activities.

8. **Consistent** - the CPMA should ensure that the nature and direction of regulation is clear for all to see, by way of rules not principles, and not subject to knee jerk reaction and changes of direction or policy on a whim.

9. **Targeted -** the CPMA should only direct its attention towards cases where action is needed. The FSA has a history of embarking on "fishing expeditions" seeking out, even creating problems without thinking through the impact of its actions. It is therefore important that the CPMA builds confidence and trust with the consumer and the IFA community in its ability as a regulator to carry out its role correctly and in a fair and reasonable way.

10. Key staff in the CPMA should be required to gain financial services qualifications to better understand the markets in which they are operating.

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18 October 2010

Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

financial.reform@hmtreasury.gsi.gov.uk

Dear Sirs

Response to the HM Treasury consultation paper on plans to change the system of UK financial regulation

As you are aware, we have recently completed, in collaboration with another firm, an extensive review of the practical aspects of implementation of a framework for supervisory control of systemic risk. That work was commissioned by the Financial Services Knowledge Transfer Network and has been part-funded by the Technology Strategy Board. In this submission, I respond in my own capacity.

We recently responded extensively to the Treasury Committee's consultation on the proposed changes to the system of UK financial regulation. I consider that our responses to the Treasury Committee to be equally applicable to and valid for your own consultation exercise. Accordingly, I refer you both the submission we prepared collaboratively with our report co-author to the Treasury Committee and the executive summary of our recent report (see URL below). A full version of the report is also available at our website.

I draw your attention to paras 24 to 29 of our submission to the Treasury Committee in which we indicate our concern that the HM Treasury consultation paper failed to distinguish between macroprudential and systemic risks in the sense of risks emerging from the system. The concern is that, by omitting the distinction, the HM Treasury consultation paper underemphasizes the problems of interconnectedness and endogenous sources of financial network instability. That may result in a subsequent failure to resource properly research on and development of solutions to the problems of network instability and endogenous risk in the financial system.

I hope you find our observations constructive and useful. I remain willing to meet officials of HM Treasury to discuss these issues at a mutually convenient time.

Yours sincerely

Peter Bonisch

Managing Director
Paradigm Risk Limited

Information referred to is available at http://www.paradigmrisk.com/systemic-risk

PAYMENTS COUNCIL

18 October 2010

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RESPONSE TO HM TREASURY'S CONSULTATION ON *A NEW APPROACH TO FINANCIAL REGULATION: JUDGEMENT, FOCUS AND STABILITY*

Please find attached a response from the Payments Council to HM Treasury's consultation on *A New Approach to Financial Regulation: Judgement, Focus and Stability.*

Please contact me if you have any questions regarding this response.

Yours sincerely

Rosalind Beaumont
Public Affairs Manager

RESPONSE TO HM TREASURY CONSULTATION ON *A NEW APPROACH TO FINANCIAL REGULATION: JUDGEMENT, FOCUS AND STABILITY*

1. INTRODUCTION

1.1 The Payments Council is pleased to have the opportunity to respond to HM Treasury's consultation on *A New Approach to Financial Regulation: Judgement, Focus and Stability*.

1.2 The Payments Council is the organisation that sets strategy for UK payments. It was established in March 2007 to ensure that UK payment systems and services meet the needs of users, payment services providers and the wider economy. Whilst the Council is funded by its membership, which consists of banks and other bodies that provide payment services, the Board does have an Independent Chair and four Independent Directors who represent consumer and business interests. These Independent Directors, whilst in a numerical minority, can collectively veto any decision of the Board. The Council also operates several User Forums to enable better understanding of user requirements of the payment system over a wide range of subjects.

1.3 The Payments Council has three core objectives:

- to have a strategic vision for payments and lead the future development of cooperative payment services in the UK;
- to ensure that the payment system is open, accountable and transparent; and
- to ensure the operational efficiency, effectiveness and integrity of payment services in the UK.

1.4 The Payments Council works closely with its contracted schemes, for the benefit of the UK payments industry. These include:

- Bacs Payment Schemes Limited;
- CHAPS Clearing Company (covering two schemes: the CHAPS Sterling and Faster Payments);
- LINK ATM Scheme;
- Cheque & Credit Clearing Company Limited;
- Belfast Bankers' Clearing Company Limited; and
- UK Domestic Cheque Guarantee Card Scheme.

1.5 The clearing schemes are run by their respective Boards which are responsible for setting the work of the schemes and their entry criteria. This response covers the contracted schemes, with the exception of the UK Domestic Cheque Guarantee Card Scheme as it has been agreed this scheme will close on 30 June 2011.

2. OVERSIGHT OF PAYMENT SYSTEMS

2.1 A primary concern for the Payments Council is any proposed change in the oversight of payment systems and where this sits in the regulatory structure.

2.2 We are pleased that the lead responsibility for oversight of payment systems remains with the Bank of England. The recent move from informal to statutory oversight has led to significant adjustments, especially for recognised schemes and the new regime should build on that work. But we note that some adjustment is going to be necessary in any event, as the embedded payment schemes – which currently are jointly overseen by the Bank and the FSA – will move exclusively to Bank oversight.

2.3 This opens up a fundamental question: will the present system by which payment systems are split between 'recognised' and 'unrecognised' be maintained; or will every scheme be expected to be authorised or recognised in some way or other? We suggest that the answer to the question has significant implication for systems and regulators and should be addressed as early as possible in the process. We also note that the Banking Act 2009 gave the Bank a power, as yet unused, to recognise payment infrastructure providers. How and where will this fit in the new regime?

2.4 Our preference – if only because it will minimise the costs and time of change – would be for continuation of the current recognition system, even if the precise list of schemes to be recognised were reviewed. The regime has not had time to be tested and change of so new a structure seems unnecessary.

2.5 We hope that those developing the new regime, in particular preparing the relevant statutory provisions, will consult fully with us and the payment systems.

2.6 Whilst payment systems have performed well during turbulent economic times, we do have an interest in the way that Special Resolution Regimes (SRRs) are implemented and would wish to ensure that they do not overlook institutions' participation and obligations to the payments system. We therefore look forward to working with HM Treasury and the authorities in their evolution of the SRR regime and providing our expertise on payment systems as input to the discussions.

2.7 With a new regime being born and several new bodies being created, the legislation will need to clearly set out the objectives of each body.

3. RELATIONS BETWEEN REGULATORS

3.1 From the perspective of payment systems, the prime regulatory focus will be on the Financial Stability part of the Bank of England. But the members of the system will be prudentially regulated by the new PRA. Experience has shown that the effect of regulatory change on behaviour in payment systems is often overlooked or underplayed. We hope that the relationship between Financial Stability and PRA will be sufficiently transparent and communication will be sufficiently good for the effect of PRA decisions on payment systems to be understood and, where appropriate, discussed and challenged by both the overseer and those who centrally operate the system.

3.2 The Payments Council will work to ensure that there is good communication between ourselves and all those with an interest in the system. We would expect to be able to share appropriate information with all the regulatory bodies, without artificial constraints, imposed by statute.

4. CONSUMER PROTECTION AND MARKETS AUTHORITY (CPMA)

4.1 The Consultation Paper sets out proposals to create a dedicated Consumer Protection and Markets Authority (CPMA) with a primary statutory responsibility to promote confidence in financial services and markets – a regulator with specific responsibility for consumer protection. This will be achieved in two ways: by the protection of consumers through a strong consumer division within the CPMA; and through promoting confidence in the integrity and efficiency of the UK's financial markets.

4.2 We look forward to seeing further detail as to the exact work currently undertaken by the FSA that would be transferred to the CPMA, and also to find out how far its remit and power extends; we are particularly interested in learning about whether (if any) interest the CPMA would be able to take in payment systems and to what process they would be subject; and whether their remit will be tightly defined in statute.

4.3 It is especially important for us to understand this role because of the market responsibilities of the CPMA which could well have a relationship to aspects of payment systems. We are pleased to see the emphasis on good communication and co-operation between the Bank and the CPMA in the Consultation Paper.

4.4 We do have a concern in that the CPMA has also been described as a “consumer champion”. We believe that the definition of “consumer champion” in these circumstances needs full clarification as the term would suggest that the body would be pushing for action on behalf of consumers, which could be at odds with its role as regulator. We would question whether a single organisation can regulate the markets at the same time acting as a consumer champion. The two roles will inevitably be in conflict on occasion.

5. CONCLUSION

It cannot be underestimated the significance of a stable payment system in delivering regulatory objectives and to the need of the payment systems to be seen as part of a good financial system; the Payments Council looks forward to continuing to work with the authorities to achieve these common objectives.

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Financial Regulation Strategy
HM Treasury
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15th October 2010

We welcome the opportunity to respond to the consultation *'A new approach to financial regulation'*.

Pensions & Investment Research Consultants Ltd (PIRC) has been an independent adviser to pension funds and other institutional investors for over 20 years. PIRC's clients have combined assets in excess of £1.5 trillion and include some of the largest pension funds, investment management companies and insurance companies in the UK and overseas. Together, they comprise a diverse group of institutional investors with long-term liabilities and broad fiduciary duties.

PIRC undertakes company research on corporate governance and corporate social responsibility issues at public companies, and provides advice to clients on proxy voting strategies and other active shareholder initiatives. Our comments are based on two decades of practical experience, which inform our views on the strengths and weaknesses of disclosures, governance structures, and the interaction of statute, regulation and codes of practice.

We wish to restrict our comments to the two questions relating to the role of the Financial Reporting Council (FRC) and the creation of a new companies regulator:

17 The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.

18 The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.

In PIRC's view, the transfer of the UKLA to the FRC makes a great deal of sense. We consider that the listing rules sit well with other aspects of company reporting. We also believe that it is important that all elements relating to the disclosure of information on the corporate governance of listed companies sit in one place.

Emphasising the seriousness given to companies' governance disclosures is particularly important in the context of the current consultation given the widespread consensus that governance failures were a contributory cause of the financial crisis. By placing the UKLA within the FRC, which has responsibility for the Corporate Governance Code, we believe this would send a clear signal that governance questions must be taken seriously by issuers.

More broadly, we strongly support the suggestion that combining the UKLA with the FRC should be the first step in the creation of a companies regulator. PIRC has advocated the creation of a companies regulator for many years, and we repeated this suggestion in our statement of ideas for reform issued in the wake of the crisis:

“[T]he FSA could amalgamate the FRC into a single companies regulator. It could be given wide ranging powers of intervention and market intelligence gathering and much more draconian powers of „stop and search’ amongst market practitioners and company directors.”[1]

Whilst we had envisaged that the FRC could be merged into the FSA to form the basis of a companies regulator, it is clear that moving functions from the FSA into the FRC would achieve the same objective. We also agree with the proposition that a companies regulator could be responsible to BIS. This makes sense given the Department’s responsibility for Company Law.

We would be happy to discuss these issues in more details.

Kind regards,

Alan MacDougall
Managing Director

[1] http://www.pirc.co.uk/sites/default/files/Manifesto%20new.pdf

3rd September 2010

FINANCIAL SECRETARY
REC 15 SEP 2010
ACTION
COPIES TO

Mark Hoban Esq MP
Financial Secretary to the Treasury
House of Commons
London
SW1A 0AA

Dear Mr Hoban

You have asked us for comments on the proposed reform of financial regulation which we have done below. We are not sure who to address the comments too and so forgive me for sending this direct to you, and perhaps you could pass it on to the relevant person at the Treasury.

We are a firm specialising in the provision of insurance to the tourist industry. Our plans include, public liability, employers liability, professional indemnity, protecting customers deposits (bonding), insurance for overseas staff, UK staff travelling on business and travel insurance for customers.

I have read of the consultation document, although not in detail, and can find very little reference to the regulation of insurance brokers and in particular our sector; tour operators and travel agents.

Since this is early days in reforming the regulation I would like to make my points known at an early stage and I hope that much of the matters addressed below can be eased in order for us to carry out our business without the kind of regulatory interference referred to.

Below is an extract from a letter to my MP Andrew Tyrie which I sent some 12 months ago.

Insurance Mediation Directive

We are regulated by venture of a directive from Brussels entitled 'Insurance Mediation Directive' (IMD). Effectively this involves insurance brokers and has little effect in Europe as on the whole Europe do not have brokers in the same way as we do.

Britain is different as we have a well-developed network of Insurance Brokers serving the public and thus the IMD has more effect on Britain than on other member states.

For some reason the British Government decided to expand the scope and extend regulation under the IMD to insurance companies and agents of companies and brokers.

There is a clause in the IMD specifically exempting Travel Agents (and Tour Operators) and as a result the

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Authorised and regulated by the
Financial Services Authority
FSA Number 308481

Government exempted Travel Agents in the legislation but with two caveats.

1. *for this to be reviewed in two years from the date of implementation*

2. *that the Insurance of baggage or Personal Effects would be included in Travel insurance for the exception to apply. This is an example of how fatuous the rules are.*

This had the effect of seriously affecting one of the main stays of our offering to Tour Operators.

Exemption Removed

The exemption for Travel Agents and Tour Operators was recently removed (with no debate in Parliament) and they are now all regulated in the same way as Brokers, Insurance Companies and the like, albeit a lighter touch as they come under a strange provision called 'CTI' (Connected Travel Insurance).

The implementation of this was cack-handed, complicated and gave no consideration to the manner in which business is done. An example of how the industry has shunned regulation is the FSA were expecting some 200-300 Tour Operators and Travel Agents to become fully licensed. In reality only 5 have applied, the remaining rely on one of the other regulatory options.

These options in themselves are over complicated and an agent may become

an appointed representative of a broker, or

an introducer appointed representative, or

an unregulated introducer, or

none of the above, or
stop selling Insurance

In addition to which there are exemptions where insurance is included in a holiday package, an area where the FSA don't even understand their own rules.

Complicated

The whole process is extremely complicated and overbearing. I don't think a day goes by where we don't have to reconsider a sales or promotional concept for fear of the

FSA. One example is Introducers may not use the word 'Recommend' but they can use 'Introduce'.

Time consuming

For a small firm such as ours it is a very time consuming exercise being a diversion from developing business and serving our customers.

Expensive

The actual cost to date for us has been £13,000 in FSA fees and consultants. This does not include the cost of my time or my staff. We could have had a new website by now for this money but we don't, we have had to pay it in fees and the FSA.

(NB. Since writing to Andrew our renewal fee for the FSA has been presented. A rise of 228% from £700 to £2300, with no change in our turnover. There is no mechanism to challenge this fee and they (FSA) are not accountable to any one)

Insurance 'Opt Out'

One of the main stays at MPI in promoting Insurance to clients (typically Tour Operators) in the manor which maximises take up rates.

Where possible we encourage an all insured route. This usually results in an improved claims experience to the underwriter thus lower premiums and typically improved cover. Where this is not possible, usually due to commercial considerations, we are able to suggest that a Tour Operator would allow a customer to 'Opt Out' of insurance.

In the last few weeks I recently presented an 'opt out' risk to underwriters who advised me this is no longer allowed under a new ruling from the FSA. So we have had to provide terms on an optional basis. The premium is 14% higher than 'opt out'! This is hardly looking after the public, being the main stay of the FSA's terms of reference.

Why they have done this is completely bizarre and has defiantly resulted in detriment to customers as they are now paying more for their insurance. This is a dis-service to my client as they will sell less insurance and a spiral of reducing take up and rising premiums will be set in motion.

We as a broker have been forced by the FSA to give bad advice, which follows most of the inept and unintelligible rules and has no regard for the way things are done, thus disadvantaging clients and the public.

Tour Operators/Travel Agents debacle

We recently renewed a contract with a Tour Operator where their sales had dropped dramatically and resulted in a substantial premium hike thus further detriment to customers.

The reason this happened is due to FSA regulations. Travel Agents are not allowed to sell the Insurance of a Tour Operator unless the necessary regulatory procedures are in place which is impossible to comply with. Another area which needs urgent attention.

Appointed Representative status

We are severely hampered from obtaining new business due to a strange rule, which restricts an agent to an AR status with only one provider. Due to the timing of printing brochures and the overlap of seasons many Tour Operators are virtually trapped with their current provider. So moving to more appropriate cover which has to be done from time to time is almost impossible.

Bi-annual reporting

We have to complete a very complicated and detailed form online to the FSA twice a year much of it involving financial information.

This has to be produced 6 weeks after the end of our financial year and again 6 weeks after the 6 month point. To obtain all the information required in performing this task, and in such a short order, puts a great strain on companies in particular small ones. In order to achieve this (and it goes to the wire each time) we have to divert resources twice a year from serving customers, which has the obvious knock on effect on reducing sales.

A company that develops software for its business is allowed under accountancy rules to place the cost of this into capital provision within the balance sheet, and this has been the case with insurance brokers until last year.

The FSA crept in rules that banned this for fully licensed firms thus putting greater strain on capital provision. This is completely unacceptable and grossly unfair. Urgent steps should be taken to stop this ridiculous practice and to bring the FSA within the law.

Replacement to FSA

It is with great relief that the Conservative Party has announced it will abolish the FSA. Please, whatever *organisation replaces it, can it have sensible, workable rules which do not interfere with underwriting or innovation, and most important the regulators must come from the industry.*

At the moment the managers overseeing the regulation of travel Insurance at the FSA are; one an ex teacher and the other a chemist. I think that says it all.

I am a committee member of the Association of Travel Insurance Intermediaries and we meet quarterly in London.

We have around 60 members most of whom are insurance brokers representing around 70% of the insurance arranged for British people travelling aboard.

May I suggest that a representative from the Treasury Committee drawing up the rules attends one of our meetings where he can explain how the rules will be implemented and affect our business and we could also take the opportunity to explain some of the issues, in order for the new set of rules to be drawn up in a manner which is workable.

I look forward to hearing from you shortly.

With Kind Regards

Yours Sincerely

Michael Pettifer

Michael A. Pettifer
Director

I am the Company Secretary of a provincial general insurance broker turning over about £3 million a year and employing 15 people.

Since the FSA commenced regulation of our line of business in 2005, I have spent more and more of my time in trying to comply with their often unintelligible rules and regulations and their fees have increased much more than the inflation rate over that period. . This year due to the FSC largesse, my fees have increased by 100% at a time when most of my suppliers have been reducing there costs by efficiencies and general competition. I therefore welcome the eradication of this superfluous body but it will be interesting to see what you intend replacing it with.

From a personal view point it is unclear to me why I am required to complete a 25+ page dossier every 6 months when all most brokers like us are doing is attending to peoples car, home or business insurance needs. To me the caveat emptor philosophy worked very well until the last government seemed to think that customers needed protection and that only their intervention was likely to ensure that happened. In the real world, which Socialists will never understand, the customer is always king. Any business that forgets that will not survive. It therefore follows that in terms of general insurance broking that regulation is irrelevant. The customer will regulate us by voting with their feet not to buy from us if we do not meet their expectations.

I would have thought that production of audited accounts annually would be more than sufficient, and indeed that information is already publicly available through Companies House, so really the general insurance division of the FSA can, in my view be simply disbanded.

Regards.

Paul Phelps
Regulated by the Financial Services Authority

To whom it may concern.

CHANGES TO FINANCIAL SERVICES AUTHORITY

I run a very small company acting as an intermediary offering woodland owners public liability cover through a broker and underwriter.

I would welcome any measures taken to change the way the Financial Services Authority operates and in particular with regard to small firms like mine and the fees they charge just to scrutinise my twice yearly returns.

I recently had to complain to FSA since they raised my annual fees from £515.46 for 2009/10 to a whopping £1,074.70 for 2010/11 without even a warning. I asked for an explanation and was informed it was "fairer" to all if everyone paid the same. Well certainly not fairer to my company!

They also told me to increase the amount of my Public Indemnity cover to £1.2 million that incurred a significant additional premium!

It is time the fee structure takes into account the very small firm/one-man-bands that operate on a small profit margin yet providing a useful service.

I do hope the new arrangements/administration will take this on board.

Roger Pittaway
Rural Arbor Products Ltd
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PLUS

PLUS MARKETS' Response to HM Treasury's Consultation 'A new approach to financial regulation: judgement, focus and stability'

EXECUTIVE SUMMARY

We welcome the opportunity to express our views on the new proposals. As we operate a Recognised Investment Exchange, the prospects of our business are closely allied to the proposed revisions to the regulatory framework.

Because of the nature of our business, we have kept our detailed responses to the questions posed in the section 'Markets and Infrastructure', namely Questions 15 to 18. However, we have also taken the opportunity to make some general comments about the operation of the new regime in terms of its potential effectiveness.

In summary, we welcome the proposed changes from the current regime but we are very concerned on two specific but vital points that are integral to the future success of our business and, more importantly, to the integrity of London's role as a globally competitive financial centre:

1) Proposed revisions to the status of Recognised Bodies

- We believe the proposals are based on incorrect assumptions and a lack of understanding as to the important and distinct role of Recognised Investment Exchanges versus authorised firms operating MTFs and crossing networks.
- We oppose any attempt to 'merge' or 'rationalise' these regimes as the roles of Recognised Bodies are quite distinct and have far less 'commonality' with MTFs and crossing networks and authorised firms than is currently assumed by the proposals in the consultation paper.
- RIEs offer primary markets, transparency, price formation and reassurance to investors that their transactions are executed on a regulated market. RIEs performed well during the credit crisis and its aftermath, posing no systemic risk or threats to financial stability.
- It is these characteristics and the generally good performance of RIEs that has prompted regulatory authorities around the world to encourage the move of trading OTC products, especially derivatives on to exchanges which offer that transparency and neutrality and open price formation.
- It is axiomatic that primary markets operated by RIEs are vital to all forms of capital raising. They also offer the opportunity for product innovation, and the expansion of the range of securities by attracting new pools of investment capital to public markets. They must be allowed to retain the initiative when it comes to the regulatory oversight of their market architecture as well as confidence in the robustness of their capital markets - perceived as associated with their RIE status.
- RIEs operate on a commercially neutral basis, do not trade on their own account, and provide reassurance to users, including overseeing the conduct of their members. They also operate statutory information sharing gateways with other official bodies and regulators.
- RIEs accept a higher level of regulatory burden whilst having statutory immunity in their decisions, although these decisions are open to judicial review.

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IN CONTRAST:

- Authorised firms such MTFs operate only secondary markets which are, in essence, parasitic price takers, using prices formed elsewhere on exchange venues to populate their own trading volumes.
- They do not create new products or lead financial innovation due to the lack of a primary function. They complete largely on price, not on investor reassurance or neutrality.
- Authorised firms have no obligations to operate in a commercially neutral fashion; they can use risk capital for their own account.
- They have no need or obligations to share information gateways, their decisions are not open to challenge by judicial review.
- These differences are, in most cases, fundamental and do not form the basis for any rationale to 'merge' the two distinct regimes.
- We can see no efficiency gains in the proposal, only a reduction in the diversity of financial institutions which make London globally competitive in financial services.
- **CONCLUSION: These proposals run counter to the imperative of financial stability and counter to the trends in EU regulation which recognise and are fully supportive of the distinct role of Exchanges/Recognised Bodies We believe strongly that there is no case under UK financial stability or likely EU regulatory initiatives for removing the status of Recognition therefore collapsing the divide between Recognised Bodies and authorised firms.**

2) The proposals to locate the UKLA in the Financial Reporting Council (FRC)

- The proposals reveal a major misunderstanding of the nature of primary market transactions. Lack of market understanding in this case will create a short cut to loss of international competitiveness for London's markets.
- The UKLA operates in a fast moving, often real time environment, requiring swift decisions in some cases and a deep knowledge of how markets operate and react. The FRC is not designed to operate in such an environment leading to some strong internal cultural differences which could hamper the UKLA's effectiveness.
- We are very concerned that the current proposals will recreate a smaller version of the tripartite system which is being dismantled in that the primary markets will be under the FRC, secondary markets will be under the CPMA and the clearing and settlement regime will be under the Bank of England.
- The FRC is concerned with the regulation of companies and their corporate arrangements and activities. The UKLA is concerned with the issuance and performance of company securities, not the companies themselves.
- The FRC's role is concerned with the activities of UK companies. The work of the UKLA covers global securities of which over 90% are not concerned with the equities of UK companies. This would be a mismatch if the UKLA was moved to the FRC.
- This will create more 'underlap' when the proposals are designed to do the exact opposite. The only location for the UKLA must be the CPMA. As a corollary point, we also see no case for the concept of an enhanced corporate regulator under BIS. There is little definition in the consultation document as which problems this proposed new regulator is trying to solve.

- Given the CPMA's consumer protection role, there is also a clear overlap with the UKLA in terms of prospectus information, disclosure and overall investor protection measures that it operates.

- **CONCLUSION: The proposal to locate the UKLA in the FRC is a retrograde step and will damage the competitiveness of London as a global financial centre. The UKLA should be located under the proposed CPMA.**

3) Overall Views

- The overall philosophy of giving the Bank of England a more close and direct role in financial stability and macro prudential supervision is clearly beneficial, given its central bank position and perspective. We do consider that there is a need for a clear link from the Bank's activities to micro prudential supervision so that overall stability can be achieved.

- We are concerned that the Bank's judgement based approach may encounter some headwinds in a more heavily operational and rules based environment. There remains a risk that tensions will arise between the respective regulated authorities in terms of accountability and cooperation as a result.

- We are concerned over the foundation and make-up of the CPMA and in particular its supervisory function – there is every reason to believe that the CPMA will inherit the deficiencies experienced in the present regime and we want to ensure that the CPMA is resourced at the front line to apply to a judgement-focused approach on the basis of adequate market understanding. Fundamental changes need to be reflected in the new landscape.

- This is particularly true in aspects of regulatory philosophy pertaining to investment risk: the new CPMA's consumer protection role could easily conflict with retail investors' desire to take investment risk on graduated basis.

- The same applies to other major areas of financial services regulation such as allowing consumers in the past to run up large personal debts but actively discouraging investors from investing in the equity securities of SMEs because they are 'too risky'. HMT itself recognises that investing (including, especially, the role of retail investors) in SMEs is vital to the UK economic recovery in its recent Green Paper on the topic.[1] This needs much more careful coordination to achieve a balanced outcome, whereby companies get equity funding and investors are permitted to assume a wide range of levels of investment risk, based on correct understanding, rather than seeking to eliminate investment risk altogether or to keep it to a minimum.

- The changes outlined in the proposals should include a renewal of understanding of how markets operate and where more coherent regulatory planning and supervision could contribute to enhancing the markets rather than constraining them. If this can be achieved, then the changes proposed will be of immense value to all concerned.

4) DETAILED RESPONSES

15. The proposed division of responsibilities for markets and infrastructure regulation.

As an Exchange, our primary concern is that the significance of market infrastructure is appreciated where they are competing priorities for the CPMA in terms of consumer protection, wholesale markets and retail markets.

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[1] HM Treasury's Consultation 'Financing a private sector recovery' July 2010

Another impact is that some Exchanges and market operators providing both trading and clearing services will be supervised by both the PRA and the CPMA (dual supervision). There is an increasing trend within the EU of Exchanges moving into the provision of clearing services (Euronext and NYSE LIFFE and the LSE for example)

This is very pertinent given the long list of foreseeable regulatory initiatives for Exchanges and market operators in the medium term (predominantly originating from the EU).

16. The possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses.

See our views set out above. We strongly oppose the rationalisation proposals as we see no benefits in terms of efficiency, commonality or a reduction in the size of rule books and a loss of market choice. There are no financial stability reasons to make these changes and if anything, they will run counter to European legislation, regulatory initiatives and structural norms.

17. Whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.

See our comments above in section 2).

Also, we believe that the CPMA's credibility may be hampered from the start by the removal of the UK Listing Authority to BIS.

We foresee particular difficulties when it comes to UK's representation and engagement with EU regulators because the CPMA will not have responsibility for the Listing function.

The Listing function is of considerable importance in maintaining the UK as a credible and competitive destination for listings.

It also should be recognised that there is also cross-over with the consumer protection brief given that within the Listing Rules.

The interests of consumers and investors are paramount when it comes to framing primary market rules and policy. Why then remove separate the UK Listing Authority from the CPMA?

18. Other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.

As stated above, we cannot see what particular problem is being addressed by creating an overarching companies regulator. The consultation paper refers to the concept, but gives little detail as to what the proposed remit would be for such a regulator beyond the existing functions of the FRC. As such, and subject to any further consultation by HMT, we see no case for such a proposal.

If anyone would like to pursue further discussions concerning the points we have made, we would welcome such an approach.

Enquiries should be addressed to:

Giles Vardey

Chairman

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Financial Regulation Strategy
HM Treasury
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SW1A 2HQ

18 October 2010

Dear Sirs

HM Treasury Consultation Paper – 'A new approach to financial regulation: judgement, focus and stability' (the "Consultation Paper")

PricewaterhouseCoopers LLP ("PwC" or "we") welcomes the opportunity to comment on the Consultation Paper. As requested we have responded to the questions that we believe are relevant to our business and experience. The response to the questions has been included in the main body of the report attached.

We have also taken the opportunity to provide some more general observations on certain aspects of the proposals; these are set out in the letter below.

Improving the regulatory framework

We agree that there were certain failures of the regulatory system during the emergence of the recent financial crisis and we support the objective of the Consultation Paper to make improvements in order to avoid similar failures in the future. We have considered all of the proposals against this overall objective and we have commented where we believe that better regulation may not ensue.

When implementing the new regulatory framework, the government and regulators should be particularly rigorous when assessing the cost and benefit implications, all potential consequences that may result and any wider economic consequences of reform, given the importance of the financial sector to the UK. For example, the following issues should be considered:

- The cost of implementing change is necessarily a secondary consideration when working towards a better regulatory model. However, for certain aspects of the proposals we suggest that a detailed cost-benefit analysis be conducted to ensure that regulatory and firm resources are deployed only where the objective of improved regulation can actually be achieved. This will be particularly critical when assessing the operational reality of disaggregating the regulatory architecture;
- There are many examples of regulatory changes having unintended consequences, which have resulted in regulatory arbitrage, market failure and loss of competitiveness for certain jurisdictions. Historically, many of these instances have occurred overseas, allowing us to

grow the financial services sector in the United Kingdom. For example, the introduction of the US Sarbanes-Oxley Act in 2002 benefitted the UK through encouraging capital flows away from the US and into the UK. Careful analysis of these reforms will be required to identify any such unintended consequences.

Moving towards judgement based regulation

We support a move towards judgement based regulation, and away from a "check box" approach; we believe that a judgement based regime, properly applied, will result in better regulatory outcomes. However, we note the inherent challenges in the design and application of any judgement-based methodology. For example, the methodology must be supported by:

- Creation and maintenance of a principles based culture throughout the organisation(s);
- Active involvement of highly accomplished and experienced individuals in setting principles, supervising and enforcing regulation; and
- Regular training and education of all people.

The regulatory bodies are likely to need to recruit additional skilled resource in order to effect successful culture change and to make a more judgement based model work effectively.

If these challenges are not overcome, there could even be a risk of future regulatory failure, through the poor application of judgement based regulation, resulting in a worse outcome than would have been achieved through a more regimented, but less thoughtful, "check box" approach. Nonetheless, we support the move towards judgment based regulation, providing that it is supported by the cultural and organisational developments that are required to implement the strategy effectively.

Our audit practice has significant experience of working successfully within a judgement based framework and we would be delighted to share more detailed experience in this area.

Statutory objectives and principles of good regulation

Under the existing regulatory framework and legislation, the Financial Services and Markets Act 2000 ("FSMA") sets out five statutory objectives that direct the regulatory activities of the FSA. The statutory objectives are supported by a set of principles of good regulation to which the FSA must have regard when discharging its functions under FSMA. The FSA's statutory objectives and principles of good regulation are set out in Appendix A.

The principles of good regulation include considerations such as:

- The international character of financial services and markets and the desirability of maintaining the competitive position of the UK; and
- The desirability of facilitating innovation in connection with regulated activities.

The Consultation Paper proposes that these considerations could be removed from the regulation setting process.

We believe that these factors, together with the other principles of good regulation, are an important part of the development of balanced regulation, although we agree that it is appropriate that they should be subordinate to overall regulatory objectives.

The financial services sector is a key part of the UK economy, contributing some 8% of UK Gross Value Added, employing over 1 million people and enabling and stimulating growth in other

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sectors. The development of an effective, respected and balanced regulatory framework is an important element of maintaining the UK's competitive position as a leading financial market. If regulation becomes imbalanced – either overly permissive or overly stringent - we will jeopardise this position, and hence the economic health of the UK.

We recognise that the principle covering innovation will need to be carefully considered. This principle should exist to support socially useful innovation, rather than overt financial engineering that generates little value for the UK economy and the wider public. We have given an example of socially useful innovation in our detailed response to Question 4.

We note that, in practice, there may be some confusion over the status of the principles of good regulation. We therefore recommend that additional guidance be published to clarify the expected actions of regulatory bodies in respect of these principles when developing new regulation.

Disaggregating the regulatory architecture and implementing the new structure

The Consultation Paper proposes that prudential and conduct of business regulation require different approaches and cultures, and thus that the Prudential Regulatory Authority (the "PRA") and the Consumer Protection and Markets Authority (the "CPMA") should be independent regulators with differing objectives. We recognise that there are valid reasons for bringing greater focus to both prudential and conduct regulation.

The FSA currently has annual revenue and costs in excess of £420 million, over 3,300 employees and the responsibility for the regulatory oversight of 29,000 firms and 165,000 individuals. The design and implementation of the current regulatory architecture took over 4 years to complete at some significant expense. The task of disaggregating this architecture will be similarly complicated and costly and we expect it will require time and additional expert resources.

The Consultation Paper also recognises that the PRA and the CPMA will need to work together in many situations, particularly in relation to firms where both authorities have a supervisory interest. It will be necessary, therefore, to create a framework which facilitates coordination and cooperation between the new regulatory bodies. This framework should incorporate a cultural attitude encouraging close liaison and a detailed modus operandi covering the practicalities of working together.

The framework should ensure that duplication is avoided, that there are no gaps in regulatory coverage and that firms have no opportunity for "regulatory arbitrage" through taking advantage of differing regulators' objectives. Functions where we believe joint operation or closely dovetailed working will be appropriate include:

- Risk assessment
- Ongoing supervision
- Enforcement
- Authorisations and permissions
- Levying fees (already contemplated in the Consultation Paper)
- Operational functions such as finance, human resources and IT.

Joint operation will not only reduce the risk of gaps and regulatory arbitrage, but will also reduce the cost of disaggregation we referred to above.

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Resolution of conflicting objectives

We expect that there will be instances where the objectives of the new regulatory bodies will conflict, in particular when taking enforcement or corrective actions. The Consultation Paper recognises this possibility and notes that, in extremis, the objectives of the PRA will be deemed superior to those of the CPMA. However, we note that the modus operandi to be established between the new regulatory bodies will need to provide a mechanism for identifying and mediating any such conflicts before defaulting to the philosophical superiority of the PRA's objectives.

The future of the UKLA

The UK Listing Authority (the "UKLA") currently resides within the FSA and is responsible for regulating access to the UK's capital markets and for setting continuing obligations for those companies with listed securities.

The Consultation Paper notes that the Government is considering whether the UKLA should be merged with the Financial Reporting Council (the "FRC"), further suggesting that any such move could be the first step to creating a powerful companies regulator, reporting into the Department of Business, Innovation and Skills ("BIS"). We note that there will be a further consultation in this regard in due course.

The UKLA currently runs a regime which strikes a balance between efficient access to the capital markets and robust reporting and regulation (often involving a degree of "super equivalence"), allowing the UK to become the pre-eminent European location for capital raising. In addition, there have been no major incidents that suggest that the UKLA's approach to regulating primary access to the UK capital markets needs reform. Whilst we acknowledge that there are certain areas where functions of the UKLA could share practice with counterparts at the FRC (for instance with respect to narrative reporting in company accounts and in prospectuses), we do not believe that combining these functions would unlock significant synergies. This backdrop does not support a case for change and therefore we question whether merging these bodies would contribute to the overall objective of improving regulation within the UK.

A move of the UKLA would also separate responsibility for primary access to capital markets from those responsible for market conduct (responsibility for which will lie with the CPMA). We believe that these two aspects of market regulation should be closely linked and that a separation could lead to poorer regulation in practice.

Finally, it is planned for the CPMA to be the UK's representative on the European Securities and Markets Authority ("ESMA"). If the UKLA were to be removed from the CPMA, the degree to which it could influence regulation in the European capital markets would be constrained. This could be particularly disadvantageous for the UK's interests, given that the new European regulatory architecture is planned to become operational from January 2011, and UK influence could be diminished at a critical stage in the development of the new EU institutions.

Maintaining influence on the European and global stage

There is a common consensus that for regulation to be effective in the future we need better communication and coordination between global, regional and national regulators. The FSA is currently regarded by many as Europe's pre-eminent financial services regulator; through the FSA, the UK has a respected voice in European and global discussions.

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The FSA is the designated competent authority under the European single market directives for banking, insurance, investment business, payment services, collective investment schemes and other financial services, including insurance intermediation. The FSA is also the competent authority under a host of other EU directives, including the Market Abuse and Prospectus Directives.

The new structure will introduce several UK regulatory authorities that do not align with the new European supervisory structure and it is not yet clear how our seats at the tables of the European regulatory bodies will be allocated, or how the competent authority designations referred to above will be delegated. Whilst this issue can be resolved by the allocation of responsibilities between the new bodies, it will be critical to ensure that splitting representation between the UK bodies, particularly in the transitional period, does not result in a loss of focus or influence in European developments.

It will be essential for HM Treasury ("HMT") and the Bank of England (the "BoE") to monitor closely European and global developments for any indication that UK influence may be diluted because of this lack of structural alignment.

The role of the auditor

The role that auditors (including PwC) should play in the future regulatory framework is already the subject of much debate, and we refer you to our recent response (dated 29 September 2010) to the combined FRC and FSA Discussion Paper DP10/3 "Enhancing the auditor's contribution to prudential regulation". We note that the Consultation Paper does not cover the role of auditors or audit firms although the responsibilities of auditors under FSMA will need to be migrated and/or amended as part of the implementation of the new regulatory framework.

[redacted]

Yours faithfully

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP

Contents

1. The Bank of England and Financial Policy Committee

1. ***Should the FPC have a single, clear, unconstrained objective relating to financial stability and its macro-prudential role, or should its objective be supplemented with secondary factors?***

We believe that the primary objective of the FPC should be to protect financial stability through identification of systemic risk and, where appropriate, addressing imbalances. However, as set out in our covering letter, in particular under the paragraph entitled "Statutory objectives and principles of good regulation" we strongly support the existence of secondary factors, to which all regulatory bodies should have regard when determining actions. These secondary factors will be an important part of the development and implementation of balanced regulation.

We note that, in practice, there may be some confusion over the status of these secondary factors. We therefore recommend that additional guidance be published to clarify the expected actions of regulatory bodies in respect of the secondary factors when developing new regulation. We suggest that particular thought be given to how the secondary factors should be applied to different aspects of the regulatory process: for instance the impact of the secondary factors on the setting of regulatory policy will be entirely differently from their impact on supervisory and enforcement decisions.

2. ***If you support the idea of secondary factors, what types of factors should be applied to the FPC?***

We suggest that, of the principles of good regulation currently enshrined within FSMA, the principles relating to "International character" and "Competition" become secondary factors to which the FPC should have regard when pursuing its primary objective. In addition, we recommend that the FPC should consider the impact of its actions:

- On the other UK regulatory bodies and their statutory objectives, including the PRA, CPMA and MPC;
- With respect to the European and global regulatory landscape so that, where appropriate, regulatory arbitrage is avoided or at least anticipated; and
- On the wider social agenda, for instance, the impact on housing access and availability which could follow from actions to slow the housing market.

In many cases, it may be determined that, notwithstanding any adverse consequences relating to the secondary factors, the FPC's course of action remains appropriate. However, we believe that the timing and proportionality of macro-prudential actions can be better calibrated if these consequences are clearly understood. In addition, the early identification of any such issues should facilitate a more effective response, where one is required.

3. ***How should these factors be formulated in legislation – for example, as a list of 'have regards' as is currently the case in the Financial Services and Markets Act 2000 (FSMA), or as a set of secondary statutory objectives which the FPC must balance?***

As noted in Question 1, there may be some lack of clarity over the status and impact of the secondary factors currently in existence. If the factors are formulated in legislation as a set of secondary statutory objectives, we believe that their status would be more easily understood; we recommend that, in addition, guidance be published to illustrate the actions that the FPC could take in responding to the secondary objectives.

2. Prudential Regulatory Authority

4. ***The Government welcomes respondents' views on:***
    - ***whether the PRA should have regard to the primary objectives of the CPMA and FPC;***
    - ***whether some or all of the principles for good regulation currently set out in section 2 of FSMA, particularly those relating to good regulatory practice, should be retained for the PRA;***
    - ***whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and***
    - ***whether there are any additional broader public interest considerations to which the PRA should have regard.***

The primary objectives of the CPMA and FPC

We believe that the PRA should have regard to the primary objectives of the CPMA and FPC. As we have explained in our covering letter, in particular within the paragraphs entitled "Disaggregating the regulatory architecture and implementing the new structure" and "Resolution of conflicting objectives", the success of the new regulatory model will be contingent on close cooperation and coordination between the new regulatory authorities.

The stipulation that the PRA must have regard to the primary objectives of the CPMA and FPC is consistent with the establishment of a culture of working together. Also, there are likely to be situations where prudential and conduct requirements overlap, or indeed conflict, and where a balance will need to be sought.

If the new bodies do not have regard for the objectives of the other bodies, there is unlikely to be an adequate framework for resolving these conflicts. Successful conflict resolution will depend on rapid identification of conflicting objectives; if the PRA is mandated to have regard to the objectives of the other regulatory bodies this should facilitate the early understanding and resolution of such conflicts.

FSMA principles for good regulation

As set out in our covering letter, in particular within the paragraph entitled "Statutory objectives and principles of good regulation", we support the retention of all of the principles for good regulation currently set out in section 2 of FSMA.

We note that the principle requiring the regulator to have regard to the desirability of facilitating innovation in connection with regulated activities could be refined to refer to "socially useful innovation", as previously referred to by Lord Turner, being innovation that supports regulatory objectives and/or provides products and services that create tangible benefits for the UK economy or wider public.

An example of such socially useful innovation was recently seen within the building society sector which developed an innovative core tier 1 instrument – Profit Participating Deferred Shares ("PPDS") to enable the raising of core tier 1 capital externally. This instrument was successfully used for the first time by the West Bromwich in 2009 which strengthened the quality of its capital when its subordinated debt holders agreed to convert their holdings into PPDS.

Systemically important institutions

When designing and implementing the new regulatory framework, the importance of focusing on those firms that are deemed to be systemically important should be emphasised. Protecting against any failure is a part of regulation, however, as has been demonstrated in recent years, failure of these firms has a far greater effect on the UK economy and public finances.

5. ***Is the model proposed in paragraph 3.16 – with each authority responsible for all decisions within their remit subject to financial stability considerations – appropriate, or would an integrated model (for example, giving one authority responsibility for authorisation and removal of permissions) be preferable?***

As noted in our covering letter, in particular within the paragraph entitled "Disaggregating the regulatory architecture and implementing the new structure", when implementing the new regulatory framework it will be important to avoid:

- Duplication of activity between the new regulatory authorities;
- Increasing the regulatory burden on firms without proportional benefit; and
- Any opportunity for regulatory arbitrage between the new regulators, for instance, through lack of clarity over who will be responsible for certain issues or risks.

In order to mitigate these risks and to increase efficiency, we support the development of an integrated model for certain regulatory functions. The degree to which integration will be possible or appropriate will vary depending on the function. For example, we suggest that:

- Authorisations and permissions be carried out by one regulatory authority, probably the CPMA. In making this recommendation, we have considered the fact that the level of prudential authorisation and permission decisions would be only a fraction of those to be performed by the CPMA (we estimate that some 3,000 to 4,000 firms will be regulated by the PRA compared to over 20,000 by the CPMA). Therefore to create a separate authorisations and permissions function within the PRA would seem inefficient;
- A consolidated register of regulated firms and approved persons be maintained by the CPMA;
- If it is not possible for one regulatory body to assume responsibility for these functions then we would encourage the regulators to explore the development of an integrated "front-end" system that would enable firms to initiate a single application process;
- Supervisory activities to be coordinated between the two new authorities, whilst noting that each regulatory authority will have individual responsibility for its own supervisory activity. However, coordination of supervisory visits will enable regulatory and firm resources to be deployed in responding properly to the most critical regulatory needs; and
- In particular, as part of the supervision process, that risk analyses of firms regulated by the PRA be carried out jointly with the CPMA, whilst recognising that the focus of risk analysis within the PRA may differ from that of the CPMA. We believe that a consistent risk analysis will facilitate a dovetailed approach to supervision and assist in appropriate prioritisation of regulatory activity.

We further suggest that cost efficiencies will be optimised if "back office" type functions are shared by the new regulatory authorities. For instance, finance, accounting and human resource functions could be provided by a shared service centre, supporting both the PRA and the CPMA.

6. ***Is the approach outlined in paragraph 3.17 to 3.23 for transfer of regulatory functions and rule making sufficient to enable the PRA to take a more risk-based, judgement-focussed approach to supervision?***

As noted in our opening letter, we support the move to a risk and judgement based approach to regulation. However, we believe that further activity beyond that outlined in the Consultation Paper will be required in order to make this move successful.

Detailed planning will be required in respect of the cultural underpinning required to implement effective judgement based regulation. The cultural shift will need to be effected through deploying resource experienced in working in a risk-based environment (additional senior level resource may need to be recruited), encouraging close coaching, supervision and review of more junior staff, and implementing a learning and development programme which supports working within a principles-based framework.

The FSA's staff currently work with a very detailed and highly prescriptive rule book; the impact of shifting these detailed rules towards sets of guiding principles, should not be underestimated. The exercise to simplify the current rulebook will be substantial. We estimate that the FSA rule book currently runs to thousands of pages and therefore resource demands (both in terms of volume of resource and capability) to simplify these rules will be significant. Finally, we note that removal of detailed rules will create a degree of uncertainty for the firms; we suggest that a careful balance between principles and more substantive guidance will need to be reached.

7. ***Are safeguards on the PRA's rule-making function required?***

We support the maintenance of the existing consultation safeguards set out in FSMA. We believe that they contribute to the development of balanced regulation which is understood and supported by all stakeholders and that they facilitate the identification, and hence avoidance, of unintended consequences of changes in regulation. To eliminate any of the current safeguards, in particular the consultation mechanisms, could result in implementation difficulties with the potential to undermine regulatory objectives.

Recent experience has indicated that, in times of crisis, it may be necessary for the regulatory authorities to act swiftly in pursuit of their financial stability objective. The new regulatory framework should include the provision for such prompt action, whilst setting appropriate safeguards for use in such an emergency situation.

Given that many of the future changes in regulation will be driven by the EU, we believe that it is important that the UK bodies, and other stakeholders, have sufficient influence to allow for these changes to be reviewed and shaped prior to their inclusion in EU Directives through the operation of suitable safeguards at the EU level.

8. ***If safeguards are required, how should the current FSMA safeguards be streamlined?***

As noted above we believe that the current FSMA safeguards are essential to achieving balanced regulation. However, we suggest that the current mechanism for the cost benefit analysis in the consultation process could be simplified to result in a simpler, quicker analysis achieving the same objectives.

9. ***The Government welcomes views on the measures proposed in paragraphs 3.28 to 3.41, which are designed to ensure that the operation of the PRA is transparent, operationally independent and accountable.***

We support the governance and oversight mechanisms proposed, in particular, the cross-membership of boards between the PRA, CPMA, FPC and MPC as this should help reduce the potential for duplication and conflict between the new regulatory bodies.

We agree with the importance of the non-executive role on the board of the PRA and the need to ensure that the non-executives have appropriate experience and background, without conflicts that could impact their objectivity.

We agree that it is appropriate for fees to be levied on firms provided they are calculated in a competitive manner.

As noted in the Consultation Paper, some of the transparency and accountability mechanisms that are included in FSMA have been omitted for the PRA. These have been included in the plans for the CPMA and are summarised in the CPMA section of the Consultation Paper (paragraph 4.36). We feel that all of the items listed in paragraph 4.36 should be replicated for the PRA, including:

- a requirement to produce an annual report to be laid before Parliament by the Treasury;
- a requirement to hold annual public meetings;
- a duty to establish consultative panels where necessary;
- a duty to maintain a complaints mechanism similar to that required of the FSA by schedule 1 of FSMA;
- decisions to be subject to appeals in the Upper Tribunal, where appropriate; and
- reviews and inquiries (along the lines of those provided for currently in sections 12 and 14 of FSMA).

In principle, we support the PRA being subject to audit by the National Audit Office ("NAO") as this will improve public accountability. However, we would like to better understand the cost and consequent benefit that will be obtained from this change and how the NAO would interact with the Internal Audit function that is currently in place.

Overall, to achieve better regulation and accountability we believe that there is a need to ensure that there is more, and not less, transparency and oversight.

3. Consumer Protection and Markets Authority

10. The Government welcomes respondents' views on:

- ***whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and FPC;***
- ***whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which;***
- ***whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and***
- ***whether there are any additional broader public interest considerations to which the CPMA should have regard.***

We believe that the CPMA should have regard to the primary objectives of the PRA and of the FPC and that the principles for good regulation currently set out in section 2 of FSMA should be retained. Our rationale in making these recommendations is set out in our response to Question 4.

11. Are the accountability mechanisms proposed for the CPMA appropriate and sufficient for its role as an independent conduct regulator?

We support the governance and oversight mechanisms proposed, in particular, the cross-membership of boards between the PRA, CPMA, FPC and MPC as this should help reduce the potential for duplication and conflict between the new regulatory bodies.

We agree with the importance of the non-executive role on the board of the CPMA and the need to ensure that the non-executives have appropriate experience and background, without conflicts that could impact their objectivity.

We agree that it is appropriate for fees to be levied on firms provided they are calculated in a competitive manner.

As we note in our response to Question 9, some of the transparency and accountability mechanisms that are included in FSMA are proposed to be retained for the CPMA and are summarised in paragraph 4.36. We support the inclusion of these mechanisms for the CPMA but recommend that similar mechanisms be implemented for the PRA. We suggest that the consultative panels to be established for the CPMA should also act as consultative panels for the PRA, recognising that a subset of the Practitioner Panel would need to be convened to debate issues relevant to the PRA.

In principle, we support the CPMA being subject to audit by the NAO as this will improve public accountability. However, we would like to better understand the cost and consequent benefit that will be obtained from this change and how the NAO would interact with the Internal Audit function that is currently in place.

Overall, to achieve better regulation and accountability we need to ensure that there is more, and not less, transparency and oversight.

12. The Government welcomes views on the role and membership of the three proposed statutory panels for the CPMA.

The Consultation Paper suggests that the CPMA should retain the two current panels required under FSMA, the Consumer Panel and the Practitioner Panel. In addition, it is suggested that the Small Business Practitioner Panel be placed on a statutory footing and retained by the CPMA.

We believe that the members of these panels should be able to demonstrate relevant experience and independence (wherever possible). In relation to the Practitioner Panel, we note the advantages that accrue from members having a degree of influence within the wider marketplace and therefore would recommend that this characteristic be considered in the recruitment process.

As part of the review of the regulatory framework, we would encourage HMT to review the objectives, operations and activities of each of the panels to ensure that they are delivering tangible benefits that are commensurate with the costs and resources incurred.

Other than as noted above, we have no specific views on the role and membership of these panels.

13. The Government welcomes views on the proposed funding arrangements, in particular, the proposal that the CPMA will be the fee- and levy-collecting body for all regulatory authorities and associated bodies.

We support the levy of fees from firms provided fees are calculated in a fair manner.

We agree that the CPMA should be responsible for the collection of fees and levies for all regulatory authorities as this should increase efficiency, reduce costs and improve transparency of the overall regulatory costs.

As we have already noted in this response, this process, along with many others, will require the regulatory authorities to coordinate and cooperate very closely.

We note that there may be a need for the regulatory authorities to monitor the degree of credit risk they face in respect of the CPMA and develop their risk management frameworks accordingly.

14. The Government welcomes views on the proposed alternative options for operating models for the FSCS.

The FSCS provides consumer protection when a firm is in default, and, as explained in the Consultation Paper, its core business is to compensate consumers for the more frequent failures of small firms such as Independent Financial Advisers.

We agree with the proposal that the FSCS should be the responsibility of the CPMA as its core business fits naturally with the scope of the CPMA's activities. However, it will be important for the PRA to work closely with the CPMA and FSCS to ensure that the role of the FSCS in the event of a failure of bank, insurer or investment bank is appropriately determined.

We believe that the main issues currently facing the FSCS are:

- The affordability of the levies for smaller firms;

- The capacity of the scheme to cope with large defaults; and
- The ability of the FSCS to enable the UK to meet its obligations under the various EU Directives which deal with compensation arrangements in different sectors of the market.

In order to overcome these issues, we recommend that the FSCS should remain a single scheme, with a cross-subsidy between different classes of levy payers. The single scheme approach should maximise efficiency and be the most cost-effective solution. In addition, without an implicit or explicit cross-subsidy arrangement, we believe that there could be situations where separate schemes would be insufficiently funded to provide adequate consumer protection. We understand that further consideration may be given to:

- pre-funding in respect of the banking class of the FSCS; and
- Future EU developments on compensation schemes.

We will consider responding to any specific consultations on these areas in due course.

15. The Government welcomes views on the proposed division of responsibilities for markets and infrastructure regulation.

We understand the principle between the separation of responsibility for regulating exchanges and other trading platform providers (CPMA) from that for regulating CCPs and settlement systems (BoE). However we note the operational difficulty of making this separation and that the regulators will need to work together effectively and efficiently, with coordinated supervision.

16. The Government welcomes views on the possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses.

We note that the current FSMA regimes for regulating exchanges, trading platforms and clearing houses treat exchanges and clearing houses (regulated directly by the FSA) differently from trading platforms owned by regulated firms. This inconsistency presents the risk of regulatory arbitrage.

We suggest that any rationalisation of the current regimes should remove this inconsistency.

17. The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.

As noted in our covering letter, we believe that the UKLA is currently an effective regulator. We do not see obvious synergies between the UKLA and FRC and question whether a merger of those bodies would contribute towards to the development of better regulation. In the absence of compelling benefits to justify a change to the existing arrangement, we recommend that in the new regulatory framework the UKLA be housed within the CPMA organisational structure; this would be consistent with the current position of the UKLA within the FSA organisational structure.

This positioning would ensure that the regulator with responsibility for primary access to the capital markets (the UKLA) would be an integral part of the regulator with responsibility for market conduct (the CPMA). We believe that these two aspects of market regulation should be closely linked and that a separation could lead to dysfunctionality and poorer regulation in practice.

We note also that it is planned for the CPMA to be the UK's representative on the European Securities and Markets Authority ("ESMA"). We believe that it is critical for the UKLA to have adequate representation on ESMA; were the UKLA not to form part of the CPMA, its voice would necessarily be diluted and it would be constrained in the degree to which it could influence the development of regulation within the European capital markets.

It is relevant to consider the inherent differences in scope and approach which exist between the FRC and the UKLA. For example, the FRC regulates a wide spectrum of UK companies, not just listed companies, and therefore has a much broader scope than the UKLA who focus on companies seeking to access the UK capital markets (the majority of whom are based outside of the UK). Additionally, the FRC typically employs a retrospective approach to regulation, with much activity focussed on review, challenge and discipline. The UKLA, in contrast, operates a more immediate approach, working with those companies seeking to access the capital markets to review and, if appropriate, approve their investment circulars, typically within a six to eight week time frame.

There are functions within both organisations that have similar roles, notably the:

- Issuing of guidance on narrative reporting in annual reports (Accounting Standards Board) and in listings documents (UKLA);
- Enforcing narrative reporting in annual reports (Financial Reporting Review Panel) and in listings documents (UKLA);
- Issuing of guidance on the role of auditors in relation to listings documents (Auditing Practices Board); the reports issued by those auditors form part of the UKLA's assessment of suitability for listing; and
- Publication of the UK corporate governance framework (Financial Reporting Council); the UKLA monitors the governance and financial reporting capability of those companies seeking to raise capital in the market.

However, we believe that in each of these areas, the current regulatory bodies take account of each other effectively without undue duplication. We do not believe that combining these functions would unlock significant synergies and in fact, since the objectives of these functions are very different, combination could potentially lead to inefficiencies.

18. The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulators.

As we note in our response to Question 17, we believe that all aspects of financial market regulation should be housed within the CPMA organisational structure. We note that further discussions and consultations on the future of the UKLA are expected and we will respond to these in due course.

5. Crisis Management

19. Do you have any overall comments on the arrangements for crisis management?

The future regulatory framework for crisis management is already the subject of much debate, and we refer you to our separate response to the HMT consultation paper "Establishing resolution arrangements for investment banks" which sets out our views on this area. Some of our most experienced insolvency practitioners have been in discussions with HMT and other relevant authorities to provide guidance in this area.

Given the ongoing consultation referred to above, and the breadth of this subject, we have responded only briefly to the crisis management consultation questions in this paper. We look forward to a continued dialogue with you as future crisis management arrangements are developed.

We believe that the change in regulatory framework proposed in the Consultation Paper and, in particular, the move of responsibility for prudential regulation under the BoE and the increased focus on macro-prudential risk, should better equip the regulatory authorities to identify and respond to future systemic risk.

The recent crisis demonstrated the need for administrators and insolvency practitioners to have flexibility to respond to unique situations. When reviewing the arrangements for crisis management, HMT should ensure that there is no erosion of this flexibility which could impede the ability of regulators and practitioners to protect financial stability and achieve effective and efficient resolutions.

20. What further powers of heightened supervision should be made available to the PRA and the CPMA, and in particular would there be advantages to mandatory intervention, as described in paragraph 6.17?

We believe that a critical element of a response to any future crisis will be the timing of any mandatory intervention or implementation of recovery and resolution plans. Any trigger points should be clearly defined, and the framework should ensure that there is sufficient frequency and transparency of reporting to allow trigger points to be identified.

We note that whilst there may be circumstances where swift mandatory intervention is necessary, we believe that it should remain the option of last resort.

21. What are your views about changes that may be required to enhance accountability within the SRR, as described in paragraphs 6.21 to 6.24?

We have no specific comments on accountability within the SRR.

6. Impact Assessment

22. Annex B contains a preliminary impact assessment for the Government's proposals. As set out in that document, the Government welcomes comments from respondents on the assumptions made about transitional and ongoing costs for all types of firm. In particular, comments are sought from all types and size of deposit-taking, insurance and investment banking firms (including credit unions and friendly societies), and from groups containing such firms.

We have not provided specific feedback on this question.

a) The Financial Services and Markets Act 2000 (FSMA) gives us five statutory objectives:

- **Market confidence** - maintaining confidence in the financial system;
- **Public awareness** - promoting public understanding of the financial system;
- **Financial stability** - contributing to the protection and enhancement of the UK financial system
- **Consumer protection** - securing the appropriate degree of protection for consumers; and
- **The reduction of financial crime** - reducing the extent to which it is possible for a business to be used for a purpose connected with financial crime.

b) In pursuing our functions under FSMA, we are required to have regard to additional matters that we refer to as 'principles of good regulation'. These are:

Efficiency and economy

The need to use our resources in the most efficient and economic way:

The non-executive committee of our Board is required, among other things, to oversee our allocation of resources and to report to the Treasury every year. The Treasury is able to commission value-for-money reviews of our operations. These are important controls over our efficiency and economy.

Role of management

The responsibilities of those who manage the affairs of authorised persons:

A firm's senior management is responsible for its activities and for ensuring that its business complies with regulatory requirements. This principle is designed to secure an adequate but proportionate level of regulatory intervention by holding senior management responsible for risk management and controls within firms. Accordingly, firms must take reasonable care to make it clear who has what responsibility and to ensure that the affairs of the firm can be adequately monitored and controlled.

Proportionality

The restrictions we impose on the industry must be proportionate to the benefits that are expected to result from those restrictions:

In making judgements in this area, we take into account the costs to firms and consumers. One of the main techniques we use is cost benefit analysis of proposed regulatory requirements. This approach is shown, in particular, in the different regulatory requirements we apply to wholesale and retail markets.

Innovation

The desirability of facilitating innovation in connection with regulated activities:

This involves, for example allowing scope, where appropriate, for different means of compliance so as not to unduly restrict market participants from launching new financial products and services.

International character

The international character of financial services and markets and the desirability of maintaining the competitive position of the UK:

We take into account the international aspects of much financial business and the competitive position of the UK. This involves co-operating with overseas regulators, both to agree international standards and to monitor global firms and markets effectively.

Competition

The need to minimise the adverse effects on competition that may arise from our activities and the desirability of facilitating competition between the firms we regulate:

These two principles cover avoiding unnecessary regulatory barriers to entry or business expansion. Competition and innovation considerations play a key role in our cost-benefit analysis work. Under the Financial Services and Markets Act, the Treasury, the Office of Fair Trading and the Competition Commission all have a role to play in reviewing the impact of our rules and practices on competition.

PRISM
COSEC

Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

15th October 2010

Dear Sir,

CONSULTATION RESPONSE: A NEW APPROACH TO FINANCIAL REGULATION, JULY 2010

Thank you for the opportunity to comment on the above consultation.

Prism Cosec is a company secretarial and corporate governance practice that seeks to promote integrity and effectiveness within the boardroom. Our principal activity is in assisting London Stock Exchange-quoted domestic and international companies on company secretarial and governance matters. A number of our clients are members of the FTSE 100 and FTSE 250 indices.

Our comments relate to the Markets & Infrastructure section, question 17; '*The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS*'.

We do not support the proposal to merge the UKLA with the FRC.

Many international companies have chosen to admit equity to trading on London's capital market. An important factor in making that decision is the unique corporate governance model that exists in the UK, where there is a clear separation of roles between the regulatory supervision function (the UKLA / Listing Rules) and the development of corporate governance principles under a comply or explain approach (the FRC / UK Corporate Governance Code).

The separation of regulatory compliance and guardianship of corporate governance principles in the UK provides the flexibility to accommodate a wide variety of companies located in many different jurisdictions when it comes to meeting their particular needs from capital markets participation. It is this adaptability that constitutes a major competitive advantage for London.

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To maintain the competitive advantage described above requires a clear distinction in cultural approach and a proactive tension between the 'rules-based system' and the 'comply or explain-based system'. The regulator needs to be concerned with monitoring and enforcement against a set of rules. The guardian of corporate governance principles needs to be more concerned with setting policy against current best practice given that 'enforcement' is through stakeholders and the market. The natural tension created between the two philosophies provides the balancing mechanism.

Merging the UKLA with the FRC could lead to a homogenous culture developing and remove the balancing mechanism. There would be a natural temptation over time to tend towards a fully rules-based system rather than towards a principles-based, comply or explain approach. Such 'regulatory creep' would move the UK towards a more prescriptive (and costly) footing akin to that administered in the US by the SEC and which incorporates Sarbanes-Oxley measures.

Ultimately, a move by the UK towards a more prescriptive system could reduce the attractiveness of London's capital markets to international companies, increase the costs of compliance to those companies admitted to the UK capital markets and so damage the competitiveness of those markets in attracting new international business.

Lastly, it would appear from the consultation that there is no evidence presented to suggest that the current separation of roles between the UKLA and the FRC is proving ineffective. We would query the need for a wholesale change to existing arrangements, where the case for such change is not driven by a failure in the current approach.

It is for these reasons that we would encourage you to reconsider the proposal to merge the UKLA with the FRC.

I hope our comments prove helpful. Please do not hesitate to contact me if you require further assistance.

Yours sincerely

Andrew Wallace

Andrew Wallace
Prism Cosec

HM Treasury Consultation Paper
A New Approach To Financial Regulation: Judgement, Focus and Stability

Prudential plc

Introduction

1. Prudential plc is an international financial services group with significant operations in the UK, Asia and the United States. Our purpose is to promote the financial well-being of our customers and their families, with a particular focus on saving for retirement and income in retirement. Our portfolio of well-known and respected brands has attracted approximately 25 million customers worldwide. Prudential plc is also one of the UK's largest institutional investors and therefore our comments reflect our views both as a leading financial services group as well as a major institutional investor.

2. We welcome the opportunity to respond to 'A New Approach To Financial Regulation' and look forward to continued engagement with HM Treasury and the new authorities as the proposals take shape over the next two years. In view of the scale of the changes, both structurally and in changes to the FSMA rules, we would request that the insurance and asset management industries continue to be consulted at each stage of the process to ensure a mutually successful outcome.

Executive Summary

3. We respond below to the specific questions in the consultation paper but we wish to highlight the following key points:

Outcomes focused

4. Prudential plc supports the rationale for change proposed by the Government, in which a focus on the macro-economic environment and greater coordination between macro and micro prudential regulation will help to ensure that risks developing across the financial system are identified early and appropriate intervention takes place. However, we ultimately regard the quality and outcomes of regulation - alongside ongoing effective cooperation between the new authorities - as more important than the precise institutional arrangements.

Judgement-based supervision

5. For Prudential plc, it is particularly important that the new, more intrusive 'judgement-based' approach taken by the authorities should be proportionate, recognising the different business models of insurers and asset managers compared to banks. Insurers and asset managers play a key role supporting growth as long-term investors in infrastructure and as potential sources of non-bank lending. Regulatory responses to the banking crisis that are inappropriately read across to insurers will, of course, impact our ability to fulfil this role in the wider economy.

Clear Roles

6. We believe that more detailed thinking is needed to address the complexities of a proposal which, in its current form, has the potential for duplication, uncertainty, lack of accountability or due process, inefficiencies and unnecessary costs. In particular, each agency should have clear objectives and accountabilities with open communication channels. This would help to avoid regulatory arbitrage and improve upon the structural weaknesses of the tripartite model identified in the consultation paper. To avoid unnecessary duplication, we would support the creation of a single function reporting to the PRA that could potentially carry out authorisations and approvals for all firms. This would help to allay concerns that large groups subject to CPMA and PRA supervision - such as Prudential plc - will encounter confusing and conflicting regulatory processes.

Micro-prudential supervision

7. The powers of the Bank of England - and particularly the Governor - are wide-ranging, with the role of HM Treasury and the accountability to Ministers and Parliament of relatively less importance in the proposals. The requirement for the Governor to brief the Chancellor once every six months is insufficient and the important scrutinising role of Parliament must not be ignored. While the focus of the Bank will be on financial stability, it is also uncertain that any regulatory action in support of this objective will take account of the potential adverse impacts on the competitiveness of the UK financial services sector and on the development of financial sector products. Additionally, it is proposed that the powers of the PRA could be implemented with less consultation. Taken together, these changes represent a marked shift from the certainty of the FSMA regime, and require more attention to ensure that due process is followed. It is especially important that the approach taken towards insurers by the PRA is proportionate, recognising that because of their business models – as distinct from banks' – insurers and asset managers are not systemically significant.

International issues

8. There is a need to ensure continued and coordinated engagement on international issues. Focus on domestic reforms should not be at the expense of UK financial services losing out in key international debates (e.g. Solvency II). In particular, the UK's ability to influence European legislation must not be weakened by the split of representation between the PRA and the CPMA. It is vital that the PRA and CPMA are given sufficient expertise, time and resources as regulation is increasingly set at an EU level. This will be especially important as greater powers, such as the ability to implement binding technical standards, will be given to the new European regulatory authorities from 1 January 2011. As these new supervisory bodies take shape, London's role as a leading international financial centre should not be compromised by domestic regulatory change.

Regulation of Markets

9. The regulation of markets is perhaps the most fragmented area of the consultation proposals. The recommendation is that regulation should be split between the Bank of England (regulation of settlement systems and central counterparty clearing), the PRA (supervision of investment banks), and a markets division within the CPMA (wholesale market conduct regulation). This has the potential for considerable uncertainty and inefficiency. The consultation paper also suggests that the UK Listings Authority (UKLA) should become part of the Financial Reporting Council (FRC). We believe that the UKLA and FRC are distinct entities and there is insufficient rationale for a merger. We do not, therefore, support this proposal. The alternative suggestion is for the UKLA to be part of the CPMA. In this case, it should be recognised that the UKLA has a role as the listings authority for all sectors and should consequently be a separate entity within the CPMA.

Treatment of Groups

10. There needs to be further clarity around how groups such as Prudential plc will be treated. It is unclear, for example, if asset manager subsidiaries will be solely regulated by the CPMA for both prudential and conduct of business activities, or will incur additional regulation by the PRA as part of the wider group. While we support the prudential regulation of our subsidiary asset manager by the CPMA, considerable care must be taken to ensure that this regulation is not duplicated by the PRA. In addition, if the rules are not applied consistently to subsidiary asset managers compared to independent asset managers, this could result in advantages for some firms over others.

Consumer Protection

11. The role of the CPMA is less well-defined than the PRA. Its function as a 'consumer champion' is potentially at odds with the neutral role of a regulator and creates a risk that the CPMA will be dominated by consumer protection issues at the expense of the markets

division where the regulatory focus on efficiency (rather than protection) is very different. Whilst we agree that the regulator should have a high regard for consumers' interests, it is also important to recognise that the role played by internationally competitive markets in serving these interests helps to drive economic growth. Long term product innovation, particularly for savings products, can also contribute to growth in the economy and the CPMA should have regard to these factors when shaping its role and objectives.

Changes to FSMA rules

12. It is important that the objectives of the regulators are balanced, that the rules are consistently applied across organisations, and that safeguards remain in place. The focus should be on enhancing the quality of supervision rather than on making new rules. As the new structures take shape, it is essential that insurance regulation and supervision is effectively resourced when compared with other parts of the financial services sector. It is also vital that regulators are not distracted from their core duties of supervising firms during the current period of unprecedented international, European and UK regulatory change. Additionally, we would regard an extended period of uncertainty as undesirable. The timetable is extremely challenging and it is important for all concerned to make these proposals work and to resolve any ambiguities quickly.

Financial Services Compensation Scheme

13. We would support an end to cross-subsidisation - in which insurers are called upon to contribute to the costs of bank failures - as suggested in the paper. We also oppose any move towards a pre-funded scheme as the long-term nature of insurance products means that an immediate call on FSCS funds is unlikely to be required. We look forward to further consultation on the structure of the FSCS expected later in the year.

<u>Questions for Consultation</u>

The Bank of England and Financial Policy Committee (FPC)	Prudential plc response
1 Should the FPC have a single, clear, unconstrained objective relating to financial stability and its macro-prudential role, or should its objective be supplemented with secondary factors?	We would support the overriding focus on financial stability, but would also welcome the recognition of secondary factors (outlined in our response to question 2 below). This is particularly important as the FPC's macro-prudential interventions will have wider economic and fiscal implications.
2 If you support the idea of secondary factors, what types of factors should be applied to the FPC?	The FPC should take into account the objectives of the PRA and CPMA as the conduits for implementing FPC policy. Further, it should be mindful of the implications of the use of macro-prudential tools on economic drivers relevant to overall GDP growth and wider policy goals such as increasing the level of savings and investment in the economy.
3 How should these factors be formulated in legislation – for example, as a list of 'have regards' as is currently the case in the Financial Services and Markets Act 2000 (FSMA), or as a set of secondary statutory objectives which the FPC must balance?	We would support a strengthened form of the current 'have regards' measures. In particular, taking into account the "international character of financial services and markets and the desirability of maintaining the competitive position of the United Kingdom" is absolutely vital for increasing growth and protecting jobs in a sector which represents 10.1% of the UK economy. We would also support a proportionate approach to decision-making by the FPC, including an explicit requirement to take into account the differing business models and diversity of sectors.
Prudential Regulation Authority (PRA)	**Prudential plc response**
4 The Government welcomes respondents' views on: • whether the PRA should have regard to the primary objectives of the CPMA and FPC; • whether some or all of the principles for good regulation	We believe it is crucial that the various bodies do not make policy decisions that undermine the objectives of the other bodies. The PRA should be required not to undermine the primary objectives of the CPMA and FPC. This is particularly important in view of the interdependencies of the institutions and the potential for overlap identified in the paper.

currently set out in section 2 of FSMA, particularly those relating to good regulatory practice, should be retained for the PRA; • whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and • whether there are any additional broader public interest considerations to which the PRA should have regard.	While the main focus of the PRA will be to promote the stable and prudent operation of the financial system, it should do this in a way that is consistent with principles of good regulation (e.g. using resources in the most efficient way and full consultation including cost-benefit analysis). We would also regard competitiveness, innovation and public interest considerations as important for the UK financial services industry, and so any regulatory action in support of the primary objective of financial stability should have regard to potential unintended consequences for these areas. As noted in response to question 3, due to its specific remit to act on individual firms, the PRA should also be mindful of the implications of the use of its powers for the differing business models and diversity of sectors, particularly insurers and asset managers.
5 Is the model proposed in paragraph 3.16 – with each authority responsible for all decisions within their remit subject to financial stability considerations – appropriate, or would an integrated model (for example, giving one authority responsibility for authorisation and removal of permissions) be preferable?	We agree with the assumption in the paper that there is the potential for significant overlap, particularly for large cross-border institutions regulated by the CPMA and PRA such as Prudential plc. For example, there is the potential for multiple risk frameworks and a duplicated ARROW process if the responsibilities of the authorities are not clearly defined. Conversely, there is also the potential for each authority to be unclear where its boundaries of responsibility start and end, resulting in regulatory voids. To avoid unnecessary duplication/gaps, costs and inefficiencies, we would support a single function reporting to the PRA that could carry out authorisations and approvals for all firms.
6 Is the approach outlined in paragraph 3.17 to 3.23 for transfer of regulatory functions and rule making sufficient to enable the PRA to take a more risk-based, judgement-focussed approach to supervision?	There is a need to ensure stability throughout the process so that there is a seamless transition to the new rules and so that the business plans of firms are not disrupted because of regulatory uncertainty. We do not think it would be in the interests of either the authorities or industry to have wholesale change which only results in duplicated and inefficient interventions across common supervisory frameworks. We would therefore support measures which help the transition process and reduce the potential for overlap. The authorities must keep in mind that the current proposal to modify

	FSMA in light of a more judgement-focused approach raises the potential for a diluted rulebook that is applied inconsistently across organisations according to the will of the PRA. In addition, in view of the new supervisory powers of the European Supervisory Authorities, the PRA's ability to adopt a different approach regarding EU regulation will be severely constrained and it will need to show that it has properly implemented EU legislation. In particular, the PRA will need to take account of binding technical standards at an EU level.
7 Are safeguards on the PRA's rule-making function required?	There is a need to ensure that the PRA is subject to sufficient safeguards, so that rule-making is not imposed without consultation on the industry. While the consultation proposals intend to retain the FSMA safeguards for the CPMA, they do not do so for the PRA. Indeed, a more intensive approach to supervision means it is even more important to have sufficient checks and balances in place. For example, it may be useful to require the PRA to consult before rules are drafted to ensure that there is an open and transparent dialogue with industry. There should also be a formal appeals and complaints process, and effective procedures should be put in place to deal with any conflicts in rule-making between the PRA and CPMA.
8 If safeguards are required, how should the current FSMA safeguards be streamlined?	As covered in our answer to question 7 above, we do not believe that safeguards should be streamlined.
9 The Government welcomes views on the measures proposed in paragraphs 3.28 to 3.41, which are designed to ensure that the operation of the PRA is transparent, operationally independent and accountable.	The PRA should be operationally independent, but subject to sufficient safeguards with appropriate accountability mechanisms. In relation to the PRA management structure, we would welcome life insurance and asset management expertise on the PRA Board and/or advisory group to ensure that the needs of the industry, alongside banking, are taken into account as micro-prudential measures are developed and applied over the coming years.

	The consultation paper does not provide any detail on how insurance regulation will be structured in the PRA and whether it will have sufficient insurance expertise at both a technical and senior management level. It may be appropriate, for example, to appoint a head of insurance supervision at the same level as the head of banking supervision.
Consumer Protection and Markets Authority (CPMA)	**Prudential plc response**
10 The Government welcomes respondents' views on: • whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and FPC; • whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which; • whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and • whether there are any additional broader public interest considerations to which the CPMA should have regard.	We agree that the CPMA should have regard to the primary objectives of the PRA and FPC. As mentioned in our answer to question 4, this is particularly important in view of the interdependencies of the institutions and the potential for overlap identified in the paper. We would also support the retention of the 'have regards' measures, including those relating to innovation and competitiveness. Whilst it is right that the regulator has high regard for consumers' interests, it is also important to recognise that the role played by internationally competitive markets in serving these interests helps to drive economic growth. The development of long term savings products will also be beneficial for both customers and the economy, and should not be undermined by regulatory change. Furthermore, it is crucial that successful cross-border organisations, such as M&G Investments, continue to be able to compete internationally and that the UK does not lose out to other countries wishing to increase their domiciled funds. The financial services sector represents over 10% of the UK economy and it is our view that regulatory action should recognise the wider potential impact on jobs and growth. We would also support the public interest measures, particularly as Prudential plc is a strong supporter of financial education. We have a long standing partnership with pfeg (the personal financial education group) and we have also worked with the Specialist Schools and Academies Trust to develop 'Adding up to a Lifetime', a multi-media schools resource that provides over 20 hours of interactive learning aimed at developing financial skills.
11 Are the accountability mechanisms proposed for the CPMA appropriate and sufficient for its role as an independent conduct	We agree with the accountability mechanisms outlined in the paper. We support making the CPMA subject to audit by the National Audit Office and ensuring that the CPMA

regulator?	conducts a full cost-benefit analysis prior to the introduction of new rules. The CPMA must also be mindful that its more intrusive approach is proportionate, recognising that insurers such as Prudential plc were a source of stability and strength in the recent banking crisis.
12 The Government welcomes views on the role and membership of the three proposed statutory panels for the CPMA.	We agree with the proposals to include the Consumer Panel, Practitioner Panel and Small Business Panel within the CPMA, as they will provide an important and diverse contribution to policy development inside the new structure. To work effectively they will need to be well resourced so that they can provide robust recommendations that contribute effectively to the decision-making processes of the new authorities.
13 The Government welcomes views on the proposed funding arrangements, in particular, the proposal that the CPMA will be the fee- and levy-collecting body for all regulatory authorities and associated bodies.	We agree that a single organisation should collect fees for both the CPMA and PRA, and associated bodies, as this will help to avoid confusion and overlap. This would avoid potential confusion, particularly around the treatment of complex groups in which the regulation of subsidiaries such as asset managers is currently unclear.
14 The Government welcomes views on the proposed alternative options for operating models for the FSCS.	We support a single FSCS organisation which operates independently of the CPMA. As suggested in the paper, we would also support an end to cross-subsidisation and look forward to further FSCS consultation expected later this year to address this issue in more detail. We agree that insurers and asset managers should not contribute to the costs of the failure of banks, given the different risk profiles of the businesses. We are also opposed to any move towards a pre-funded scheme as the long-term nature of insurance products means that an orderly wind-down of clients' policies can take place over a long period in the event of financial failure. This means that an immediate call on FSCS funds is unlikely to be required. Changes to the FSCS should recognise that insurers have a different business model to banks and the introduction of any changes should therefore be proportionate.

Markets and Infrastructure	Prudential plc response
15 The Government welcomes views on the proposed division of responsibilities for markets and infrastructure regulation.	The new structure creates the potential for confusion for markets, investors and organisations. As regulation is dispersed across the CPMA and PRA, it is unclear if the new regime will sufficiently recognise the complexity of wholesale markets and whether it will be able to effectively and efficiently regulate the asset management subsidiaries of larger organisations. It is currently unclear how groups such as Prudential plc will be treated, particularly individual entities within groups (e.g. asset managers). If the rules are not applied consistently to subsidiary asset managers compared to independent asset managers, this could result in benefits for some firms over others. While we support prudential regulation of our subsidiary asset manager by the CPMA, considerable care must be taken to ensure that this regulation is not duplicated by the PRA, given that other parts of the Group will fall within the PRA's remit. Regarding the regulation of markets within the CPMA, we agree with proposals for a structurally distinct approach in which market issues are considered separately to retail issues. This would ensure that the focus on efficiency within markets can be given appropriate weighting alongside consumer protection.
16 The Government welcomes views on the possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses.	The regulation of central counterparty (CCP) clearing houses and settlement systems by the Bank could create confusion, as they will be regulated separately from the markets in which they operate. This potential fragmentation needs to be addressed to ensure certainty and clarity in the FSMA regime going forward.
17 The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.	This proposal would bring together aspects of corporate governance and disclosure in one place, but in practice each authority has a range of functions and operates very differently. Their distinct roles should be recognised and a merger may not be the best way of bringing about the synergies indicated in the paper. The proposal would:

	• result in further regulatory fragmentation, by separating primary market regulation from the regulation of trading by the CPMA; • exclude the UK from having representation on primary market regulation issues within the new European Securities and Markets Authority (since the UKLA would not be represented through the CPMA); • potentially reduce the attractiveness of the UK as a venue for issuers and investors. In view of these outcomes, we do not believe that UKLA should be merged with FRC. However, we recognise that the UKLA has a role as the listings authority for all sectors and should therefore be a separate entity within the CPMA.
18 The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.	We await the consultation regarding the need for a new companies regulator in order to give full consideration to this question.
Crisis management	**Prudential plc response**
19 Do you have any overall comments on the arrangements for crisis management?	It is important that the UK authorities continue to play an active role in EU and international developments in relation to crisis management. The financial services sector is diverse, and this should be recognised with appropriate and proportionate policy responses that recognise the differences between the business models. In particular, insurers should not be regarded as systemically significant for the following reasons: • insurers do not have a financial, structural or liquidity mismatch between assets and liabilities; • they are not key participants in the payment systems which act as critical infrastructures in the economy and potential channels of contagion effects in cases of bank failures; and

	• they are not typically subject to the sort of short-term counterparty risks that some banks became exposed to due to their high dependency on inter-bank lending. The insurance and asset management sector also has a positive role to play in support of the global recovery, and should not be stifled by the unprecedented pace and cumulative impact of international and EU policy reforms aimed at addressing the banking crisis.
20 What further powers of heightened supervision should be made available to the PRA and the CPMA, and in particular would there be advantages to mandatory intervention, as described in paragraph 6.17?	In view of the proposed more intrusive regulation, any further powers must be appropriate and proportionate with sufficient safeguards. Increased mandatory tools may have the unintended consequence of removing the options open to regulators in unforeseen crisis management situations. In addition, as discussed in the answer to the previous question, it should be recognised that the different business model of insurers means that any failure is unlikely to result in contagion effects on the financial system as a whole.
21 What are your views about changes that may be required to enhance accountability within the SRR, as described in paragraphs 6.21 to 6.24?	The operation of the SRR is critical to resolving failing institutions and preventing contagion, and we would support any changes that would improve the clarity and overall effectiveness of the regime. There is a particular concern, however, regarding the role of the Bank as lead resolution authority at the same time as the new PRA has a role in putting a failed institution into the SRR. As a representative of both the Bank of England and the PRA, this creates a potential conflict of interest for the Governor. An independent PRA Chair could be an appropriate solution. In view of these issues, any changes to the SRR - including an extension of its powers - should be subject to wide and detailed consultation.
Impact Assessment	**Prudential plc response**

22 Annex B contains a preliminary impact assessment for the Government's proposals. As set out in that document, the Government welcomes comments from respondents on the assumptions made about transitional and ongoing costs for all types of firm. In particular, comments are sought from all types and size of deposit-taking, insurance and investment banking firms (including credit unions and friendly societies), and from groups containing such firms.	Clarity around how Prudential plc will be regulated - particularly for our asset management business - is critical to determine the likely costs. The setting up and ongoing development of new regulators indicates a potential for significantly increased costs. Throughout the consultation process and formation of the new institutions, the authorities must be fully transparent regarding their costs and should ensure that expenditure is carefully controlled.

Publish What You Pay

October 2010

Treasury consultation: A new approach to financial regulation
Submission from Publish What You Pay

Background

Publish What You Pay (PWYP) is a network of over 600 civil society organisations from resource rich developing countries and international non-governmental organizations working to ensure that oil, gas and mining revenues are used for economic development and poverty reduction.

In framing our response to the consultation on financial regulation, we would like to draw your attention to historic legislation passed by the United States Congress on 15 July 2010.

Provision 1504 (Disclosure of Payments by Resource Extraction Issuers) contained in the new Dodd-Frank Wall Street Reform and Consumer Protection Act requires oil, gas and mining companies that file an annual report to the Securities and Exchange Commission (SEC) to publicly report how much they pay each government for access to their oil, gas and minerals[1]. This information must be presented annually on a country- and project-specific basis.

This new listing requirement was passed because it is seen to be of value both to investors (in valuing companies and assessing risk) and to citizens in producing countries who will be able to use this information to scrutinize the collection and use of revenues generated by natural resource extraction. The US government has announced that it is actively seeking to work with other jurisdictions to ensure similar requirements are enacted and will make this a priority in the year ahead.[2] The Hong Kong stock exchange had already updated its stock listing rules in June 2010 to require new applicant oil, gas and mining companies to disclose "payments made to host-country governments".[3]

We are calling on the UK Government to introduce an equivalent transparency requirement for extractive industries listed on the London Stock Exchange.

Revenues from natural resources represent the largest transfer of money from wealthy to poorer nations and the single best opportunity for economic growth and poverty alleviation. In 2008, for example, exports of oil and minerals from Africa, were worth roughly $393.9 billion, nearly 9 times the value of international aid to the continent ($44 billion), and over 10 times the value of exports of agricultural produce ($37.9 billion). Instead of contributing to development and prosperity however, natural resources too often fuel conflict and corruption leading to increased poverty and suffering. The failure of companies to disclose the payments they make to foreign governments for access to natural resources can allow corrupt government officials to loot their states' wealth for their own personal benefit without the knowledge of their citizens.[4]

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[1] http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h4173enr.txt.pdf
[2] http://www.whitehouse.gov/the-press-office/statement-press-secretary-transparency-energy-sector
[3] http://www.hkex.com.hk/eng/rulesreg/listrules/mbrulesup/Documents/mb96_miner.pdf
[4] Organisations such as Global Witness produce expert reports on embezzlement and corruption associated with the natural resource sector: www.globalwitness.org

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***Question 17**. The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.*
***Question 18**. The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator*

Regardless of the financial architecture for the UKLA and the companies regulator, reform to the financial regulations presents an opportunity for the Government to introduce a requirement for the UKLA to require **all** extractive industry companies (both UK and foreign) listed on the London Stock Exchange (LSE) to disclose their payments to foreign government, as in Section 1504 of the US Dodd-Frank Wall Street Reform and Consumer Protection Act.

UKLA regulations to require country-by-country and project-specific financial reporting by all extractive industry companies listed on the LSE would be good for investors, for business , for the UK government and for international poverty reduction:

<u>Good for business:</u>

- Major British companies listed with the US SEC like BP would benefit from a level playing field. Some of the world's largest energy and minerals companies, such as Gazprom, Anglo American and Xstrata, would only be captured via a rule change on the London Stock Exchange.

- Transparency provides a stable investment climate for business. Investors are more able to assess the risk of investing in a company if they know where it is paying taxes and how much it is paying. In a world of growing competition between companies from North America, Europe, Asia and other regions, transparency favours the best companies and deters their less scrupulous competitors.

- Companies in the extractive industries need to protect themselves from false or unfair accusations and blame-shifting by host governments that can tarnish their reputations and lead to hostile operating environments, litigation and loss of investment.

- British corporations often represent the public face of the UK abroad and need to be seen as fair players by the people of countries where they operate and the world at large.

- When disclosure of payments leads to better management of government resources, companies will receive fewer demands from host communities for 'social services' and may see less need for corporate philanthropic projects in developing country contexts. Shell and Exxon spent $64 million combined on community development projects in Nigeria in 2001. Payment transparency is a low cost way to reduce the amount of such programs.

- Properly managed resource-rich economies feature higher and broader-based economic growth. This would increase the stability of developing countries and create new markets for investors and companies, including in the non-natural resource sectors.

<u>Good for investors:</u>

- Investors need to be able to assess the risks of their investments. They need to know where, in what amount, and on what terms their money is being spent in often very high-risk operating environments that may be politically unstable, corrupt, and with a history of civil conflict fuelled partly by natural resources. Secrecy of payments carries bottom-line risks for investors. F&C Asset Management states, "Investors have a strong interest in ensuring that the oil, gas and mining companies in which they invest have access to resources and can operate in a stable and predictable business climate, especially at a time when the most attractive reserves are often in politically unstable regions."[5]

- Investors should know how much money is being invested "up front" in oil, gas and mining projects. Oil companies often pay large "signature bonuses" to secure the rights for an oil field, long before the first oil is produced - in addition to the capital investment. In Angola, $500 million is not unusual for a signature bonus and single fields can cost over $2 billion to develop. These costs take years for companies to recoup through their production sharing arrangements with host companies. It is in the interest of investors to know the amount and timing of payments in high-risk operating environments.

- In countries where there is a history of mismanagement of extractive industry revenues, new governments may come to power on platforms of nationalization or expropriation of foreign assets. Where revenue payments *are* disclosed, there is a better chance that natural resource wealth will be better managed for the benefit of all, reducing risks.

- Reputational risk for companies could affect investors – for instance, by holding an extractive industry company in a portfolio that could be target of campaigning. Companies need to protect themselves from false or unfair accusations and blame-shifting by host governments that can tarnish their reputations with the investor community and the general public. Disclosure of payments is one way to address reputational risk. Extractive companies are less likely to be asked to pay bribes, and transparency over payments is less likely to leave them open to allegations of bribe paying.

Good for the UK government:

- Money from natural resources often dwarfs money from ODA. In the UK the burden on our aid budget could be reduced if developing countries were able to achieve sustainable growth by mobilising their own natural resources. Transparency would help by making sure these resources are better-used in order for countries to move beyond aid dependency.

- UK energy security will benefit from the fostering of stable, long-term, and mutually-beneficial relationships with oil producing nations.

- The British people want to know that their government and corporations are not contributing to the corruption, conflict, poor governance, and unmitigated poverty that too often afflict resource-rich countries in the developing world.

- The UK (along with the USA) will establish itself as a world leader in the movement to promote transparent business practices as part of the fight against corruption and poverty.

Good for poverty reduction

[5] http://www.accpf.org.uk/investment/inv_pdf/reo4q06.pdf F&C Asset Management, REO Report, 4th Quarter, 2006.

- Corruption within host governments increases the potential for global economic and political instability in the form of civil unrest, Failed States, terrorism, and economic and humanitarian crises. Transparent business practices are an important step in combating corruption and the instability it fosters.

- Transparency means citizens are better able to hold their governments to account, ensuring natural resources generate benefits for the whole country rather than being misdirected into the hands of a select few.

- Resource-endowed countries have a window of opportunity right now in which to convert natural resource wealth into lasting benefits for their citizens and a more stable world; the resources will not last forever.

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