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

8 September 2011

Dear Sir/Madam

A new approach to financial regulation: a blueprint for reform

Introduction

The Direct Marketing Association (UK) Limited (DMA) is Europe's largest trade association in the marketing and communications sector, with approximately 800 corporate members and positioned in the top 5% of UK trade associations by income. The total value of direct marketing to the UK economy is estimated to be £72.5 billion. This comprises three separate figures; £43.3 billion on expenditure on direct marketing media and activities, £16.7 billion on employment and £12.5 billion on overheads resulting from employment (The Value of Direct Marketing 2010 published by the DMA). The DMA represents both advertisers, who market their products using direct marketing techniques, and specialist suppliers of direct marketing services to those advertisers - for example, advertising agencies, outsourced contact centres etc. The DMA also administers the Mailing Preference Service, the Telephone Preference Service and the Fax Preference Service. On behalf of its membership, the DMA promotes best practice, through its Direct Marketing Code of Practice, in order to maintain and enhance consumers' trust and confidence in the direct marketing industry. The Direct Marketing Commission is an independent body that monitors industry compliance. Please visit our website www.dma.org.uk for further information about us.

The DMA welcomes the opportunity to respond to this consultation by HM Treasury on A new approach to financial regulation: a blueprint for reform. The DMA would like to provide comments on a few issues.

1) The current regulatory regime

The DMA is a member of the Committee of Advertising Practice (CAP) and the Broadcast Committee of Practice (BCAP) and is fully supportive of the self-regulatory and co-regulatory schemes under these organisations with the Advertising Standards Authority enforcing the rules. The existing arrangement whereby the ASA and the FSA co-operate on financial promotions should be maintained by the Financial Conduct Authority (FCA).

2) Product Intervention Rules

The DMA agrees with the Government that the proposed new power for the FCA to intervene quickly and decisively when it considers that a product or product feature is likely to result in significant detriment to consumers, could impose a significant impact on firms. It welcomes the proposal that the FCA will be required to consult on and publish a statement of policy governing the conditions in which the FCA may make such product intervention rules. It also agrees that the maximum period for such temporary rules should be 12 months and that if the FCA wants to make such temporary rules permanent it would need to follow its normal rule-making procedure.

3) Financial promotions power.

The DMA believes that this new power to ban or demand changes to advertising and marketing communications could have a significant impact on firms. There needs to be more clarity about how and when the FCA can exercise this power. The DMA is pleased that the FCA will allow for written representations from the firm in question before publishing details of the action.

4) Co-operation with FOS and other organisations

The DMA welcomes the proposal that the Financial Ombudsman Service (FOS) will have a statutory duty to pass information on to the FCA. It would also like to ask that the FCA considers whether or not the Direct Marketing Commission and the Advertising Standards Authority should also be able to formally refer issues for the FCA's attention.

The DMA is a member of the Advertising Association. We have reviewed the Advertising Association's own response to this consultation and fully support it. Please contact the writer of this letter if you have any further queries. The DMA looks forward to working with HM Treasury as the plans progress.

Yours faithfully.

James Milligan
DMA Solicitor
The Direct Marketing Association (UK) Limited

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Financial Regulation Strategy
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Our ref: FSAB11
Your ref:

8 September 2011

Dear sirs

Financial Services Bill

We are a small compliance and complaint investigation consultancy concentrating on ensuring that small firms regulated by the Financial Services Authority meet their regulatory obligations in a manner that is fair to both them and their customers.

We welcome the decision of the Government to reform financial services regulation. It is quite clear that the proposed changes, in particular the establishment of the Prudential Regulatory Authority are intended to address the failure of the Financial Services Authority.

We also understand the need to guard against the possibility of widespread misselling.

However, we have grave concerns that, in doing so, it has failed to properly safeguard those small businesses, in many cases sole traders, that include our market.

Last year, the Prime Minister made clear that the Government intended to combat the so called "compensation culture". Whilst we appreciate that foremost in Mr Cameron's mind at the time was those who attempt to claim compensation for a supposed health and safety deficiency, it is a fact that those inclined to seek to profit by making claims are not particular about what the supposed reason for the compensation is. They will just as happily seek their gains from financial services firms.

Of course those who have genuinely suffered as a result of a failure on the part of a financial services firm. They should have a straightforward means of seeking redress that provides them with an "equality of arms".

We do not think it is appropriate to expect a consumer to but forward a complex legal argument in order to win their case and think that all the evidence available from both sides should be considered, not simply whatever the complainant can muster. So we support the concept on which the Financial Ombudsman is founded.

However, in our experience, the concept is far different from the reality. For small firms in particular, there is no such “equality of arms”.

We believe the principle that “he who asserts must prove” has been sacrificed on the altar of consumer protection. In our experience, we find the Financial Ombudsman Service too ready to give the benefit of the doubt to consumers and fails to properly consider whether an assertion that they were “risk averse” may now be made solely with the benefit of hindsight.

We also find that, in reaching its conclusions, the Financial Ombudsman Service frequently ignores crucial FSA rules. In particular:

- COBS 9.2.5R (A firm is entitled to rely on the information provided by its clients unless it is aware that the information is manifestly out of date, inaccurate or incomplete)
- COBS 2.4.6R(2) (A firm will be taken to be in compliance with any rule in this sourcebook that requires it to obtain information to the extent it can show it was reasonable for it to rely on information provided to it in writing by another person)
- COB 2.3.3R (A firm will be taken to be in compliance with any rule in COB that requires a firm to obtain information to the extent that the firm can show that it was reasonable for the firm to rely on information provided to it in writing by another person.)

Our clients are small businesses – partnerships, sole practitioners or family businesses. They are reliant on their businesses for a living. They do not have infinite resources and are not able to run large compliance departments. Given that the FSA handbook has the force of law, we do not believe it is equitable that the Financial Ombudsman Service should be able to simply set aside a defence that the handbook provides.

We are also concerned that our clients, and similar firms, are denied the protection of the “long stop” granted in Section 14B of the Limitation Act 1980 to all other types of business. The justifications for this are well rehearsed and two-fold – Parliament did not make provision in the Financial Services and Markets Act 2000 for a long stop and therefore did not intend it to apply and that it can take many years for the consequences of taking out a long term investment to become apparent.

Both these arguments are, though, flawed. It is not a surprise that Parliament did not make provision for a long stop within the Financial Services and Markets Act because there was no need. It was already present in existing legislation. There is no such provision within the Legal Services Act 2007 either, yet Solicitors are permitted to rely on the long stop.

The argument is, in any case, misleading because the reality is that Parliament did indeed consider the regulation of financial services at the same time as it introduced the long stop. Although it was not until the Financial Services Act 1986 was passed that there was any bespoke regulation of financial services and the Limitation Act was already in place, Section 14B was inserted by the Latent Damage Act 1986. Both pieces of legislation are referred to in the Queen's Speech that year.

Of course, it is true that it may take many years for a loss to come to light but that is equally true of work carried out by a solicitor. A faulty conveyance may cause a problem until the customer comes to sell a property, perhaps several decades later, whilst I covenant can last as long as 80 years and a solicitor's negligence not come to light until a problem arises.

With this in mind, we think it reasonable to ask why an IFA should be denied a protection granted to a solicitor?

We know this causes considerable distress to retired advisers who find it difficult, if not prohibitively expensive to obtain run off cover. If a complaint is received many years later, when no documentation exists then an award of up to £150,000 could be awarded against a retired adviser who could then lose everything.

We are extremely concerned at the distress this will cause on such individuals who will probably be elderly and have no opportunity to recover from an award made in respect of an allegation which they are no longer able to properly defend.

Sadly, we believe that if this situation is allowed to prevail, **it is only a matter of time before we see a former IFA driven to such despair that they take their own life**. We will take no satisfaction in seeing our prediction come to pass and very much hope we are wrong but feel that our hope is far less realistic than our expectation.

The Financial Ombudsman Service also charges an IFA a fee of £500 per case in excess of four in any one year, whether or not the complaint is upheld – even, in many cases, where it decides it has no jurisdiction and, to all intents and purposes there is no case to answer.

It has been argued that the four "free" cases will mean that most small firms will not incur such fees. However, this overlooks the fact that if the firm conducts its business via a "network" it is the network, not the individual firm that is entitled to the four cases and the individual adviser must pay in all cases.

Furthermore, the publicity surrounding so called misselling scandals leads to large numbers of speculative complaints and even very small firms find they have more than four cases taken to the Financial Ombudsman Service.

S136 (2) (2) of the Legal Services Act, details the equivalent situation for Solicitors. It says:

"The rules must provide for charges payable in relation to a complaint to be waived (or wholly refunded) where—
(a)the complaint is determined or otherwise resolved in favour of the respondent, and
(b)the ombudsman is satisfied that the respondent took all reasonable steps to try to resolve the complaint under the respondent's complaints procedures."

We think IFAs should be subjected to the same treatment. This is fairer on the individual IFA.

Furthermore, the fee is only payable if it is apparent that the respondent carried out a proper investigation before either rejecting the complaint or, where necessary, offered appropriate redress. If the Ombudsman concludes that the firm reached the wrong decision or only reached the right one by luck rather than judgement. We think this is a really powerful incentive to firms and would lead to much fairer consumer outcomes and less need for involvement of the Financial Ombudsman Service.

We referred above to the award limit of £150,000 which will apply to complaints received by the Financial Ombudsman Service after the end of 2011. Whilst we accept that there should be a reasonable and inexpensive means for consumers to seek redress we clearly securing high calbre staff will be expensive. Given the high level of qualification now required to practice as an IFA (all IFAs practising beyond the end of 2012 will be required to achieve a relevant QCA level 4 qualification) we would question whether personnel who have not achieved that qualification have the necessary expertise to adjudicate and, for disputes about advice given many years ago, the necessary historical understanding of the market at the time.

Such knowledge and expertise is unlikely to be secured cheaply and the potential consequences of a series of wrong decisions is such that we think the limit is far too high in respect of what boils down to a dispute between two individuals, rather than one individual and a large corporate entity.

We also note that the current requirement for a written acceptance of an Ombudsman's decision by a complaniant is being abolished. We think it is reasonable to allow this in exceptional circumstances but see no good reason why a written response should not ordinarily be required.

We are also concerned that the complainant will no longer need to reply within a specified timescale. We think that is unfair because it will mean that the IFA is unable to achieve “closure” on the matter.

We do, however, appreciate there may be exceptional circumstances where a complainant does not respond in time. Nevertheless, we think the Financial Ombudsman Service should implement the rules, not write them.

In summary, we very much support the principle that consumers should be entitled to fair treatment and should not be disadvantaged because they do not have specific knowledge and may not be able to present their case as clearly as the firm they are complaining against.

However, in making legislation, Parliament needs to make sure that it, and any person to whom it delegates decision making powers, is always mindful of the fact that most small IFAs also have limited resources as well and can all too easily fall victim to speculative, or even fraudulent, claims and the application of a “one size fits all and always has fitted all” approach.

IFAs and mortgage brokers are not the same as banks, insurance brokers.

We do not believe the current legislation, even with the proposed changes, achieves a proper balance for small independent firms. For that reason, we feel that we must oppose it but we would make clear that we are more than happy to play a full role in finding an approach that balances and protects the legitimate rights and expectations of both consumers and small firms.

Yours sincerely

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Peter Turner CeRCC, CeRCH
Director

White Paper: A Blueprint for Financial Reform

EMCAS is one of the UK's leading financial claims management specialists, since the company's inception in 2003 EMCAS have helped over 350,000 customers pursue complaints regarding mis-sold or ill advised financial products. EMCAS currently take on the complaints of c5,500 consumers per month, a figure which is steadily increasing, as such we have a vested interest in the government's Blueprint for Financial Reform and welcome many of its proposals.

We particularly welcome the government's proposals regarding consumer redress and mass claims as outlined in section 2H of the most recent White Paper and in section 6 of the earlier (February) paper.

We agree that access to fair & effective redress is an important protection for consumers. In our experience, the Financial Ombudsman Service (FOS) offers a valuable service for customers by resolving complaints impartially (and importantly free of charge to the consumer) where they cannot be resolved in the first instance.

While the internal complaint handling procedures of regulated firms (in particular, banks) are inconsistent and often demonstrably flawed; the FOS is arguably the most important part of the existing framework for consumers in terms of redress procedures.

EMCAS works on behalf of thousands of customers whose complaints are referred to the Financial Ombudsman Service and in the majority of cases we and our customers have found the FOS' service to be user friendly, transparent, generally consistent and a very necessary alternative to the courts.

However, with the onset of more and more mass claims such as those referred to in the white papers, coupled with inconsistent complaint handling and often resistance from banks and other regulated firms; the FOS has become less effective and this is at the detriment of the consumer. Customers regularly find that they have to wait for an extended period of time (upwards of 12 months in many cases) before a case is reviewed by an adjudicator and there is very little contact during this time. Further, cases which require a full Ombudsman review take considerably longer due to the immense pressure which the FOS is currently under.

Consultation Question 8

Backlogs at FOS caused by mass claims have created a barrier to redress for many consumers with valid complaints as has been highlighted in industry commentary and press over the past 18 months. This does not suit the FOS' purpose and we therefore welcome the proposals as outlined.

However, the ideology by which the proposals specific to consumer redress are driven is not dissimilar from that which governs current working relationships between the regulator and the FOS. Currently, the regulator and the FOS regularly share information "behind closed doors" and the FOS (and other interested parties) can invoke the "Wider Implications" process in cases of widespread consumer detriment.

This is an important process for consumers and, if used to escalate matters to the regulator (with its new powers under S.404) can, in theory, be beneficial to many consumers.

We believe that it is important that the roles of the regulator and FOS are separate and that the FOS can remain operationally independent of the regulator. We also believe that the FOS (and other parties) have access to information and experience which will be valuable to the regulator in tackling widespread issues. Therefore, the proposal to place the FOS under a duty to share relevant information with the Financial Conduct Authority (FCA), which the FCA will be required to consider in fulfilling its consumer protection objective, is a sensible evolution of the existing processes.

However, we would welcome clear guidance as to what the government or the regulator deems to be “relevant information” as well as how and when this information should be shared in the interest of consumers. The risk is that if the FOS or another party is placed under a “duty” to share information without clear guidelines on how and when to do so, the process could be ineffective. Similarly, we would encourage the government or the regulator to set out clearly *how* the regulator should consider such information in fulfilling its consumer protection objective.

The current “wider implications” procedure essentially offers the same process for sharing information as that which is outlined in the bill but is not clearly defined and is therefore ineffective.

Regarding the government’s consideration of giving “other parties” a clear, statutory role in this process: a criteria or similar such set of rules should be agreed to determine which types of organisation would be included in the process. There are certainly a number of consumer facing bodies which could support this initiative provided that they are carefully chosen and that the sharing of information is effectively managed. This would help to mitigate the risk of the regulator being burdened unnecessarily with having to investigate “issues” which may not be suitable for this process.

Question 9

Our view is that the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing widespread consumer detriment and preferred course of action would increase transparency and be beneficial for regulated firms and consumer groups alike. However we are concerned that the FCA does not currently possess the skill sets to make this work.

In cases where the FCA does not consider a product or process to be faulty, this sort of clarification would help to diffuse potential mass claims which would otherwise have to be dealt with by the FOS. However, where products or processes then change and this is at the detriment of the consumer, the FCA must be able to review its decision and have the flexibility to amend its decision.

Similarly, this would help to clarify the regulator’s position on matters affecting large numbers of consumers and by setting out its decision clearly, the regulator can offer guidance for firms and consumers on how to settle complaints and compensate those who are affected. This would also support any action taken by the regulator to use its new powers under S.404.

We are grateful for the opportunity to comment on these issues and we look forward to seeing how these proposals develop and would be delighted to have further opportunities to offer our comments.

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London, 9 September 2011

Dear Sir/Madam

A new approach to financial regulation – the blueprint for reform

This response is provided on behalf of Euroclear UK & Ireland Limited (***EUI***) which, as you will be aware, operates the CREST system, the UK's securities settlement system. EUI welcomes this opportunity to respond to the consultation regarding the proposed new approach to financial regulation set out in the June 2011 paper (the ***consultation***).

Summary of key responses

In summary, EUI wishes to make the following key responses to the consultation document:

- there remains uncertainty regarding the regulatory framework and proposals for oversight of EUI. We would welcome the opportunity to discuss this further with HM Treasury;
- the draft legislation entails a fundamental reform of the current Recognised Body (***RB***) arrangements (with these reforms confusingly referred to as 'technical changes' in the consultation). No case at all has been made for these changes. We are very concerned that such radical and unnecessary reform is being made in this way and are concerned that unnecessary and unexplained reform in this area will undermine the distinctive nature of the RB regime. The current arrangements are well established, successful and have a proven track record, including through the financial crisis;

- the draft legislation also entails a radical change to the current Uncertificated Securities Regulations arrangements, with a wide new rule, guidance and code making power without any procedural restraints. No deficiencies in the current arrangements have been identified and no case has been made for this change. We are concerned that such unnecessary reform is being made to what is a long established and successful set of arrangements for the dematerialised holding and settlement of securities.

We set out below EUI's detailed responses.

Reform of the Recognised Body arrangements

The RBs previously discussed in detail with HM Treasury, the FSA and the Bank the proposal to abolish the RB arrangements. Although the draft legislation does not abolish the regime, it does proceed with a number of significant modifications which result in a radical reform. These reforms are confusingly, and incorrectly, referred to as 'technical changes', and include:

- an entirely new rule making power for the appropriate regulators;
- watering down of the procedural requirements for the making of directions in respect of RBs;
- new powers of public censure and fining;
- new powers of information gathering and investigation, including powers to require skilled persons reports and to carry out investigations.

As with the original proposal to abolish the arrangements entirely, EUI is very concerned that these changes fail to understand the nature of the RB regime and only serve to undermine it. RBs are systemically important and this is reflected in the regulatory permissioning architecture of FSMA, with a distinct regulatory status under Part 18.

The nature and status of RBs is now unclear and it is increasingly difficult to distinguish the arrangements from those for authorised firms (removing this distinction was the intention of the original abolition proposal). We consider these changes will reduce the effectiveness of the RB regime by calling into question the previous clear and distinct role of RBs.

We have asked for greater detail on the rationale for these changes, although none has been provided. We have also asked for greater detail on any actual issues or regulatory failings that have resulted from the existing successful arrangements as we are not aware of any. The short statement in the consultation that the reforms will be 'more efficient' and 'more responsive' are not at all clear.

The proposals should either be subject to a proper review, analysis and transparent consultation, or they should not be taken forward.

Detailed comments regarding proposed changes to the Financial Services and Markets Act

We set out below certain more detailed comments on specific aspects of the draft Bill.

Schedule 17A

As a general comment, the approach taken of adding a new schedule to FSMA, which in turn applies, with varies complex additions, omissions and modifications, various provisions of FSMA in relation to the Bank of England is complex and lacks transparency. The approach masks various modifications and discrepancies between the RB arrangements for RIEs and those for RCHs. EUI considers a more straightforward, transparent and direct approach should be taken which treats all RBs in the same manner.

Notification requirements

Section 293 would require EUI to notify both the Bank of England and the FCA regarding changes to RIEs it provides services to and changes to criteria when determining to whom it will provide services. EUI considers such notifications should only be made to the Bank of England as regulator of RCHs.

Memorandum of understanding

Part 1 of new Schedule 17A relates to memorandums of understanding between the FCA, Bank of England and the PRA. These provisions would be better placed in FSMA itself rather than in a schedule relating specifically to Bank of England powers. The memorandua are significant aspects to ensure effective regulatory coordination and relate to all three regulators.

ESMA seat

As we have noted previously, cooperation and coordinated action between the FCA and the Bank of England is essential in relation to the FCA's ESMA seat. This is particularly the case given that the FCA has no oversight role in respect of Recognised Clearing Houses. EUI therefore considers paragraphs

1(2) and 2(2) of Schedule 17A should explicitly require the memorandums of understanding to deal with ESMA coordination arrangements.

Suspension of instruments from trading

Paragraph 8 of new Schedule 17A requires the FCA to notify the Bank of England when requiring an RCH to suspend or remove a financial instruments from trading. RCHs don't operate trading facilities and we therefore do not see that the FCA would ever be able to seek to require an RCH to suspend trading. In any event, we do not think an RCH is an 'institution' within the meaning of section 313A and the FCA therefore has no such power.

Rule making arrangements

Paragraph 10 of Schedule 17A applies section 138K with modifications. As noted above, close cooperation between the Bank of England and the FCA is essential. EUI therefore considers that the Bank of England should consult with the FCA prior to making rules (as the PRA is required to do).

Information gathering and investigations

No explanation is provided for the extension of section 165 to RBs (and this provision is not noted in the consultation). The Bank of England already has extensive powers regarding notification requirements under section 293. EUI does not consider section 165 should be extended to RBs.

New powers in respect of investigations are made in relation to Recognised Investment Exchanges directly in Part XI. However, for RCHs paragraph 13 and 14 of Schedule 17A apply those provisions with a number of modifications and omissions. No explanation is given as to why one regime is applied to RIEs and another to RCHs. EUI is concerned that inconsistencies in approach will undermine the integrity of the RB regime and consider that the provisions should be applied in the same manner to all RBs.

Annual report

Paragraph 29 of Schedule 17A imposes a requirement to make a report in respect of the discharge of the Bank of England's functions under Part 18 (by applying paragraph 19 of Schedule 1ZB). EUI considers that the provisions in relation to consultation (paragraphs 20 and 21) should equally apply to ensure the same levels of transparency and consultation for the Bank of England as for the PRA.

Reform of the Uncertificated Securities Regulations arrangements

As we noted in our previous responses, EUI is already subject to: the detailed requirements of the USRs, FSMA requirements, the Recognition Requirements, the REC sourcebook, Banking Act requirements, the Bank of England's 14 Principles of Oversight for Payment Systems (with potential additional codes and guidance under the Banking Act), the Settlement Finality Regulations and CPSS/IOSCO Principles.

It is entirely unnecessary and disproportionate to add a further new rule, guidance and code making power for the Bank of England under the USRs. No case at all has been made for this change. No deficiencies in the existing USRs arrangements (which have been in place since 1995) have been identified and no explanation is provided as to what gaps in the regulatory framework, if any, need to be covered by such an addition.

We do not see that such further rules, guidance and codes could add anything to the existing multiplicity of requirements applicable to EUI. We would therefore suggest that further complexity to the regulatory framework should be avoided and this proposal not taken forward.

If, despite the lack of any case for this change, a new rule, guidance and code making power is to be added, EUI considers it essential that the powers are subject to procedural requirements to ensure transparency, legitimacy and the opportunity for comment. We see no reason that this rule making power under the USRs should not be subject to the same arrangements as the new rule making power under the Recognition Requirements (ie subject to the detailed provisions of Part 9A of FSMA).

Immunity under the Uncertificated Securities Regulations

As noted in our previous response, EUI welcomes the intention to clarify settlement system operator immunity. EUI considers that the opportunity should be taken to rectify the long standing lacuna in the immunity provisions applicable to EUI by providing for immunity in performing functions as an approved Operator under the Uncertificated Securities Regulations (to bring the USRs into alignment with the equivalent immunity in relation to the discharge of its regulatory functions as a recognised clearing house).

If you have any queries with regard to the contents of this response, please do not hesitate to contact us.

Yours faithfully

David Whitehead
Company Secretary
Euroclear UK & Ireland Limited

FairPensions™
The campaign for responsible investment

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Friday 2 September 2011

To whom it may concern,

FairPensions welcomes this opportunity to respond to the consultation *'A new approach to financial regulation: the blueprint for reform'.*

Introduction

FairPensions (FairShare Educational Foundation) is a registered charity established to promote responsible ownership practices by pension providers and fund managers. FairPensions champions greater transparency and accountability to the millions of people whose long-term savings are managed by institutional investors and other professional agents. FairPensions believes that responsible investment helps to safeguard investments as well as securing environmental and social benefits.

We work primarily with pension funds and their investment managers, and as such our comments focus primarily on questions relating to the FCA. However, we also make some comments about the proposed PRA.

In general, we welcome the government's proposed approach. However, we have two key concerns, both of which have been alluded to in our previous responses:

- We continue to have concerns about the 'consumer responsibility' principle which we do not believe are fully addressed by the draft Bill.
- We continue to be concerned that investment governance and responsible ownership may fall between the cracks of the new regulatory architecture, despite its importance both to outcomes for consumers and to preventing the build-up of systemic risk.

These and other issues are elaborated in our response to the specific questions below.

The Charity Awards 2010 Highly Commended

Question 4: Do you have any comments on the objectives and scope of the PRA?

We agree with the PRA's insurance objective and believe it is right that this objective should be focussed on the protection of policyholders and potential policyholders. We also welcome the government's indication that the PRA's responsibilities in relation to policyholders will need to be exercised in close co-ordination with the FCA.

Our particular interest lies in the specific case of pension savers as policyholders. We are concerned that this group may be particularly vulnerable since they bear the investment risk on their savings but are not protected by the same stringent legal duties and governance structures that exist in trust-based pension arrangements. We believe that the duties of insurance companies towards their policyholders may need to be strengthened and have made representations to the FSA on this matter (see attached paper). We therefore believe that this is a particularly important area for co-ordination between the PRA and FCA, and would welcome proposals from the government to supplement the co-ordination MOU in ensuring effective consultation. See also our response to Question 13.

It is an odd consequence of the redrafting of the PRA's objectives that the FCA now has an objective of "*protecting and enhancing the integrity of the UK financial system*", including *"its soundness, stability and resilience",* but the PRA has no such objective. We would question whether the proposed new section 2B(3) of FSMA is sufficient to reflect the PRA's intended role and focus, or whether the promotion of financial stability continues to be deserving of an objective in its own right.

We continue to have concerns about the drafting of the regulatory principles, particularly in relation to consumer responsibility. Please see our comments in response to Question 6.

Question 5: Do you have any comments on the detailed arrangements for the PRA?

As indicated in our previous response, we are disappointed by the decision not to retain a Consumer Panel for the PRA, particularly given the responsibility it is being given for the protection of policyholders. Retaining a requirement to consult with industry but not with those whose capital and financial wellbeing is at stake seems at odds with the government's stated aim of creating a more robust and effective regulatory system.

We believe that this decision renders even more crucial the government's recognition that the PRA's engagement with industry must be transparent – not for the sake of the regulated community itself, but rather in order to mitigate the risk of regulatory capture. Transparency is vital not just on the PRA's processes for consultation but also on the operation of those processes: ie. which entities are making representations to the PRA, on what issues, and how the PRA has engaged or responded, whether formally or informally.

Question 6: Do you have any views on the FCA's objectives?

We welcome the reordering of the FCA's objectives so as to give priority to the consumer protection objective rather than the efficiency and choice objective. We believe this better reflects the government's stated intentions for the FCA.

However, we continue to have concerns about the principle of consumer responsibility which we do not feel are fully addressed by proposed new section 1C(2) of FSMA. Indeed, to an extent the law recognises that the principle of 'caveat emptor' is inappropriate in financial services: this is precisely why fiduciary duties apply to agents responsible for managing other people's money. As indicated in our previous consultation responses, it is impossible to eliminate the information asymmetries that characterise financial services, and therefore to arrive at the conditions necessary for informed consumer choice to be a reliable tool for achieving fair and efficient outcomes.

This is particularly true in the case of long-term savings vehicles such as pension products, where, as former FSA Chairman Howard Davies has noted, *"there is little that investors can do by way of withholding their business, and, by the time the effect of this conflict is evident, it is likely to be too late for investors to act."*[1] We therefore consider that the principle *"consumers are responsible for their decisions"* can be accepted only with significant qualifications. In particular, we would suggest that the Bill should explicitly qualify, or indeed disapply, this principle in relation to long-term investment products, for the reasons given above. The particular vulnerability of consumers of such products is not adequately captured either by proposed section 1C(2)(a), which deals with investment risk, or 1C(2)(b), which deals with consumer experience and expertise.

We continue to believe that the issue of investor stewardship and governance should be accorded greater priority within the regulatory framework and that the FCA's remit might benefit from an explicit requirement to 'have regard' to, for example, the importance of promoting effective stewardship of listed companies by institutional investors. Alternatively, the FCA's rule-making powers in relation to shareholder rights and responsibilities could be strengthened.

Question 7: Do you have any views on the proactive regulatory approach of the FCA?

We strongly welcome the proactive approach detailed both in this White Paper and in the FSA's subsequent paper, '*Financial Conduct Authority: Approach to Regulation',* published in June. As indicated in our previous response, we believe that more robust tools, such as the proposed product intervention power, clearly offer benefits to consumers which far outweigh the likely reduction in choice.

We believe that the FCA's proposed approach to product regulation is complementary to the focus on firm culture and governance pursued through its 'Treating Customers Fairly' initiative. We believe that these factors remain crucial to consumer outcomes and would only caution that the enhanced focus on early intervention to prevent mis-selling should not lead to a correspondingly weaker focus on ongoing intervention to ensure that conflicts of interest are properly managed and that firms are putting clients' interests first. In this regard, see also our comments on the importance of investment governance in response to Question 13.

Question 8: What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?

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[1] Sir Howard Davies, *'Conflicts of interest for banks, auditors and law firms',* in Clark (ed.), 2005/06, *'Conflicts of interest: Jurisdictional comparisons in the law and regulation for the financial services, auditing and legal professions'*, European Lawyer Reference.

Question 9: What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?

We welcome these proposals, which we believe will make a significant contribution to the FCA's ability to investigate and deal with potential or actual consumer detriment. This would also provide an appropriate channel for consumer groups and others to raise matters of concern, thus perhaps helping to address the 'inequality of arms' between consumer groups and regulated entities.

Question 12: Do you have any comments on the governance, accountability and transparency arrangements proposed for the FCA?

We are somewhat concerned that the existence of three practitioner panels and only one consumer panel in a regulator intended to be a "strong consumer champion" may send out the wrong message. We recognise that different groups of practitioners have different needs and interests; however, as we have pointed out in our previous responses, the same is true of consumers. The consumer panel is expected to represent an enormously wide range of consumers of vastly differing products (from mortgages to unit trusts to pension products), with different levels of experience and expertise, different levels of risk exposure, etc.

We suggested that it might be appropriate to specify the range of interests and/or expertise which must be represented on the panel to ensure that particular sub-groups of consumers are not neglected. It seems to us that a similar approach could have been adopted in relation to the practitioner panels, and that this might have resulted in a more proportionate and balanced framework. In our experience, the FSA's engagement with regulated entities is already far wider, deeper and more extensive than its engagement with consumers and civil society organisations; indeed, FSA officials privately acknowledge this. We are somewhat concerned that the new regulatory architecture may not mark the fresh start we had hoped for in this respect.

It might be appropriate for the consumer panel to be larger than the respective practitioner panels in order to redress any perceived imbalance. We also continue to believe that there would be value in measures to ensure that the consumer panel represents an appropriately wide range of interest and expertise, as outlined in our previous responses.

Question 13: Do you have any comments on the general coordination arrangements for the PRA and FCA?

Co-ordination between the PRA and FCA is important not just because of its potential to reduce burdens on dual-regulated firms, but because of its contribution to effective regulation. As we have argued previously, it is vital that in seeking to address the 'cracks' created by the previous system, the government does not inadvertently create new gaps in regulation. Effective co-ordination – not just between the PRA and FCA, but also with other relevant regulators such as the Financial Reporting Council (FRC) and The Pensions Regulator (TPR) – is essential if this risk is to be minimised.

We therefore understand the reasons for the inclusion of proposed section 3D(1)(c), which specifies compliance with regulatory principles in relation to matters of common interest as one objective of regulation. However, we believe it is important that the narrative around co-ordination does not focus solely or largely on this objective at the expense of the purposes specified in 3D(1)(a) & (b). For this reason we also disagree with those who have suggested that the industry should be consulted in the drawing up of the MOU.

We would also suggest that the purposes of co-ordination might be framed not just in relation to what each regulator *is* doing, but also what it is *not* doing. One of the criticisms made of the previous tripartite regime prior to the financial crisis was that important risks went unchecked because no single body had effective responsibility for managing them. If one regulator does not aggressively pursue an issue that is brought to its attention on the basis that it falls within another regulator's remit, it is important that some co-ordination takes place to ensure that the second regulator has not also neglected the issue on the basis that it does not fall within its remit.

As indicated in our previous responses, we believe that investment governance is one issue which has the potential to fall between two regulatory stools – as indeed it arguably does under the current regime. For , in the dual regulation of insurance companies, the PRA is likely to focus on solvency issues and the FCA on product regulation and sales processes. This runs the risk that neither regulator is attending to the behaviour of these firms as market participants and as owners of major companies, including other financial industry entities. We continue to believe that the framing and exercise of the PRA and FCA's co-ordination duty should reflect the need to be vigilant against the emergence of gaps in regulation.

We remain at your disposal and would be pleased to meet with you to discuss any of the issues raised in this response.

Yours sincerely,

Christine Berry
Policy Officer, FairPensions

Fidelity Holdings Limited

Response to HM Treasury Consultation

A new approach to financial regulation: the blueprint for reform

Dear Sirs,

Fidelity International is a global asset management business. We operate in fifteen countries in Europe and a further nine in India and the Far East. Our UK business, Fidelity Holdings Limited, is a substantial component of our overall business and we manage £24 bn in the UK for private investors, pension funds and insurance companies. We also administer a further £23bn of retail and pensions funds.

Fidelity is strongly supportive of any measures which strengthen the position of consumers in the financial services market and therefore supports the underlying direction of the draft Bill as it relates to retail consumers.

Overview comments

There are two overarching issues which we would wish to draw to your attention at the earliest possible stage.

The first is the fact that nowhere in any of the objectives for the new regulatory bodies is there any mention of having regard to the international competitiveness of the UK's financial services industry.

It would wrong if this omission is an intentional reaction to a perceived elision of international competitiveness and light touch regulation. FIL operates with regulators globally and a number of them produce appropriate regulations and supervision which protects investors but also does minimal damage to their country's competitive position.

The second is our request that the FCA is given a specific objective to manage its prudential responsibilities on a basis that is proportionate and bespoke to its constituent firms in order to further demarcate the difference between the FCA's 'gone concern' and the PRA's 'going concern' obligations.

We cover both in full detail below. We would also raise as secondary issues:

Consultation Questions

In answering we have not sought to answer all the questions but only those most relevant to our business.

Bank of England and the Financial Policy Committee

Q1 Do you have any specific views on the proposals for the FPC as described above and in Chapters 3 and 4?

We do not have any specific comments about the objectives of the FPC as set out in section 9C. We welcome new Section 9E(2) (the duty to seek to avoid prejudicing the advancing by the FCA and PRA of any of their objectives) and new Section 9E(3)(c) (having regard to the international obligations of the UK with particular regard to the FCA and PRA). As stated above, this latter is a concept we would wish to see also advanced to the FCA at least.

Q2 Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payment systems as described above and in Chapters 3 and 4?

We would continue to argue against the current split of oversight for RCH, payment and settlement systems (at the Bank) and RIE, MTFs and other exchanges together with market conduct (at the FCA) on the grounds that the affected market infrastructure components are increasingly intertwined – not least in European legislation and its own interaction (e.g. between MiFID, EMIR and CRD IV).

We understand that settlement systems can be systemic, but so too can recognised investment exchanges and other trading venues, not least as policymakers turn to 'on exchange' trading as a proxy for systemic risk mitigation (e.g. for OTC derivatives under MiFID). In this respect, the relationship between exchanges and the clearing and settlement systems that underpin them is symbiotic. While we understand that the MiFID Directive covers both wholesale and retail conduct of business, we wonder if it would make more sense to put the exchanges and clearing and settlement systems together in the Bank which has a history of market operations.

In the meantime, we welcome the proposal for a MoU between the Bank, the FCA and the PRA (under new Schedule 17) and agree that the nature of the RCH regime will need to be reviewed in light of EMIR (your paragraph 2.38). Naturally, we feel any review will also need to take into account Dodd-Frank, IOSCO/CPSS Principles and any other elements of global clearing, payment and settlement regulation.

Q3 Do you have any comments on:

- *The proposed crisis management arrangements; and*
- *The proposals for minor and technical changes to the Special Resolution Regime as described above an in Chapter 3 and 4*

We do not have any comments on the crisis management arrangements at such a high-level.

However, we continue to be concerned about the UK's one-size-fits-all application of SRR controls to insurers, deposit-takers *and* investment firms alike – as witnessed in the FSA's recent CP 11/16 that extends the Financial Services Act 2010's requirement for deposit-takers to create a "living will" out to (undefined) significantly important investment firms.

For this reason, we think that recovery and resolution policy-making should be shared equally by FCA (and PRA) and the Bank, not least because of the FCA's role as the body primarily concerned with client money and custody asset policy – the other element of the FSA's recent CP11/16.

The Prudential Regulatory Authority (PRA)

Q4 Do you have any comments on the objectives and scope of the PRA, as described above and in Chapters 3 and 4?

Our overarching concern with the PRA relates to the lack of clarity around the scope of its reach over asset managers in two key respects:

- when asset managers have an insurance subsidiary for the sole purpose of writing unit-linked reinsurance contracts; and
- when asset managers might be considered "other firms designated for supervision by the PRA" on the grounds of presenting significant risks either to the stability of the financial system or to one or more PRA-supervised entities within the firms group.

In the absence of clarity, we would note that FIL has an insurance subsidiary that might be deemed to fall within the remit of the PRA in the first respect. FIL as a group might then also be deemed to be systemically significant either *suis generis* or to its PRA-regulated insurance subsidiary (if so designated) and thus to fall within the remit of the PRA in the second key respect.

In terms of the first key respect, we would argue that connected insurance subsidiaries should remain FCA-regulated where they only write unit-linked insurance contracts. We sense that this is the intended direction of policy travel as the Bill and draft documents all appear to work on the presumption that the PRA will only become involved in a group where the group should *suis generis* be PRA-regulated – i.e. because it is either an insurance or banking group with an asset management arm and not *vice versa*.

Indeed, to allow the use of insurance to permit the PRA involvement in groups which, in all other policy terms are meant for the FCA alone, would appear muddled and would certainly add complexity to the running of an asset manager out of proportion to any benefit in terms of the mitigation of the risk of financial instability.

In terms of the second key respect, we would argue that BIPRU 125K firms with limited permissions to deal on own account (generally speaking, asset managers with permission to deal in box management) should be ruled out of scope from "other firms designated for supervision for by the PRA" leaving only BIPRU 730K firms with full permissions to deal as principal (generally speaking investment banks) within scope of PRA supervision.

In both instances, we would suggest it is critical that the nature of the split is made clear as soon as practicable and at least ahead of the Bill's consideration.

One final point is to observe that we are intrigued by the appearance of a PRA 'insurance objective' (in draft section 2C(2)) – "contributing to the securing of an appropriate degree of protection for those who are or may become policyholders." Aside from the clarity needed around implications of attempting to cover those who *may* become policyholders, we wonder why there is no equivalent FCA 'investment objective' to require the FCA to contribute to the ongoing interests of investors – and even those who *may* invest. Adequate investment is clearly as vital to the UK's real economy and citizenry as adequate insurance.

Q5 Do you have any comments on the detailed arrangements for the PRA described above in Chapters 3 and 4?

Our chief concern remains the veto power that the PRA retains enabling it to require the FCA to refrain from specified action under draft section 3H. Not only does this threaten to pierce conduct of business regulation where it is arguably most pressingly required (it was banks who mis-sold PPI), but it may skew consumer protection depending on whether it is a PRA- or FCA-regulated entity in question. UK banks in their recent results have reserved billions of pounds for redress related to misselling of PPI. Given that this is a conduct issue which was revealed at a time of great stress on bank capital, would the PRA have allowed the FCA to force through this issue?

This split might also bring bias into the financial system. If a similar conduct issue were to occur equally in a PRA regulated firm and an FCA regulated firm, the PRA might protect the capital of the PRA firm but not the FCA firm – as with the Keydata fiasco during which the Norwich and Peterborough Building Society acquired regulatory forbearance from the FSA by not having to respond to consumer complaints. This that effectively passed the cost of compensating its investors on to investment firms via the FSCS.

We remain unclear about how the proposed judgement-led approach will operate alongside UK regulatory requirements which will have to comply with relevant EU directives (such as CRD and Solvency II) which contain many detailed, technical rules. As the UK regulatory regime sits within the EU level regulatory regime, and EU level rules and decisions take precedence over rules and decisions generated domestically, the UK regime clearly needs to be transparently situated in its EU context if regulated companies are to avoid double jeopardy.

Otherwise, we feel the requirements for the PRA to consult are much improved since the initial consultations but would observe that they nonetheless remain less secure than those for the FCA. For instance, many of the requirements to consult are to be developed by PRA rather than being set out in legislation. We also note that the PRA has no power to make statutory guidance and would observe that it would be helpful to understand whether it is expected the PRA will ever issue anything other than a rule.

The Financial Conduct Authority (FCA)

Q6 Do you have any views on the FCA's objectives – including its competition remit – as set out above and in Chapters 3 and 4?

As mentioned above, there are two overarching issues which we would wish to draw to your attention at the earliest possible stage.

The first is the fact that nowhere in any of the objectives for the new regulatory bodies – and most importantly the FCA – is there any mention of having regard to the international competitiveness of the UK's financial services industry.

It would wrong if this omission is an intentional reaction to a perceived elision of international competitiveness and light touch regulation. FIL operates with regulators globally and a number can produce appropriate regulations and supervision which protects investors but also does minimal damage to their country's competitive position.

It therefore seems to us that it would be helpful to add to the current draft Bill a further operational objective, for the FCA at least, which might sit as an addition to Part 1A, Chapter 1, Clause 1B (3)

> *(d) the international competitiveness objective*
>
> This should be followed by a new 1F (subsequent clauses to be renumbered)
>
> *1F The international competitiveness objective*
>
> *The international competitiveness objective is: maintaining the competitive nature of the United Kingdom in respect of financial services and markets having regard to best practice in international regulation and supervision.*

The second is our belief that the FCA should be given a specific objective to manage its prudential responsibilities on a basis that is proportionate and bespoke to its constituent firms in order to further demarcate the difference between the FCA's 'gone concern' and the PRA's 'going concern' obligations.

The stark difference can be illustrated with experience in the Barings crisis. Over a weekend the bank went into administration. Dealing in units of the Baring unit trusts was suspended on the following Monday but resumed on the Tuesday. For asset managers, lack of prudential capital may cause welfare losses to consumers, but their money is not lost.

The need for separate prudential treatment by the PRA and FCA is driven by European practice where, unlike anywhere else in the world, asset managers will continue to fall under the Capital Requirements Directive (CRD) alongside banks. This awkward position is then exacerbated for asset managers in three key respects:

- firstly by the fact that the CRD is at base a 'going concern' piece of regulation derived globally from the Basel Accord's banking regulations. In this context it is worth noting Europe is the only area to have pushed Basel banking requirements down onto asset managers. In the US and Asia regulatory authorities have applied Basel requirements to banks and insurers only, and have continued to treat their asset managers under separate 'gone concern' prudential regimes;
- secondly by the fact that in its latest iteration (CRD IV) the CRD has itself removed a number of its own proportionate elements that previously gave non-bank entities some relief – leaving European asset managers with a whole raft of bank-like prudential obligations ranging from liquidity arrangements to counter-cyclical buffers; and
- thirdly by the fact that fund management companies already have their own prudential requirements under the UCITS and AIFMD Directives (in the form of a proportion of AUM), as well as legislation governing the custody of fund assets, the custody of uninvested client money and appropriate forms of consumer redress.

Thus, while we believe it is entirely correct that for the FCA the focus will be on ensuring that firms can fail in an orderly manner it is becoming increasingly clear that the CRD is not the appropriate vehicle for delivering this objective for UK regulation. This may in part explain why the majority of Continental asset management regulators have chosen simply not to apply the CRD to their asset management firms (in what we believe is a wilful, but understandable and helpful, mis-reading of the Directive).

Instead and in the meantime, it will fall to the FCA to make a proportionate reading of an inappropriate Directive. In this context we would remark that the recent IMF mission's comments on the need for a single prudential rule book for the PRA and FCA is wrong and probably arises from a lack of understanding of the FSA's unique approach to the interpretation of an already defective Directive for asset managers.

The FCA must therefore be given the appropriate tools and powers to enable it to implement the CRD appropriately – again in three key respects:

- in terms of European representation the FCA will need to be empowered to represent the interests of UK asset managers under the CRD in a debate that is likely to be dominated by the UK bank lobby and the PRA; the FCA's role in the current consultation will be crucial;
- in terms of the legislative process the FCA will need to be empowered and encouraged to make a proportionate implementation of the CRD in order to meet its 'gone concern' objective – e.g. through strategic gold-plating of European legislation; and
- In terms of supervisory approach (also touched on below) the FCA will need to break from current FSA – and future PRA – practice of designing supervisory ARROW visits around the calculation and holding of adequate quantities and qualities of regulatory capital. The FCA's supervision of asset managers will need to be redesigned to focus much more on conduct of business systems and controls.

We think the best way of delivering these elements is for the FCA to be given a specific objective to manage its prudential responsibilities on a basis that is proportionate and bespoke to its constituent firms.

As also mentioned, we would also argue for an 'investment objective' to match the 'insurance objective' of the PRA on the clear grounds that investment is as vital to the UK's real economy and citizenry as adequate insurance. The FSA often points out that it is not statutorily required to put weight on the potential benefits from more consumers having access to financial products that meet their basic financial needs. If, however, the Government wants to ensure that the FCA does not act as a barrier to additional saving and a resilient society – especially in light of its new product intervention powers (that we welcome) – we suggest a reference to access should be added to the efficiency/choice objective at the very least.

Finally, it is worth noting that the objectives of the FPC, PRA and FCA all seem to overlap in making reference to financial stability in one respect or other. Where financial stability is rightly the core objective of the FCP, it makes a muddled appearance in 2B(3) of the PRA's objectives. Where the general objective (2B(2)) clearly sets a micro-prudential remit for the PRA which we believe is the correct focus, subsection (3) then seems to require the PRA to meet this objective by focusing on financial stability issues in the form of a macro-prudential objective.

For the FCA the financial stability remit takes the form of the new section 1D introduced by clause 5 (the integrity objective) that looks to "protecting and enhancing the integrity of the UK financial system". While we think this objective is critical given the FCA's role in ensuring safety and soundness in relation to critically important market infrastructure, we think it should be tightened to reflect this obligation more closely. In the meantime, we welcome the proposal for a MoU between the Bank and the FCA in particular, as a key plank in joining up supervision of RCH, settlement, payments systems and RIEs. Indeed, if the arrangements stay as currently drafted we believe their should be a statutory overarching joint committee to manage these issues.

We think 2B(3) should be removed from the PRA's objectives altogether leaving the PRA as the micro-prudential regulator of its firms alone, as the FCA will be the micro-prudential regulator of its firms alone.

Q7 Do you have any views on the proactive regulatory approach of the FCA, detailed above and in Chapters 3 and 4?

While we are very supportive of the FSA's current moves towards swifter intervention in the areas of product intervention and financial promotions and have no difficulty with seeing them enshrined in law for the FCA, We have some concerns that the relevant proposed clauses in the new Section 137C either give the FCA intentionally unprecedented powers or are poorly drafted. The whole sections seems to give the FCA almost unlimited width in defining, developing and enforcing its product intervention powers.

On the question of early publication of disciplinary action we are somewhat ambivalent. We could accept it in egregious cases but that is rather difficult to enshrine in statute. In particular we feel the current drafting leaves too much discretion to the FCA on this matter. We would not want early publication to become the norm as it would be likely to unecessarily damage the reputation of firms and individuals concerned, and potentially, the whole industry – including the regulator. We believe that a decision to publish a warning notice should be reviewed by the RDC and it would have to be shown that the public interest out-weighed the potential damage to the firm or indicvidual.

Finally, we feel it would be helpful for the FCA to have a clear policy of approach for firms. At the moment firms wishing to approach the FSA with information or concerns are limited to whistleblowing channels and are constrained by uncertainty about the attitude of their line supervisors to such reports. They thus tend to act anonymously through trade associations where they decide to act at all. We feel that this runs counter to the reliance that the FCA's Business Analysis should in future be placing on intelligence-gathering from across all market participants.

Q8 What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?

Q9 What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?

We are not clear why a new statutory process is needed in order for the FCA to deal with any future issues that are causing mass detriment. Given the FCA's proposed objectives and powers (including the FSA's recently enhanced consumer redress powers) it might reasonably be expected that the FCA would be in a position to take responsibility for addressing such issues, without requiring external parties to alert them.

Q10 Do you have any comments on the competition proposals for the FCA set out in paragraphs 2.111 to 2.119 and in Chapters 3 and 4?

We are content with the specific proposals regarding the FCA's competition powers. However, we believe further thought needs to be given to the implications of the FCA's enhanced role in ensuring competition in financial services. Given the OFT will retain general competition law powers and the right to conduct market studies in relation to financial services markets, there is a risk of duplication and/or lack of coordination between the two bodies. We suggest the FCA and the OFT ought to be subject to a statutory duty to cooperate and to produce a Memorandum of Understanding (the FSA and OFT have voluntarily published a MoU in recent years).

Q11 Do you have any views on the proposals for markets regulation by the FCA, described in paragraphs 2.120 to 2.123 and in Chapters 3 and 4?

In addition to concerns already aired about the split in market infrastructure oversight, we have concerns about both wholesale and retail market participants being defined as 'customers' – a semantic blurring that seems to us to fail to recognise the huge void in understanding, expertise and practice between, say, a retail investor in stocks and an investment bank acting as counterparty to a trade.

If the policy objective here is to seek to control the flow of 'products' from the wholesale market into retail investors' hands (by making each participant in the chain responsible for the next participant as their 'customer') we think there are more effective ways of achieving this end – namely, by focusing solely on those entities that act as the conduit between wholesale and retail markets as under the FSA's current TCF guidance on the respective roles of product providers and distributors.

Q12 Do you have any comments on the governance, accountability and transparency arrangements proposed for the FCA, as described in paragraphs 2.124 to 2.132 and in Chapters 3 and 4?

We have concerns that the accountability arrangements for the FCA (in following those of the FSA) may be prove to be less than effective. We would therefore recommend a number of statutory changes. We believe the chairs of the practitioner and consumer panels should be *ex officio* members of the FCA board and we believe the board meetings should be open to the public when discussion is on policy, as happens with the SEC. Our understanding is that the current board rarely, if ever, considers matters relating to authorised firms or individuals that would prevent such publication.

We would also like to see a more public role for FSA Board non-executive directors, with dissenting views and comments on specific rule changes being recorded. Again we find the publication by the SEC of supporting and dissenting positions on regulatory issues very helpful. We also believe it would be helpful if the FCA had a statutory duty to report annually to the Treasury Select Committee.

We note as regards annual reports that the PRA must carry out a public consultation but has no obligation to hold a public AGM, whilst the FCA must hold a public AGM but is not required to carry out public consultation. Naturally, in the absence of a policy reason for this discrepancy, we would advocate the both should do both.

On another issue we believe the alteration to the terms of reference of the statutory tribunal with respect to an inability to substitute their judgement for that of the FCA is unwelcome. It can be foreseen that cases could arise where if the tribunal can merely refer a decision back to the FCA, the FCA could make minor alterations to its case and start the process again, which can be hugely costly for those involved. We are not aware of any cases where the tribunal has replaced its own judgements with those of the FSA which can be held to be a miscarriage of justice.

Q13 Do you have any comments on the general coordination arrangements for the PRA and FCA described in paragraphs 2.138 to 2.149 and in Chapters 3 and 4?

The proposals for co-ordination are not clear and need further work whether in statute or in an operational framework.

On the one hand, given the split of prudential regulatory approach that we advocate between the PRA and FCA (for more proportionality) we would not advocate a joint rule book. On the other, we would advocate much closer shared working practices between the Bank and the FCA in the area of market infrastructure as well as between the Bank, the FCA and the PRA in recovery and resolution policy-making.

The proposed MoU between the PRA and FCA will clearly be a vital tool for ensuring that co-operation works in practice and believe that HMT should ensure that a draft of the MoU – along with the apparatus for its agreement and ongoing maintenance – is available for public discussion during the pre-legislative scrutiny phase, rather than being delayed until the time the Bill is introduced, in order to inform debate at this important stage of the process.

We also have sympathy with the remarks in the Technical Notes of the recent IMF mission that more formal co-ordination arrangements between the PRA and FCA would be welcome, particularly with regard to representation in Europe and internationally, as well as on day-to-day supervision.

Q14 Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described in paragraphs 2.150 to 2.195 and in Chapters 3 and 4?

We would urge HMT to take this opportunity of reviewing the correlation between the 'permissions' granted to UK firms under the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (the RAO) and the investment activities and ancillary services as prescribed under the European Union's Markets in Financial Instruments Directive (MiFID).

Currently there is a mismatch between the two which puts UK firms out of kilter with a whole range of European Directives and Regulations – not least the CRD- which are, quite naturally, built upon the set of investment activities and services set out under MiFID and not those prescribed by the UK's singular RAO.

Q15 Do you have any comments on the proposals for the FSCS and FOS set out in paragraphs 2.196 to 2.204 and in Chapters 3 and 4?

We have a particular concern that the FOS powers have not been altered. Because authorised firms operate under FSA/FCA rules and guidance but the FOS applies a "fair and reasonable" test, it can, and has, happened that actions by a firm which met the FSA rules has nonetheless led the FOS to impose redress *ex post*. These cases may be of benefit to the individuals concerned but because of the uncertainty this behaviour introduces for firms the effect has been to prevent firms from introducing services which would otherwise be of benefit to a wide range of the population, such as simplified advice.

We believe the FOS should accept that compliance with FSA/FCA rules and guidance at the relevant point in time should provide a safe harbour for providers. If the FOS believed that insufficient protection had been provided by those rules they should take the matter up with their board and the FCA and publically state their reasons for so doing. Furthermore, by operating on a set of alternative standards to those guiding FSA/FCA supervision, the FOS also loses its utility as an early warning system *for* the FSA/FCA.

We would also advocate that the respective responsibilities of the FCA, FOS and the courts should be set out in statute. For example, novel points of law should be referred to the courts and broader regulatory matters determined by the FCA. In addition, new measures are needed to ensure that the FOS is properly transparent and accountable.

As ever, we would be more than happy to discuss any of the opinions set out in this submission.

Yours Sincerely

Philip Warland

Head of Public Policy

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Dear Sirs

Issue 157: HM Treasury Consultation – A New Approach to Financial Regulation: the Blueprint for Reform (June 2011)

The role of the Financial Markets Law Committee (the "FMLC") is to identify issues of legal uncertainty or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.

HM Government has been developing proposals for the reform of the framework of financial regulation in the UK. It is not the role of the FMLC to question the policy underlying the proposals for reform. It is, however, the view of the FMLC that the implementation of that policy may in the future raise some serious issues, both conceptual and practical, for the UK markets and that it is in the interests of a robust system of regulation that these issues are recognised and addressed in the legislation which is proposed.

The appendix to this letter provides a brief and non-exhaustive list of legal uncertainty points which the FMLC has identified in HM Treasury's consultation paper entitled 'A New Approach to Financial Regulation: the Blueprint for Reform'. It also includes some proposed solutions. The FMLC will provide HM Treasury with a comprehensive paper on these issues later this month.

The appendix to this letter covers legal uncertainty issues regarding: co-ordination between the regulatory authorities; enforcement; authorisation, permission and regulated activities; passporting; listing and extra-territoriality; rules and guidance; administrative discretion and other powers issues; and systematically important infrastructure.

The FMLC would be happy to discuss any of the comments made in this letter and appendix further. Please do not hesitate to contact us with any questions.

Yours faithfully

Joanna Perkins

FMLC Director

Enc: Appendix

FINANCIAL MARKETS LAW COMMITTEE

Appendix: Issue 157 - A non-exhaustive list of issues of legal uncertainty arising from HM Treasury's consultation entitled 'A New Approach to Financial Regulation: the Blueprint for Reform' (June 2011)[1]

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1. INTRODUCTION

1.1. It is not the role of the Financial Markets Law Committee (the "FMLC") to question the policy underlying the proposals for reform. It is, however, the view of the FMLC that the implementation of this policy may in the future raise some serious issues, both conceptual and practical, for the UK markets and that it is in the interests of a robust system of regulation for these issues to be aired and addressed.

1.2. The FMLC is housed and partially sponsored by the Bank of England, but is entirely independent. Any views it expresses are its own and are not those of the Bank or any other interested party.

1.3. This appendix provides a brief and non-exhaustive list of legal uncertainty points which the FMLC has identified in HM Treasury's consultation paper entitled 'A New Approach to Financial Regulation: the Blueprint for Reform' (the "Consultation"). It also includes some proposed solutions.

2. CO-ORDINATION BETWEEN THE REGULATORY AUTHORITIES

Clause 3 of the draft Financial Services Bill (the "Bill"): the Financial Policy Committee (the "FPC") - Amendments to the Bank of England Act 1998

2.1 Section 9E(2) imposes a very low hurdle to be surmounted by the FPC before acting in a way that prejudices objectives of the Prudential Regulation Authority (the "PRA") and the Financial Conduct Authority (the "FCA"). There is, however, no mechanism provided in the Bill by which the FPC will take into account the views of the PRA and FCA in striking a balance between the Bank's Financial Stability Objective and the objectives of the PRA and FPC. The absence, for example, of a duty to consult renders it unclear how the FPC will assess the existence and extent of any potential prejudice to those objectives. In view of the numerous provisions requiring consultation, the lack of a provision concerning a duty to consult increases uncertainty about the process.

2.2 By expressly setting out only one aspect of the principle of proportionality, section 9E(3)(a) creates uncertainty about the application of the other elements of proportionality, in particular the requirement that a measure should go no further than necessary to achieve the legitimate aim being pursued. The provision is also unclear regarding the method of measurement of benefits expected to result from the burden or restriction and regarding the parties who should be taken into account for the purposes of that measurement.

2.3 Section 9H(2) specifies no basis for a decision to exclude procedural requirements in an order by HM Treasury which relates to macro-prudential measures. Express provision as to the circumstances in which procedural requirements may be disapplied would therefore reduce uncertainty.

2.4 Section 9J gives HM Treasury discretion as to whether to publish a direction made to the FCA or PRA under section 9G. If a direction is not published, it may make it extremely difficult for those affected by the resulting measures, put in place by the PRA or FCA, to review those measures against relevant provisions of the Financial Services and Markets Act 2000 ("FSMA"). It would therefore increase certainty if there was a presumption under section 9J in favour of publication and for the provision to require that any suspension of publication last for only as long as necessary to meet the interests of financial stability.

Clause 5 of the Bill: PRA and FCA – amendments to FSMA

2.5 The requirement under section 1G for the FCA to consult the PRA before giving guidance about which matters it regards as primarily its own responsibility, rather than the responsibility of the PRA, will not necessarily resolve concerns about duplication or inconsistency in the actions of the PRA and FCA. Nor will the equivalent power under section 2H, which requires the PRA to consult the FCA, necessarily resolve duplication and inconsistency. Duplication or inconsistency is intended to be dealt with by the duty under section 3D which is discussed further below.

2.6 The risk of some instability is inevitable in the financial system. However, as framed, section 2B(3) appears to suggest that the PRA should ensure its population of firms is effectively risk-free. Clarity could be improved by, for example, replacing the words "avoids any" with "minimises".

2.7 Prior to the introduction of the new section 2C ("Insurance Objective") for the PRA, the split between the FCA and PRA as far as insurance was concerned meant that the FCA would be responsible for enforcing the Conduct of Business Sourcebook / Insurance Conduct of Business Sourcebook type obligations and the PRA responsible for the prudential, i.e. INSPRU sourcebook type obligations. Section 2C creates uncertainty because the extent to which the PRA's obligations thereunder will overlap with the obligations of the FCA is unclear. The creation of the new "Insurance Objective" could exasperate problems of co-ordination between the FCA and PRA, particularly if the PRA seeks to assert responsibility for a matter on the basis of the objective.

2.8 Section 3B(1)(b) suffers from the same uncertainty brought about by the partial inclusion of the proportionality principle as discussed above with regard to section 9E(3)(a) of the Bank of England Act 1998.

2.9 As referred to above, there are a number of aspects of section 3D that give rise to uncertainty as to how the PRA and FCA will manage co-operation and avoid possible overlaps, underlaps and inconsistencies which could create legal and regulatory uncertainty and impair the effectiveness of the proposed regime. In particular:

(a) It is not clear under section 3D(1)(a) how the PRA or FCA will determine whether the exercise of its functions may have a material adverse effect on the other.

(b) The carve-outs in section 3D(2) seem to neuter the obligation to co-ordinate. Under section 3D(2)(a), if the PRA or FCA concludes that co-ordination is not compatible with the advancing of its own objectives—which will inevitably be the case when one regulator decides to exercise its powers in a way which is likely to be adverse to the achievement of the other regulator's objectives—then the reluctant regulator will not be under the obligation to co-ordinate. As regards section 3D(2)(b), it is unclear why the burden that co-ordination puts on the regulator—relative to the benefits of compliance—is an appropriate test, or how the cost-benefit analysis would work.

2.10 Section 3E(1) provides for the publication of a memorandum in general terms by the PRA and FCA in relation to regulatory co-ordination. Although the list in section 3E(2) is not exhaustive, it is not clear that the memorandum is required to set out a mechanism for the timely resolution by the regulators of boundary and other issues between them. In view of the practical importance of this issue an express reference to this requirement in section 3E would be useful to reduce uncertainty. Legal certainty would also be aided by a requirement for the memorandum to set out how the regulators will ensure consistent interpretation of provisions that are applicable to each of them, though this may be better expressed as a regulatory principle in section 3B.

2.11 Section 3F shifts responsibility for "With Profits" policies to the PRA. Responsibility for the interests of the policyholder and their reasonable expectations, which the FCA might be expected to take on, is, pursuant to section 3F, transferred to the PRA, which could, as with the new "Insurance Objective", give rise to issues surrounding co-operation and co-ordination.

3. ENFORCEMENT

Warning notices – amendments to FSMA

3.1 Some legal uncertainty is inherent in the discretion given to the PRA and FCA in deciding when to publish or not to publish warning notices, what details to publish and in what manner.

3.2 There are safeguards (substantive and procedural) by which firms may challenge such decisions and these must be considered for uncertainty:

(a) Under section 391(6)(a), a decision to publish can be challenged for unfairness. This provision creates legal uncertainty as it is not clear what will constitute "unfairness" and there is no detail as to what objective criteria a decision will need to satisfy in order for it to be challenged for "unfairness".

(b) There is uncertainty as to the process for challenging decisions to publish as it is not clear whether the process (including timing) will be the same as that currently used for disputing the giving of a warning notice under section 387 FSMA. Clarification as to whether this is the case and, if it is not, further detail in section 391, would reduce this uncertainty.

3.3 Section 395(1), regarding the issuing of statements of policy on, *inter alia*, warning notices by the FCA and PRA, is unclear as to whether it covers the FCA and PRA policy on the publication of warning notices because the text refers specifically to the "giving" of notices.

Appeals to the tribunal – amendments to FSMA

3.4 Rights to refer a regulator's decision on appeal to the tribunal are changing, so that in some areas there will be no such right—other than by means of judicial review where the relevant grounds can be satisfied—and in some cases, where the right exists, the tribunal will not be entitled to come to a view on the merits of the decision being challenged so as to substitute that decision for its own. It is important for legal certainty that a body of case law can develop to inform firms and their advisors on the application of new powers and a wider recourse to the tribunal would in this way increase certainty.

4. AUTHORISATION, PERMISSION AND REGULATED ACTIVITIES

Regulatory processes

4.1 Paragraphs 2.134-137 of the Consultation are not favourable to suggestions for "shared services" or a "single point of contact" for regulatory processes, preferring an approach whereby the PRA and FCA develop their own systems. Such a developmental approach may not provide firms with legal certainty or clarity in their dealings with the regulators during the development and improvement of these systems.

Authorisation – amendments to FSMA

4.2 Applications for authorisation must be made to the "appropriate regulator" in accordance with section 55A(2). Section 55U gives each regulator the freedom to develop its own application processes and approach to the provision of information with respect to authorisation applications. This creates uncertainty for firms regarding the process, timing and paperwork of the authorisation process required for authorisation. This might be the case particularly for firms that initially sent their application to the "wrong" regulator; a circumstance acknowledged in section 55G.

4.3 Section 55C provides a mechanism whereby the regulators may arrange among themselves which of them is to be responsible for ensuring compliance with particular threshold conditions. The mechanism is expressed as a power, rather than an obligation, but there is uncertainty as to how compliance by a firm regulated by both the PRA and FCA will be ensured if no such arrangement is reached.

Approved persons regime – amendments to FSMA

4.4 Under section 59 both regulators have the power to designate controlled functions, although the PRA is stated in the Consultation (paragraph 2.160) to have "primary responsibility" for designating significant influence functions. Section 59A provides that the FCA must "keep under review" the exercise of its power to designate significant influence functions and exercise that power in a way which it considers will "minimise the likelihood that approvals fall to be given by both the FCA and the PRA" in respect of performance by an individual of a significant influence function. The section leaves uncertainty as to how a firm might deal with a situation where its approved persons are subject to overlapping or inconsistent requirements imposed by the two regulators.

4.5 Under section 63 both regulators have the power to withdraw an approval, even if the approval was granted by the other regulator (in the case of the PRA, where the function is a significant influence function in a PRA-regulated firm). As it seems that both regulators are entitled to take action against an approved person, it remains unclear whether a firm, or a relevant individual, will, at a time when difficulties are in any event being encountered, need to deal separately with the two regulators in relation to the same set of circumstances.

Change in control – amendments to FSMA

4.6 Applications for change in control approval are to be made to the “appropriate regulator” and each regulator is given power to specify the form in which such application must be made and the information which is required to accompany it. It seems possible that the two regulators may, over time, develop quite separate processes and approaches. There is therefore uncertainty as to whether, in the case of an acquisition of a group including both PRA and FCA regulated firms, the acquirer may be required to go through two, potentially different, processes of approval.

Other issues – amendments to FSMA

4.7 As regards regulated activities, it is difficult to comment on many practical aspects of the proposals in the absence of a definition of “PRA-regulated activities”. Although it is clear that banks and insurance companies are to be PRA-regulated, there is at present no clarity as to how “systemically important investment firms”—which are also intended to be regulated by the PRA—are to be identified, but that will presumably be through the definition of “PRA-regulated activities”. Uncertainty is created by the fact that the Consultation (paragraph 2.58) suggests that the PRA is to have the power to designate firms for prudential supervision, whereas clause 6 of the Bill gives HM Treasury the power to specify PRA-regulated activities for the purposes of the Bill. Greater clarity as to whether there is to be a quantitative or other objective test to identify “PRA-regulated activities”, how such a test would work and the extent to which the PRA will exercise discretion on a firm-by-firm basis would increase legal certainty in this area.

4.8 The threshold conditions set out in Schedule 6 to FSMA are to be amended by the insertion in the “suitability” condition of a new requirement that the firm satisfy the regulator that its "strategy for doing business" is suitable, having regard to the regulated activities that the firm carries on or seeks to carry on. Uncertainty arises as it is not clear how this new continuing obligation (distinct from the current application requirement to present a business plan) will be applied in practice.

5. PASSPORTING

5.1. Schedule 3, part 1, paragraph 2 of FSMA includes within the scope of "the banking co-ordination directives" the Capital Requirements Directive 2006/48/EC (also known as "CRD I") as amended by implementing Directive 2009/111/EC (also known as "CRD II"). The European Commission adopted the Capital Requirements Regulation and a revised version of the Capital Requirements Directive ("CRD IV") on 20 July 2011.[2] The latest legislative package replaces CRD 1 and the Capital Adequacy Directive 2006/49/EC. To avoid legal uncertainty, it would seem sensible that, as part of the changes which the Bill introduces, FSMA is amended to reflect these changes.

5.2. Schedule 3, part 2, paragraph 14(4) of FSMA as amended defines the "appropriate UK regulator" relevant to incoming EEA firms as "whichever of the FCA and the PRA is the competent authority for the purposes of the relevant single market directive". This may mean that systemically important financial institutions (excepting banks) that are incorporated in the UK will be regulated by the PRA, but could be subject to the Markets in Financial Instruments Directive ("MiFID") for passporting. The Bill could avoid this uncertainty if the proposed definition of "appropriate UK regulator" and the associated passporting arrangements were amended or clarified as to who the competent authority would be for such incoming dual regulated firms.

6. LISTING AND EXTRA-TERRITORIALITY

6.1 The removal of the existing section 72(1) of FSMA creates uncertainty as to the designation of the UK's central competent authority required by article 21(1) of the Prospectus Directive. It may be that HM Treasury will use its current power under Schedule 8 of FSMA to designate the FCA as the UK's competent authority for this purpose but this is not clear.

6.2 The removal of the specific duties imposed on the UK Listing Authority (the "UKLA") under the existing section 73 of FSMA and the subjection of the listing authority to the same

[2] http://ec.europa.eu/internal_market/bank/regcapital/index_en.htm#crd [last accessed 29 July 2011].

duties as the FCA may produce legal uncertainty because both the listing and the conduct of business elements of the FCA will be subject to the same strategic objective (protecting and enhancing confidence in the UK financial system) and operational objectives (including securing an appropriate degree of protection for consumers). However, the FCA will be constrained when carrying out its functions as the UK's competent authority for the purposes of the Prospectus Directive. Although perhaps unlikely, it is theoretically possible that the FCA will be forced by compliance with EU obligations to do things that put it in breach of its statutory duties. Section 1B(1) of FSMA as amended deals with this conflict to some extent by only requiring the FCA to discharge its general functions in accordance with the strategic and operational objectives "so far as is reasonably possible" but more clarity is needed.

6.3 The removal of the existing section 73 of FSMA may create legal uncertainty through the removal of a number of matters to which the UKLA must have regard in carrying out its functions. The new section 1B(4) of FSMA does retain a requirement for the FCA to discharge its duties in a way that promotes competition but this is subordinate to the strategic objective and operational objectives. The loss of the controlling principles in the current section 73 of FSMA, coupled with the new regulatory tool allowing product intervention, is likely to deprive issuers and other primary market participants of the certainty they currently enjoy. At present, except in extreme cases where an issuer or an issue is clearly unsuitable for admission to the regulated markets, provided the requirements of the Prospectus Directive regime are complied with the UKLA must grant admission to the UK's regulated market. This certainty is threatened because the competent authority will be subject to the same duties as the conduct of business division (including the overriding operational objective to protect consumers) and the competent authority will have the power to intervene in the design of products. It appears necessary to make clear in law that the regulatory tools that are available to achieve consumer protection will be used somewhat differently, depending on whether the FCA is engaged in listing or conduct of business regulatory activity.

7. RULES AND GUIDANCE

The product banning power

7.1 Para 2.100 of the Consultation suggests that product bans are only intended to be used in a retail context. However, the definition of consumer in the new section 1C of FSMA is very wide creating uncertainty as to the extent of the power. If the intention is that the FCA should only be entitled to use this power in a retail context, a narrower definition of "consumer" might increase certainty.

7.2 Section 137C(5)(a) of FSMA could be interpreted as allowing the FCA to use its product intervention powers to ban products that are currently not regulated by the Financial Services Authority (e.g. credit cards and personal loans). If this is not the intention, a revision of the section might reduce uncertainty.

7.3 Section 137C of FSMA deals with the FCA's general duties with respect to product intervention. Section 137C(5) of FSMA seeks to exclude certain items as relevant factors in the making of any order under section 137C(1) of FSMA. The effect of these provisions is that the FCA, in deciding to make product intervention rules, may ignore the fact that the person with whom an authorised person enters an agreement in the course of promoting, selling or otherwise carrying on an activity with respect to a financial product is another authorised person. This appears to be at odds with the current principle of variable degrees of protection for counterparties under MiFID and the scheme under the Financial Services Authority's Conduct of Business Sourcebook with an authorised person, in effect, enjoying more discretion in the context of its dealings with an eligible counterparty such as, *inter alia,* another authorised person. The principle of differential treatment rests on, *inter alia*, the FCA's consumer protection objective, embodied in section 1C of FSMA and paragraph 2.100 of the Consultation states that the product banning power is unlikely to be appropriate in relation to the protection of professional or wholesale customers. Excluding the factors in section 137C(5) of FSMA may give rise to legal uncertainty as to the proper and consistent application of the consumer protection measures in the context of the product banning power, suggested by the proposed section 137C(1)(a) of FSMA.

7.4 The effect of the product intervention powers in section 137C(1) of FSMA is such that it would, as a matter of the proper application of any test of proportionality under section 6 of the Human Rights Act 1998, be difficult to justify the exclusion of the items in section 137C(5) of FSMA. This potential conflict gives rise to uncertainty as to the application of section 137C(1) of FSMA where the product in question is intended for use by authorised persons.

7.5 Section 138N of FSMA allows the regulator wide discretion to disapply the obligation to consult under section 138J of FSMA in the case of temporary bans. In the absence of a product pre-approval process and of a right of appeal to the Tribunal for affected firms, strong safeguards are required to ensure that legal certainty is maintained in relation to existing contractual arrangements, except for in the most serious of cases.

7.6 Section 138O of FSMA gives the FCA the power to make temporary product intervention rules and section 138N of FSMA creates exemptions from the consultation requirements for temporary product intervention rules. Sections 138C(5) and 138C(6) of FSMA have the effect that the FCA cannot extend the rules beyond a 12-month period without following the general rule-making procedures. It would appear more consistent with the temporary or emergency nature of the power if the FCA were to be obliged to make use of the full and proper consultation procedures as soon as practicable after making use of the temporary product intervention rules.

Directions regarding financial promotions: amended section 137P FSMA

7.7 Subsection (3) could be interpreted not only as preventing firms from reissuing banned financial promotions with minor amendments but also as imposing a positive obligation on firms to review and assess other financial promotions that they may have in issue at the time to decide whether those should also be withdrawn. A clarification in the text would reduce this uncertainty.

General powers of intervention

7.8 In general, there is no clear delineation of the basis on which the powers of intervention, for example those given under section 137C, are to be exercised. Intervention may take place where considered "necessary or expedient" for the purpose of advancing the consumer protection or efficiency and choice objective - where the integrity objective is relevant, then the Treasury must first have made an order to apply the relevant section. There is a danger that as the basis for the use of these powers is unclear, issues surrounding the predictability and transparency of their use will arise.

8. ADMINISTRATIVE DISCRETION AND OTHER POWERS ISSUES

Judgment-led supervision (referred to in the Consultation and previous approach papers published by the Bank of England and Financial Services Authority)

8.1 The FMLC's Issue 157 Paper dated December 2010 (available at http://www.fmlc.org/papers.html) discusses more fully the legal uncertainty which appears to result from judgment-led supervision. The Paper points out, in particular, that moving away from compliance with specific rules may have the effect that "there will be nothing that will provide regulated persons with bright lines for individual self direction for their operations on a day-to-day basis".

8.2 Details on how and when powers will be exercised, and how the regulators will coordinate in exercising these powers, are not included in the Bill and it is instead intended that Memorandums of Understanding and statements of policy cover these issues. There may be legal uncertainty until these documents have been developed.

Power to direct unregulated holding companies: Part 12A FSMA

8.3 The breadth of the proposed power of direction over parent companies of UK authorised firms presents a number of possible issues of legal uncertainty.

(a) The power gives discretion to HM Treasury to define both (i) the kinds of UK authorised subsidiaries whose parent companies may be directed (section 192A(4)) and (ii) the persons who may be directed, that is the nature of business of the parent, and conceivably its location of incorporation (section 192B(8)).

(b) The power in section 192B(8)(a) appears to allow HM Treasury to remove the limitation that directions can only be applied to financial institutions, creating significant potential uncertainty as to how or to whom the powers will be applied. The wording of section192B(8)(2)(b) could also be construed as allowing HM Treasury to change the application of the provisions to go beyond parent bodies corporate incorporated in the UK.

(c) The trigger for exercise of the power under section 192B is widely drawn, leading to uncertainty. For example, under section 192B(5) the power of direction may be exercised if the regulator considers that acts or omissions of the parent "may" have a material adverse effect on the regulation of "one or more qualifying authorised persons". This is arguably not limited to the directed person's own subsidiary or subsidiaries and would perhaps benefit from narrowing to refer to the relevant authorised persons.

(d) It appears that the use of the power could fundamentally damage the private legal rights of parties dealing with the parent company, in particular, creating significant legal uncertainty for creditors and shareholders of the parent were the parent forced to provide additional capital or liquidity for a subsidiary. The use of the power could cause a parent to breach undertakings or comfort letters given to other non-UK regulators. Listed parent companies may also face difficulties in making accurate financial and other public statements

(e) Regarding the ability to appeal or challenge the use of the power, the requirement under section 192F for a person to be “aggrieved” before referring a matter to the Tribunal adds uncertainty.

(f) At a general level, the power, as currently drawn, appears to introduce legal uncertainty by potentially undermining the principle of separate legal personality between parents and subsidiaries.

9. SYSTEMATICALLY IMPORTANT INFRASTRUCTURE

9.1 It may aid stability and certainty if account is taken of the development of the European Market Infrastructure Regulation (“EMIR”) as part of the development of these proposals because further legislative changes as a result of EMIR are likely to be required in the future. Resolution powers for Recognised Clearing Houses (“RCH”) also require consideration in the context of these proposals.

9.2 The FCA, which will be the relevant regulator for Recognised Investment Exchanges (“RIE”), is obviously subject to the general duties in section 1B of FSMA as well as the provisions on consultation in section 1H of FSMA and the regulatory principles in section 3B of FSMA. These provisions would apply equally to the FCA's functions in relation to RIEs. The Bank of England is not subject to equivalent provisions in respect of its role as the relevant regulator of RCHs. It would appear that the Bank of England's financial stability objective will be the overriding objective in relation to RCHs. However, this will result in a difference between the regulatory framework for RIEs and RCHs (for example, the FCA's "efficiency and choice objective" specifically refers to the promotion of efficiency and choice in relation to the services provided by an RIE however, there is no similar provision in relation to RCHs).

Financial Services Consumer Panel response to

Cm 8083 - a new approach to financial regulation: a blueprint for reform

September 2011

Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

Response to Cm 8083 - A new approach to financial regulation: a blueprint for reform[1]

Introduction

The Financial Services Consumer Panel welcomes the opportunity to comment on the questions posed in Cm 8083 and would be happy to discuss further any of the points raised in this response. Getting the regulation of financial services right is a crucial element in revitalising the economy, supporting an efficient and effective industry, and above all protecting and supporting the rights of consumers. As a statutory body under the Financial Services and Markets Act 2000 the Panel advises the current FSA on the interests and concerns of consumers and reports on the FSA's performance in meeting its objectives, and is therefore well positioned to comment on the proposals for future regulation.

In summary, the main points of this response are:

1. The Panel believes consumers would be best able to take responsibility for their decisions if the authorised persons with whom they deal have an explicit fiduciary duty towards them and if all matters relevant to the conduct of such firms are disclosed.
2. The FPC should have a duty to consider representations made to it by the Consumer Panel.
3. The PRA should have a specific ‘have regard’ to the need to minimise the adverse effects on competition that may arise from anything done in the discharge of its function.
4. The Consumer Panel must retain its function for the PRA, in order to advise on prudential matters in general and the interests of with-profits policyholders in particular.
5. The Panel proposes there should be a statutory requirement for the PRA and FCA to estimate both the costs and benefits of proposed new rules. The new legislation should be taken as an opportunity to improve rather than water down the evidence base used in consultations.
6. Relying on increased disclosure of information is not sufficient to ensure consumer protection and the FCA must be mindful not to rely on this in carrying out its consumer protection obligations.
7. Relating to competition powers, the existing proposals are excessively complex. The starting point should be the assumption that the FCA is the lead on competition issues in financial services. It should refer to the Competition Commission (or its successor) only if structural change needs to be considered.
8. We welcome the proposed new powers relating to financial promotions, which in conjunction with the product intervention power will assist the FCA in preventing inappropriate products reaching the market. We

[1] http://www.official-documents.gov.uk/document/cm80/8083/8083.pdf

believe there should be a presumption in favour of publication of specific and identified action in the case of misleading promotions.

9. The FCA should have the ability to publish information of disciplinary action without consultation with the firms involved, where it considers there is a risk of serious consumer detriment.
10. The FCA should have the ability to publish information received for the purposes of its functions under FSMA, where it considers this appropriate.
11. Memorandum of Understanding provisions between the PRA and FCA must give detailed provision on ensuring coordination with the European Supervisory Authorities (ESAs) of which they are not members, as well as the ESAs of which they are members, to ensure that both prudential and conduct of business issues are addressed across all sectors.

1. Proposed principles of regulation for the PRA and FCA - fiduciary duty

The Regulatory Principles in clause 3B of the Bill include 'the general principle that consumers should take responsibility for their decisions'. It is recognised that different consumers have differing degrees of experience and expertise (clause 1C(2)(b)). Given this, it would help consumers take responsibility if authorised persons had an explicit fiduciary duty towards their clients.

A fiduciary is someone who has undertaken to act for and on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. Fiduciary duty implies a stricter standard of behaviour than the comparable duty of care at common law. The fiduciary has a duty not to be in a situation where personal interests and fiduciary duty conflict, a duty not to be in a situation where his fiduciary duty conflicts with another fiduciary duty, and a duty not to profit from his fiduciary position without express knowledge and consent. A fiduciary cannot have a conflict of interest.

The recent US Dodd-Frank Act[2] provides authority for the Securities and Exchange Commission (SEC) to impose regulations requiring "fiduciary duty" by broker-dealers and investment advisers to their customers. Although the Act does not create such a duty immediately, the Act authorises the SEC to establish such a standard and requires that the SEC study the standards of care which broker-dealers and investment advisers apply to their customers and report to Congress on the results within 6 months. The SEC is due to propose rules later this year.

For consumers with limited experience and expertise, dealing with a provider of financial services which has a fiduciary duty would reduce the chances of detrimental outcomes when such consumers take responsibility for their decisions.. It would be desirable to extend this approach to the generality of relationships between consumers and authorised persons.

An important outcome of the FSA's Retail Distribution Review is that independent financial advisers will no longer be able to take commission from product providers but will be paid a fee agreed by their clients, so that the adviser acts clearly as agent for the client.

The Panel proposes that a further sub clause be added to clause 3B(1):

> *'the principle that, where appropriate, authorised persons should have a fiduciary duty towards the consumers who are their clients'.*

The reference to 'where appropriate' allows the fiduciary duty principle to be disapplied in certain cases if, after consideration, it were to be judged by the FCA to be inappropriate, for example on account of unintended consequences.

[2] Dodd-Frank Wall Street Reform and Consumer Protection Act 2010, H.R. 4173-453

2. Responses to specific questions

1. *Do you have any specific views on the proposals for the FPC as described in paragraphs 2.6 to 2.24 and in Chapters 3 and 4*

The Panel has concerns about the structure and functioning of the FPC as currently conceived, and in particular the lack of diversity in the membership, in that the majority of members are directly connected to the Bank of England. A more robust structure would include a wider range of experience, with the majority of members not from the Bank, in combination with an adequately resourced independent secretariat.

The FPC will seek to achieve its main objective by identifying, monitoring and taking action to remove or reduce systemic risks. These systemic risks include in particular unsustainable levels of leverage, debt, or credit growth, where 'credit growth' is defined as the growth in lending by the financial sector to individuals and businesses in the UK, and 'debt' is debt owed to the financial sector by individuals and businesses in the UK.

As part of its concerns about the breadth of knowledge and experience of the FPC, the Panel believes it should have adequate information from a consumer perspective on factors which may be influencing the levels of debt and credit growth and which contribute to the sustainability of these levels. The relatively narrow objective of the FPC, focusing on financial stability, should not restrict its ability take account of the wider impact on the economy and society of its actions.

As it stands, there is no direct consumer representation on the FPC. This could be resolved by requiring it to consider representations made by a body such as the Consumer Panel, in the same way the FCA will be required to do. It proposes the following section to be inserted into the Bank of England Act:

> *'The FPC must consider representations that are made to it by the Consumer Panel in accordance with arrangements made under section 2J of FSMA.*
>
> *The FPC must from time to time publish in such manner as it thinks fit responses to the representations'*

The Panel has a unique position in that it can represent consumer issues while regulation is being developed, before that regulation reaches the public domain. In the case of the Mortgage Market Review, for example, the Panel has been supportive of the principles of the Review, but voiced concerns about the thrust of the FSA's original proposals, including questioning the FSA's proposals on responsible lending, the role of macro-prudential tools and the scope and quality of its economic analysis. As a result of the work of the Panel and others the FSA was persuaded that it should proceed with greater care and deliberation.

The Panel also has a breadth of experience in the areas of consumer debt and credit. It has in the past carried out its own research into, for example, mortgage arrears[3] and the experiences of consumers with overdrafts[4], as well as providing input and advice to the FSA and others on the consumer credit regime, mortgages, insolvency, banking services, credit and store cards. A list of recent public responses is attached as an Appendix.

As a consequence of lack of consumer orientation, the Panel is concerned that the FPC may not take adequate account of the consumer interest when making important decisions about the mortgage market. The Panel has previously suggested[5] that instruments, such as loan-to-value caps, may be effective in stabilising the financial system but may additionally have serious adverse consequences for some consumers, limiting their options.

The Panel proposes that the FSA should pro-actively engage with the interim FPC to subject each macro-prudential instrument to a rigorous cost benefit analysis which takes account of the goals of financial stability and consumers' welfare. This preparatory exercise would facilitate the selection of preferred macro-prudential tools that would contribute most to financial stability while inflicting least direct damage on consumers, judged in terms of the impact on the availability and cost of financial services, including mortgages. Except in circumstances of immediate crisis, we would also expect the FPC, once fully operational, to consider in consultation with the FCA the consumer welfare implications of macro-prudential interventions.

2. Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payment systems as described in paragraphs 2.32 to 2.40 and in Chapters 3 and 4?

The Panel believes there is scope for significant improvements in payment options in financial services, and has already commented on this in its response to the ICB interim review.[6] In particular, the current payments system acts as a barrier to new entrants to the banking system. On this basis, the Panel recommends that the payments system be the responsibility of the FCA, in line with its competition remit.

3. Do you have any comments on:

- *the proposed crisis management arrangements; and*
- *the proposals for minor and technical changes to the Special Resolution Regime as described in paragraphs 2.41 to 2.44 and in Chapters 3 and 4?*

No comment.

4. Do you have any comments on the objectives and scope of the PRA, as described in paragraphs 2.46 to 2.61 and in Chapters 3 and 4?

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[3] *Mortgage Arrears*, Financial Services Consumer Panel, June 2009
[4] *Overdraft Complaints*, Financial Services Consumer Panel, June 2008
[5] '*Six point plan for a sustainable and healthy mortgage market*; Financial Services Consumer Panel, 1 June 2011
[6] http://www.fs-cp.org.uk/publications/pdf/response_icb_report.pdf

Insurance objective

The Panel welcomes the proposals that the PRA's objectives will now make specific reference to its responsibilities with regard to insurers.

This reflects the different priorities, timescales and business models of the insurance industry when compared to the banking industry. It particularly welcomes the requirement to secure an appropriate degree of protection for those consumers who are or may become policyholders.

Regarding the PRA's objective to regulate policyholder reasonable expectations (PREs) for with-profits policies, the Panel has in the past been broadly supportive of the FSA's approach to protecting the interests of with-profits policyholders[7]. However, the reference to the term 'policyholder reasonable expectations', is unhelpful in this context. There is no universally accepted definition of the term, and its use could lead to potential confusion. We would recommend the following change;

> *3F(1) In relation to PRA-authorised persons carrying on the activity of effecting or carrying out contracts of insurance, responsibility for contributing to the securing of an appropriate degree of protection for ~~the reasonable expectations of~~ policyholders as to the distribution of surplus under with-profits policies is that of the PRA rather than the FCA.*

Competition

The Panel agrees that competition should not be a primary objective for the PRA, but does have concerns that its actions could potentially have a damaging effect on competition and consumer welfare. It is important that issues such as barriers to entry are considered, as well as the concerns of large institutions. Therefore it proposes that the PRA's regulatory principles should include:

> *"The PRA must have regard to the need to minimise the adverse effects on competition that may arise from anything done in the discharge of its functions".*

5. Do you have any comments on the detailed arrangements for the PRA described in paragraphs 2.62 to 2.78 and in Chapters 3 and 4?

Consultation

The Panel agrees that there should be no significant reductions to the existing FSMA requirements to consult on rules. It is appropriate that regulators will continue to conduct cost benefit analysis of rules originating from Europe, on the basis that there are in practice few, if any, instances where there is

[7]We have previously commented on this area in our response to CP11/5*** '*Protecting with-profits policyholders'* http://www.fs-cp.org.uk/publications/pdf/cp115_with_profits_final.pdf

absolutely no discretion or room for interpretation when implementing such rules.

The Panel strongly believes that the existing FSMA requirement to conduct a cost benefit analysis, where this is defined as an estimate of the costs together with an analysis of the benefits that will arise from a new rule, is a sounder foundation for regulation than the proposals for an analysis of costs and benefits, which may well lead to less quantification and worse decision making. At the very least, the existing definition of cost benefit analysis should be retained.

Our preference would be for a statutory requirement for the PRA and FCA to estimate both the costs and benefits of proposed new rules: the new legislation should be taken as an opportunity to improve rather than water down the evidence base used in consultations.

The Panel's view is partly informed by its experience of the FSA's current Mortgage Market Review. The statutory requirement on the FSA to estimate costs, which it had failed fully to do in its July 2010 consultation, puts the Panel in a far stronger position to press the FSA for a "robust and credible CBA", a request to which the FSA has now responded.

Consumer Panel

The Consumer Panel believes its function should be retained for the PRA. . The justification given for its removal is that PRA will be taking decisions on prudential matters, and that the PRA will be required to consult the FCA to take advantage of its expertise on consumer issues.

We believe this reasoning is flawed on two counts. First, we believe that prudential matters are as valid a subject for direct consumer input as conduct of business issues. This is particularly the case given that the PRA will have sole responsibility for insurance and for securing an appropriate degree of protection for with-profits policyholders.

Additionally, although the FCA will have consumer expertise, in its relationship with the PRA it will inevitably be balancing a number of different viewpoints, including industry as well as consumer. There is serious risk that the consumer interest will not be given proper consideration.

The PRA will have a statutory duty to put into place arrangements for engaging with practitioners (although what form this will take has still to be decided) – to delegate responsibility for consumer input to the FCA is to place the interests of consumers on a lower footing than that of the industry.

The Panel has in the past been acknowledged as a credible, authoritative and constructive body advising the FSA on prudential as well as conduct of business issues. As mentioned in the context of the FPC, it is currently in a unique position in that it can represent consumer issues while regulation is being developed, before that regulation reaches the public domain. To discontinue a relationship which already exists is to leave a gap in the regulatory jigsaw.

The example of intervention of the Mortgage Market Review was given in the answer to question 1. Other examples of significant interventions by the Panel in the prudential area include:

With profits
The Panel has conducted various research and reviews into the with-profits sector, and has advised the FSA on issues such as a lack of advice available from financial advisers, poor information provided by companies to consumers, inconsistent treatment of different investor groups and concerns about with-profits governance, leading to a steady improvement in the minimum standards of treatment of customers.

Forbearance and Impairment Provisions – Mortgages
The Panel was asked for its advice on the FSA's June 2011 guidance consultation on forbearance and impairment provisions. This resulted in a better balance in the final document between the conduct issues associated with forbearance and the prudential risk issues.

On the basis of the evidence above, the Consumer Panel proposes the following additions to FSMA Chapter 2, 'The Prudential Regulation Authority'.

Arrangements for consulting practitioners *and consumers*

2K The PRA must consider representations that are made to it in accordance with arrangements made under section *2J and by the Consumer Panel, as established in section 1L.*

It is anticipated that the Consumer Panel's primary relationship will be with the FCA, including arrangements for establishment and maintenance, and that the bulk of its resource will be used for FCA-related business, but that strategic input to the PRA would be an important part of the regulatory process.

6. Do you have any views on the FCA's objectives – including its competition remit - as set out in paragraphs 2.80 to 2.90 and in Chapters 3 and 4?

Consumer protection objective

The consumer protection objective is of particular relevance to the Panel. It agrees with the requirements for the FCA to have regard to risk issues, experience and expertise. It particularly welcomes the requirement to have regard to consumers' needs for advice and accurate information, but would point out that information disclosure in itself is not sufficient to ensure consumer protection. Information must be supplied in a format, and quantity, that consumers need and can use to make informed decisions.

We would not argue with the need for consumers to read key information and answer questions honestly, but there is an unacceptable view in some sectors of the industry that complex and potentially detrimental products can be widely promoted, provided they are transparent through good disclosure. This is accompanied by an expectation that consumers can, and should, acquire the skills, knowledge and understanding required to deal with this complexity and choice, which places an unreasonable burden on the consumer and is not an approach adopted by other industry sectors.

There is evidence indicating that providing more information can be counterproductive. The FSA's 2008 report on behavioural economics[8] suggests that 'attention is a scarce resource and processing power is limited' and makes reference to research that indicates that introducing additional information, even if accurate, may lead to worse decision-making outcomes. Further evidence[9] suggests that 'information overload' can lead to procrastination and poor decisions. Therefore the Panel would strongly recommend rigorous testing of any initiatives involving consumer-facing information to ensure it achieves its desired outcomes.

The Panel welcomes the requirement that the FCA must have regard to information supplied by the consumer financial education body (Money Advice Service (MAS)) in the exercise of the consumer financial education function. In support of this it recommends that the Financial Capability Baseline Survey[10] be rerun, either by the MAS or the FCA. However, the presence of the MAS should not absolve the FCA from responsibility in improving the financial understanding of consumers and helping them to engage with the market.

It is no longer possible to function outside the financial services system, not only in relation to transactional services but increasingly in pensions and insurance, as responsibilities in these areas pass from the Government to consumers. Access to financial services is a precondition of functioning in society and needs to be intermediated. The Panel believes that the FCA's third operational objective should be amended to:

'promoting efficiency, <u>access</u> and choice in the market for certain types of services'

The FCA will be well placed to drive real progress in this area.

The definition of 'consumers' in the Bill is extremely broad. In this context, it is the provision in section 1C(2)(b), requiring the FCA to have regard to the differing degrees of experience and expertise that consumers may have which will be the key to ensuring that consumer protection is appropriate and fair, and which can be the means of addressing the potential and actual information asymmetries between providers and customers.

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[8] *Financial Capability: A Behavioural Economics Perspective*, FSA July 2008
[9] *Consumer Decision-Making in Retail Investment Services: A Behavioural Economics Perspective*, Decision Technology Ltd for European Commission October 2010
[10] *Financial Capability in the UK: Establishing a Baseline*, FSA March 2006

The Panel has already voiced its concerns[11] about the position of SME's, and in particular the existing regulatory gap for non-financial businesses that are not given protection by the Consumer Credit Act, by competition policy or by redress mechanisms such as the Financial Ombudsman Service. This gap appears likely to be continued under the new proposals and will need to be addressed if the responsibility to regulate consumer credit falls to the FSA, and ultimately the FCA.

Competition objective

The Panel has previously stated[12], that it believes the FCA should have an objective to promote effective competition that improves consumer outcomes in retail and wholesale markets. We have concerns that section 1B(4), requiring the FCA only to discharge its general functions in a way which promotes competition, when this is compatible with its other objectives, is not a strong enough obligation.

We believe that in order to exercise a competition function effectively the FCA's powers and authority have to be equivalent to those of the sector regulators. The fact that this will not be the case, or the potential for there not to be a super-complaint process, seems a retrograde step, inconsistent with a strong competition mandate. The case for the FCA to have concurrent powers, as do other industry regulators, is to use its expertise to carry out market investigations, with reference to the Competition Commission only if structural change needs to be considered.

7. Do you have any views on the proactive regulatory approach of the FCA, detailed in paragraphs 2.91 to 2.110 and in Chapters 3 and 4?

Product intervention power

In its response[13] to the FSA's recent discussion paper, the Panel set out the consumer outcomes we would like to see from a system of regulatory product intervention:

1. Consumers should be able to buy straightforward outcome products that deliver what they promise including value for money, through all distribution channels including execution only.
2. Those unable or unwilling to pay for a full independent advice service should have access to a process for delivering simplified advice with appropriate levels of consumer protection.
3. Consumers should have access to a wide range of financial products that meet a diverse set of needs and aspirations, that have been subject to appropriate internal and regulatory scrutiny both at the

[11] FSCP response to "*A new approach to financial regulation: consultation on reforming the consumer credit regime*", March 2011
[12] Financial Services Consumer Panel Response to '*A new approach to financial regulation: Building a stronger system*', April 2011
[13] Financial Services Consumer Panel Response to DP11/1: Product Intervention, April 2011

design stage and during subsequent product development, such that regrets and complaints to FOS are minimal.
4. Consumers should have access to fair redress and compensation if things go wrong.

The Panel notes that any FCA actions will need to avoid conflict with those of the European Supervisory Authorities, which also have product intervention powers, and recommends that details of arrangements to avoid such conflict are detailed in the MOU outlining the UK approach to international coordination.

The Panel has responded separately to the FCA approach document. It has concerns in some areas – in particular that the FCA regulatory toolkit will be restricted and will not cover areas such as product kitemarking, product approval, and product authorisation other than for those products authorised under the current FSA regime. This seems contrary to the desire to take full advantage of the opportunity to develop a new approach to conduct regulation.

New financial promotions power

The new provisions to give the FCA powers to take action in the case of misleading financial promotions, and to have a duty to publish the fact that it has done so, are a significant move towards improving regulatory transparency and enabling early action to prevent detriment which the Panel supports. It believes that the regulation of financial products should be no different in this respect to the regulation of other products. Early publication of action would encourage good consumer outcomes within the market and act as deterrent to poor behaviour.

A presumption in favour of publication of specific and identified action in the case of misleading promotions should be included in the Bill, with appropriate timescales.

Early publication of disciplinary action

The Panel supports the new power to enable the regulators to disclose the fact that a warning notice has been issued in relation to proposed disciplinary action. It is important that the wording of this power, as outlined in Schedule 8, paragraph 24 (‘after consulting the persons to whom the notice is given’), does not imply that consent must be obtained to publish information from the party under investigation.

It is also important that the requirement to consult, and to allow firms to make representations, could slow the process and allow consumers to continue making potentially irreversible decisions based on unsuitable or misleading information. We therefore propose there should be a mechanism for the FCA to initiate, and publish details of, immediate regulatory action without consultation with the firms involved, where it considers there is risk of serious consumer detriment.

In addition, we believe the FCA should be able to use information collected in pursuit of its regulatory objectives, (such as complaints data) where appropriate, to inform consumers and promote good behaviour. Section 348 of FSMA currently restricts the FSA's ability to publicly disclose confidential information which is not already lawfully publicly available, relates to the business or affairs of any person and is received by the FSA for the purposes of its functions under FSMA. Currently a person who contravenes s.348 can be fined or imprisoned for a period of up to two years.

The Panel believes the threat of such action acts as an excessive restraint on publication of information which should be in the public domain, and conflicts with the Government's commitment to transparency of the new regulatory organisations[14]. It is difficult to see how this principle can be exercised while the existing s.348 exists, therefore while publication should still be subject to rigorous safeguards the Panel believes the regulator should have the discretion to publish such information where appropriate.

Additionally, we would seek assurance that regulations could be made under s.349(1), in the light of the principle of transparency, that would allow the FCA to publish information it considers would assist consumers to accept responsibility for their actions and would encourage firms to avoid misconduct for fear of disclosure and reputational damage.

8. What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?

and

9. What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?

The Panel believes the FCA should be the lead on competition issues in financial services. In line with this, it welcomes proposals to give specific bodies a statutory role to bring issues of mass consumer detriment to the FCA's attention, and believes it appropriate for all the statutory Panels to have this function. In an environment where consumer bodies are currently under review it is important that an organisation already in place, such as the Consumer Panel, with experience and a specific financial services consumer remit is able to raise issues where others might in future not have the flexibility to use or divert resources in this way. In conjunction with Clause 5, section 1M(2), requiring the FCA to publish a response to representations received from the Panel, this would underline the importance of the consumer voice.

In the wider regulatory environment, there is a potential regulatory gap in the area of super-complaints. If the OFT is to cease to exist in its current form,

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[14] Cm 8012 *A new approach to financial regulation: building a stronger system* , February 2011, para 1.29

and its responsibilities are taken over by the new Competition and Markets Authority (CMA), the question arises of which body will have responsibility for financial services super-complaints which do not relate to competition. This is an area where the FCA could potentially have a role.

10. Do you have any comments on the competition proposals for the FCA set out in paragraphs 2.111 to 2.119 and in Chapters 3 and 4?

The Panel believes that the proposals for competition are overly complex, particularly when compared with other sectors.

As stated in its response to Q 6, the Panel is disappointed that the FCA will not have fully concurrent powers. We continue to endorse the sentiments of the recent BIS consultation[15] that it is necessary to maximise the ability of the competition authorities to secure working competitive markets and to promote productivity, innovation and economic growth.

The Panel recommends a more straightforward framework for the competition environment should include the following elements:

1. The starting point should be that the FCA should (in line with its duty to discharge its general functions in such a way which promotes competition), be the lead on competition issues in financial services. Like other industry regulators it has the expertise and information derived from supervision, and can utilise this information to make informed judgements.
2. The FCA should refer competition issues to the OFT/ Competition Commission when rules cannot be made to solve a problem and structural changes may be needed.
3. It should be possible to address supercomplaints regarding financial services to the FCA, with consumer bodies, including the Panel, able to apply for designated status.

11. Do you have any views on the proposals for markets regulation by the FCA, described in paragraphs 2.120 to 2.123 and in Chapters 3 and 4?

The efficiency and competitiveness of wholesale markets are critical for people with savings and pension funds invested in them. In particular, the proportionality of costs is important as higher transaction costs in these markets mean higher charges for consumers which have an adverse impact, especially when compounded over a lifetime of savings. The Panel has previously stated that the FCA needs the power to intervene to drive down these transaction costs, and remains concerned that it will still lack sufficient tools to do this.

12. Do you have any comments on the governance, accountability and transparency arrangements proposed for the FCA, as described in paragraphs 2.124 to 2.132 and in Chapters 3 and 4.

[15] *A Competition Regime for Growth: a consultation on options for reform*, BIS, April 2011

The Consumer Panel regards its continuing input to the regulatory process as a key aspect of the new regime, and is content that the wording of section 1L is a sound foundation for such input to the FCA.

The Panel is in favour of a drive towards greater transparency of regulation, and as such supports new section 1M(2) requiring the FCA to publish a response to representations received, regardless of whether it is in favour of such representations.

However, as noted in the answers to questions 1 and 5, it believes that an similar duty for the PRA and the FPC should be an integral part of the regulatory process.

13. Do you have any comments on the general coordination arrangements for the PRA and FCA described in paragraphs 2.138 to 2.149 and in Chapters 3 and 4?

The Panel has concerns that the issues of coordination and authority in the way the FPC, PRA and FCA work together may simply replace the multiple objectives that caused confusion in the current structure. These processes and responsibilities must be clarified and resolved. The cost and effort of moving to twin peaks needs to provide something better for consumers.

Memorandum of Understanding provisions between the PRA and FCA must give detailed provision on ensuring coordination with the European Supervisory Authorities (ESAs) of which they are not members (PRA with ESMA and FCA with the EBA and EIOPA), as well as the ESAs of which they are members, to ensure that both prudential and conduct of business issues are addressed across all sectors.

The proposed new structure does not fit well with the European regulatory structure, where all three European supervisory authorities have responsibility for both prudential and conduct of business issues. A possible solution to this issue would be to have a joint European/international team which operates and communicates with both the FCA and PRA. There is a precedent for such a structure at European level, where directorates-general have been split in the past, and the new regulators could learn from these experiences.

14. Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described in paragraphs 2.150 to 2.195 and in Chapters 3 and 4?

Currently, the Bill sets out that with regard to the authorisation of firms undertaking a Significant Influence Function (SIFs) the FCA has to ‘consent’ to the authorisation of firms that are regulated by the PRA. However, the legislation is presently silent on the matter of individuals who exercise a significant influence function. The Panel believes that this will be one of many matters with regard to the interrelationship between the PRA and FCA which will be covered by the memoranda of understanding.

The Consumer Panel has already raised the issue of FCA ‘consent’ to individual approvals with HM Treasury, as given the impact exercised by individuals on the behaviour of firms, this could represent a risk for consumers.

15. Do you have any comments on the proposals for the FSCS and FOS set out in paragraphs 2.196 to 2.204 and in Chapters 3 and 4?

The Bill proposes that responsibility for FSCS should be jointly exercised by the PRA for deposit-taking and insurance business and the FCA for all other financial activities including intermediation, and proposes a number of coordinating mechanisms. The Panel urges the Government to take an active role at EU level in the developments on guarantee and compensation schemes to ensure that consumer protections already in place in the UK are not eroded, and in fact can be used as best practice for development of schemes elsewhere.

Appendix – Consumer Panel responses to public consultations 2011

The Consumer Panel is a statutory body under the Financial Services and Markets Act 2000 and was initially established by the Financial Services Authority in December 1998. The Panel advises the FSA on the interests and concerns of consumers and reports on the FSA's performance in meeting its objectives.

The emphasis of the Panel's work is on activities that are regulated by the FSA, although it may also look at the impact on consumers of activities outside but related to the FSA's remit. More information about the Panel's work is available on its website at http://www.fs-cp.org.uk/

Date	Consultation
2 Sept	Response to Joint Committee on the draft Financial Services Bill call for evidence
1 Sept	Response to FCA Approach document
28 August	Response to Work and Pensions Select Committee call for evidence on NEST and autoenrolment
05 August	Response to FSA CP11/11 Quarterly Consultation no. 29 chapters 5, 6 and &
20 July	Response to FSA CP/11/10 Consumer Complaints: Ombudsman award limit and changes to the complaints-handling rules
04 July	Response to CP11/8** data collection: Retail Mediation Activities Return and complaints data
04 July	Response to the Independent Commission on Banking interim report
01 July	Response to the Review of the UK's regulatory framework for covered bonds
31 May	Response to Guidance Consultation GC 11/10 forbearance and Impairment Provisions - 'Mortgages'
31 May	BIS competition regime consultation final
31 May	Response to quarterly consultation CP 11/7 on consumer redress
2 May	Response to the CP 11/5 Protecting with-profits policyholders
03 May	Response to FSA CP 11/3 Product disclosure
27 April	European Commission consultation on collective redress
21 April	Response to FSA DP11/1: Product Intervention
14 April	Response to the HMT consultation A new approach to financial regulation: Building a stronger system
31 March	Response to the Treasury Committee Inquiry into the Accountability of the Bank of England
25 March	Response to HMT CP: Simple Financial Products
22 March	Response to the joint HMT/BIS consultation on reforming the consumer credit regime
17 March	Response to HMT/FSA consultation document: transposition of UCITS IV

15 March	Response to European Commission CP: on Alternative Dispute Resolution
10 March	Response to FSA CP 11/1: Proposed changes to BCOBS
28 February	Response to DG Markt consultation document: Review of the Insurance Mediation Directive
25 February	Response to HMT CP: Early access to pensions savings
21 February	Response to FSA CP 10/28*** Mortgage Market Review: Distribution and Disclosure
16 February	Response to CP10/29: Delivering the RDR and other issues for platforms and nominee-related services
4 February	Response to FSA CP 11/1: Removal of the requirement to annuitise pension savings by age 75
1 February	Response to consultation document on the Review of the Markets in Financial Instruments Directive
1 February	Response to FSA CP10/26* Pension reform - Conduct of business changes
31 January	Response to consultation by Commission Services on legislative steps for the Packaged Retail Investment Products Initiative

THE FINANCIAL SERVICES PRACTITIONER PANEL

RESPONSE TO HM TREASURY CONSULTATION PAPER
'A NEW APPROACH TO FINANCIAL REGULATION: THE BLUEPRINT FOR REFORM' JUNE 2011

06 SEPTEMBER 2011

INTRODUCTION

The Financial Services Practitioner Panel is the statutory Panel set up under FSMA to represent the interests of practitioners to the FSA. As such, we have a close understanding of policy development at the FSA, and have taken a keen interest in the Government's plans for regulatory reform. The details of the Panel's remit, and its current membership is at Appendix 1.

We would like to start our response with a reiteration of the key points that, from a practitioner point of view, are essential requirements from the regulatory system. Our latest survey of regulated firms which was published in early 2011, showed that the overwhelming majority of firms across all sectors agreed that strong regulation is for the benefit of the financial services industry as a whole.

The most important aspects of regulation are as follows:

1. Clear regulation
Firms need to understand clearly what is expected of them, and for there to be firm and consistent guidance from the regulators on what is required. This is why it is vital that the new UK system is fully joined up, and the new regulators work in an **integrated manner with EU and international initiatives.**

A need for clarity is behind our concern about **judgement led regulation**. We were pleased to see Government support for rigorously evidence-based judgement led decision making in the White Paper. The PRA Approach to Banking Supervision document stated that the PRA will put in place the necessary management and oversight processes to support the judgements required from supervisors and we will continue to engage with the FSA and Bank in their development of the PRA Approach. We urge the Government to continue to emphasise the importance of clarity and consistency in this area.

For the FCA, we are concerned about the wide remit of the FCA, particularly in regard to the **broad definition of consumer** being proposed. We believe this could have a detrimental impact on the operation of wholesale and markets sectors. The FCA must be empowered to make a clear distinction on how it regulates wholesale markets, as too stringent regulation of wholesale and markets risks being counter-productive: it could inadvertently encourage firms to base their wholesale activities in jurisdictions with less stringent regulation, so ultimately undermining the interests of the UK economy and consumers.

On the retail side, the FCA must state more clearly how it will incorporate **consumer responsibility** into its operations. We were disappointed that this was not addressed in the FCA Approach document published in June 2011.

In addition, we believe the FCA should publicly set out its **risk appetite**. The FCA should closely define what type of risk it will be willing to accept, and the type of risk that it will not. This would provide the FCA with a measure of its own performance and allow the FCA to refer to its risk appetite in intervening (or choosing not to intervene) in particular cases.

2. Effective and responsive regulation

The industry is as keen as everyone else for regulators to act firmly and effectively when things start to go wrong: it is the industry as a whole that pays the cost when things go wrong as confidence is undermined, and more directly through payments to the FSCS levy. The recent increase in the levy to provide compensation for the customers of KeyData, has had a significant impact on the bottom line of contributing firms. The FCA will have an increased remit to intervene early, and it must use it to ensure that it acts on issues of detriment in a way that industry can respond to effectively before they reach the size of recent problems with PPI and mortgage endowments.

3. Efficiency and competitiveness

Practitioners recognise that maintaining financial stability has a major role to play in helping firms deliver services efficiently and competitively. However, the cost of regulation in and of itself, as well as the way in which regulatory initiatives impact firms' operations, are also important.

Whilst it is important for the regulators to take strong and effective action, it is also important for them to have an awareness of the impact that their actions may have on the competitiveness of the industry. We believe that, at the very least, there should be an understanding that if the regulators have the choice of two options for action of equal merit, they should select the action which has the least adverse effect on competitiveness. UK firms compete in a global environment, and a lack of regard of regulatory actions on the relative competitive impact of our industry compared to those of competitors situated abroad could have significant long term implications for the presence of the UK and London as a financial centre.

4. Coordination

With the adoption of the twin peaks approach, it is crucial that there is effective coordination of action and requests at all levels – from the detailed point of not overlapping on regulatory visits, up to clear coordination of regulatory approaches. Ensuring effective coordination between the regulatory authorities going forward is key. This has also been highlighted by the IMF in their July 2011 United Kingdom Technical Note, where it stated that: "Balancing the enhanced focus of individual authorities with the checks and balances, and coordination needed on an ongoing basis and in a crisis will be key success factors of the new arrangements[1]" and which recognised that: "…there is also a need for cooperation between the PRA and the FCA in the ordinary course of business[2]". The Panel recommends that the proposed coordination measures are supplemented by a statutory duty to coordinate to be included in the regulatory principles. The aim of this would be to ensure that processes are streamlined as much as possible.

Coordination is all the more important for the UK's input into EU policy development. The new UK system does not fit neatly into the European structures, and yet it is vital that the regulators are able to provide comprehensive and coordinated input into all EU (and other international) policy debates.

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[1] P.19, *United Kingdom: The Future of Regulation and Supervision Technical Note – International Monetary Fund Country Report No. 11/230 July 2011*

[2] Dito

5. Cost effectiveness

It is important to have clear disciplines of budgetary control and effective challenge on spending in the new system. There is a danger of duplication of efforts in the two organisations and this must be controlled. The NAO should take an early and proactive part in monitoring the costs of the PRA and FCA.

Already, we are concerned that assurances of aiming for a cost neutral impact after transition costs are looking unlikely. The Panel strongly supports high quality regulation, but would like to emphasise the importance of ensuring value for money in spending and avoiding throwing away existing valuable initiatives in the proposed new structure for regulation.

Engagement with Industry

As we trust that our responses to the debate on regulatory reform have shown, we believe that effective engagement with industry can help to build better and more effective regulation. We remain concerned about the lack of any requirement for a statutory standing body of practitioners in the PRA, similar to that prescribed for the FCA. Key reasons to have a Panel include the Panel's ability to recognise the impact of regulation across sectors, to provide an overview on coordination between the regulatory bodies and to retain 'corporate memory'.

In addition, there must be clear engagement with industry to provide input to FPC decisions. The FPC will have a hugely significant role in the new structure. The macro-prudential instruments that it will be deploying are relatively untested, and yet have not only economic, but often social consequences. The choice of members of the FPC – their experience and balance of interests – is therefore fundamental to the success of this model as they must provide effective challenge of the Bank's view within the FPC. We welcome the Government's decision to continue to consult on FPC membership during the period of pre-legislative scrutiny.

Our detailed responses to the questions posed in the White Paper published in June 2011 follow.

CONSULTATION QUESTIONS

FPC AND BANK OF ENGLAND

1. Do you have any specific views on the proposals for the FPC as described in paragraphs 2.6 to 2.24 and in Chapters 3 and 4?

The Panel supports the Government's continued intention to require the FPC to balance its objective by the condition that its actions should not have a significant adverse impact on the ability of the financial sector to contribute to the UK economy in the medium or long term. However, we continue to urge the Government to strengthen this by requiring that the FPC to have regard to the competitiveness of the UK financial services industry as a whole when exercising their functions. This is discussed further under question 4 below.

We are also concerned to ensure that the FPC considers fully the practical implications of its requirements on the industry. Given the key role played by the FPC in the new regulatory structure, it is vital that the FPC has access to the appropriate expertise and experience of industry, as well as the resources to enable it to fulfil its duties.

This is particularly the case where the FPC has the potential to impact directly on the regulatory requirements on firms. As such, there must be some means of open debate and questioning of the practical implications of these demands. For instance, with reference to the policy recommendations from the first meeting of the Interim FPC in June 2011, the following policy requirements have a significant potential impact on firms:

1. FSA to ensure that improved disclosure of sovereign & banking sector exposures by major UK banks becomes permanent part of reporting framework (and work with FPC to consider further extensions of disclosure in future)
   Firms already provide a huge amount of information to the regulator, and so it is concerning if the FPC can also demand more information in future, which brings associated costs. There should be an opportunity for a dialogue with the FPC as to whether the requests for additional information are necessary – as there is currently through FSA Consultations.
2. FSA to extend its review of forbearance & associated provisioning practices across UK banks' household and corporate sector exposures on a global basis.
   The FPC presumably recognises that this impacts both conduct and prudential regulation. The FPC is leaving the FSA to decide which lenders it is appropriate to proceed with, and it is important that the FPC going forward recognises constraints such as these and does not dictate exactly what regulator must do. For instance, if the FPC suggested the FCA must request firms to amend their conduct and regularly report on management of mortgage forbearance with their customers, firms would not be able to challenge the FCA: the need for such action would be justified by the requirement of the higher level FPC.
3. Advises UK banks that during transition to new Basel II capital requirements, they should take opportunity of periods of strong earnings to build capital so that credit availability is not constrained in periods of stress.
   Here the FPC is issuing advice to banks directly, without going via one of the other regulators who have a duty to consult with industry.

The Panel recognises the importance of ensuring the FPC has access to the right sort of macroeconomic tools. Industry could provide valuable input in the development of these, and we would strongly encourage the regulatory bodies to reach out to Practitioners in developing these instruments.

We also agree with other previous respondents who have argued that the currently proposed FPC membership is overweighted towards the Bank. As such, we welcome the Government's decision to gather views on this issue over the period of pre-legislative scrutiny. We believe that more consideration needs to be given to the balance of membership of the FPC, and its degree of control by the Bank of England. We question why the FPC is proposed to be a sub-committee of the court of directors of the Bank, when the MPC is a separate committee in its own right. It will be important that the FPC provides independent views and challenge to the Bank, PRA and FCA on all their contributions to financial stability.

We are particularly concerned about the power vested in the Governor of the Bank of England under the current proposals According to the proposals, the Governor of the Bank of England will be Chairman of the MPC, the FPC and the PRA, in addition to having the role of sitting on the FCA board and maintaining oversight of the bank resolution regime. There are strong views in the industry that such a large concentration of power in one individual in one organisation is a cause of concern and arguably an over-reaction to the criticisms of the previous tripartite regime. The Panel strongly believes that there needs to be greater clarity on this subject, and as such welcomes the ongoing investigations by the TSC into the accountability of the future Bank of England as a regulator as well as that of the FCA.

2. Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payment systems as described in paragraphs 2.32 to 2.40 and in Chapters 3 and 4?

We note the Government's decision to move the regulation of RCHs to the Bank of England; however, we are concerned about the implications for vital European regulatory developments and associated negotiations. Under these proposals, effective representation of RCHs in debates in Europe could be undermined, as the FCA (and not the Bank) will be responsible for representing markets and CCPs at ESMA. This is despite ESMA being responsible for such things as the drafting the technical standards under EMIR. It will be vital, at the very least, for the proposed statutory MoUs to cover RCH representation via the Bank.

We also question whether the new Bill needs to confer new powers on the Bank to impose disciplinary measures on RCHs, particularly as there is no evidence of market failure being attributable to the actions of RCHs and RIEs. Notwithstanding that, we believe that if such powers are to be imposed, adequate checks and balances must be put in place that are **at least equivalent** to those that currently exist for those firms authorised under Part IV of FSMA.

3. **Do you have any comments on:**
   a. **The proposed crisis management arrangements; and**
   b. **The Proposals for minor and technical changes to the Special Resolution regime**

   As described in paragraphs 2.41 to 2.44 and in Chapters 3 and 4?

Although we are pleased to see a clear authority and responsibility for crisis management action in the event of a future crisis, we remain concerned about the amount of power and responsibility vested in the Governor of the Bank of England. We question whether giving a single person so many different roles is the best answer to the coordination problems exposed in the last crisis. As noted in our answer to Q1, the Governor will have a large number of extremely significant roles in the new structure. In relation to crisis management, the Governor also has a significant role in the Special Resolution Regime, and there is a potential for conflict in these two roles.

We would ask the Government to consider if greater scrutiny of the role of the Bank of England is necessary in order to be assured that all the roles of the Governor can be carried out effectively.

PRUDENTIAL REGULATION AUTHORITY (PRA)

4. **Do you have any comments on the objectives and scope of the PRA, as described in paragraphs 2.46 to 2.61 and in Chapters 3 and 4?**

The Panel strongly believes that the regulators should have a specific requirement to consider competitiveness in its own right. We therefore disagree with paragraph 2.51, which states that financial stability, supported by a rigorous and effective regulatory framework provides a strong platform for industry growth, which will in turn foster a competitive industry. In our view, this is necessary but not a sufficient condition for arriving at the appropriate regulatory stance. We believe that competitiveness and financial stability are complementary goals and not competing ones. However, a lack of regard of regulatory actions on the relative competitive impact on our industry could increase firms' costs unnecessarily, and in the extreme, could even encourage firms to locate more of their operations abroad and could have significant long term implications for the presence of London as a financial centre. Given the contribution made by the British financial sector to the UK economy as a whole, we regard the inclusion of competitiveness as key.

A strong regulator with regard to competitiveness (as well as proportionality) should lead to a reasonable and not overbearing level of regulation by the PRA. This will be important for all, because if it becomes considerably more expensive or cumbersome for firms to conduct their operations in the UK, they may consider moving all or part to countries where regulation is significantly less demanding, and attempt to sell in products and services. This is not in the interest of the UK economy, consumers or firms.

We support the Government's commitment to a flexible approach in the objectives of the PRA in order to allow the PRA to focus on the specific needs of particular firms. The new recognition in the objectives that the insurance sector is significantly different from the banking sector in nature is welcomed. However, this brings a very different skill requirement into the PRA in considering the needs of consumers. The Government has included a recognition that the PRA will need to consult with the FCA in this area, and so it remains unclear what the 'policyholder protection' objective means in practice for the PRA, and we look forward to seeing greater detail on this area as the Bill is debated.

5. Do you have any comments on the detailed arrangements for the PRA described in paragraphs 2.62 to 2.78 and in Chapters 3 and 4?

The Panel has supported the development of judgement-led supervision, only if there are strong systems in place to ensure that the decisions are made according to recognised principles and are consistent over time. We were pleased to see that in the PRA Approach to Banking Supervision document published in May 2011, it stated that the PRA will put in place the necessary management and oversight processes to support the judgements required from supervisors in its approach. The Panel would welcome greater detail on how these processes will be developed and approved, and believes it would be helpful for the FSA/PRA to consult on these.

There must also be clear mechanisms for challenging outcomes under this approach. We note that the Government is now proposing to leave the Tribunal's scope of review of supervisory decisions unchanged. However, we remain concerned about the curtailment of the Tribunal's powers if it chooses not to uphold the relevant regulator's decision. We believe that the Tribunal provides an important check and balance on the regulator. We would like to see it retain all its powers, or if not , for the PRA to have to report back and gain approval from the Tribunal on how it proposes to reconsider matters rejected by the Tribunal in the light of the Tribunal's findings.

We also continue to believe that there should be the development of an informal and confidential appeal process in the regulators going forward which would be a mechanism for judgement-led supervision to be challenged, and which would contribute to ensuring greater consistency across regulatory judgements and cases.

We continue to believe that there should be a statutory Practitioner Panel for the PRA, as well as for the FCA. This was also recognised by the majority of respondents to the last consultation. As stated on page 377 of *'A New Approach to Financial Regulation: the Blueprint for Reform'*, 'almost all respondents [to the February consultation] argued that the PRA should retain the Practitioner Panel in its current form'. A detailed paper on the arguments for a statutory body is at Appendix 2 of this response. The three key advantages are listed below:

a) A statutory standing body of practitioners representing the wider industry would be able to *recognise the impact of regulation in one sector on another*. Specialist ad hoc groups drawn together for e.g. the purposes of giving input on regulation in the mortgage market would not appreciate the potential impact that same regulation could have in other sectors.
b) A standing body could comment on and therefore contribute to more effective *coordination between different regulatory bodies*. It could monitor how successfully they coordinate and provide feedback on an ongoing basis. This would work best with a Panel that has some overlapping membership or coordination requirements with the FCA practitioner panels.

c) A statutory standing body of practitioners would have a '*corporate memory*' and so recognise links and repetitions over time that may not be obvious to ad hoc working groups.

The FCA Approach document published in June 2011 has recognised that specific engagement with industry can be a valuable tool in improving the quality of regulation. The PRA Approach to Banking Supervision makes clear that despite increasing regulatory initiatives being created at an EU level, the Bank of England and the FSA expect the PRA to be involved in policymaking in a range of areas. As such, we believe it would benefit from the expertise of a statutory standing body of Practitioners in assessing the impact of proposed new regulation and advice on industry and consumers.

The most important aspect of such a PRA Practitioner Panel would be to consider and advise on the most effective way for the PRA to implement regulation. For the avoidance of doubt on this matter, we would stress that this is not an accountability of regulators point, but an engagement point. Therefore, we would like to suggest that the wording of new sections 2J (2) and 2K (1) are amended as follows, with insertions flagged in bold type:

2J The PRA's general duty to consult
(2) Those arrangements ~~may~~ ***should*** *include the establishment of ~~such panels as the PRA thinks fit~~* ***a Practitioner Panel to provide a regular forum for policy debate with a cross section of senior representatives of those firms regulated by the PRA and to consider the cumulative impact of regulation by the PRA and FCA on firms.***

2K Duty to consider representations
(1) The PRA must consider representations that are made to it in accordance with arrangements made under section 2J, ***but the PRA will not be accountable to practitioners for its decisions having considered the representations.***

FINANCIAL CONDUCT AUTHORITY (FCA)

6. Do you have any views on the FCA's objectives – including its competition remit - as set out in paragraphs 2.80 to 2.90 and in Chapters 3 and 4?

In theory, the overall strategic objective and operational objectives of the FCA seem sensible and we support the thrust of the Government's proposals. However, we have grown increasingly concerned about how these overall objectives will be interpreted.

The White Paper points to more detail being made available in the FCA Approach document, published in June. Although much of that document sets out a balance approach, we were somewhat concerned at the tone of conference that the FSA held to launch that document. The tone of debate at the launch conference seemed to concentrate on criticism of the industry, rather than adopting a more constructive and forward-looking tone. Having made this point, we appreciate that there was only a short time period for the FCA Approach conference to be developed and that the new FCA Chief Executive has only started work this month.

The FSA has said[3] that the FCA's interventionist stance and lower tolerance for consumer detriment is likely to result in more enforcement cases. We would wholeheartedly support this approach if it targets clear examples of non compliance where there is potential detriment for example, 'boiler rooms' and other unregulated financial services including money lenders. However, if this refers to all regulated firms, the FCA is starting out with an extremely pessimistic presumption about the impact of its new approach on its regulated firms. Building on the exisisting conduct initiatives, for example, around Treating Customers Fairly should mean that the proposed product intervention and a more proactive approach to regulation will result in less, not more, enforcement cases. If the FCA interprets its objectives in this way, there is a real danger that the FCA will undermine rather than enhance confidence in the UK financial system..

We would appreciate further commitment from the Government that the FCA must take a proportionate, balanced and constructive approach, whilst carrying out robust challenge. This is all the more important as the FCA will have a crucial role in the regulation of the wholesale and markets arena, where it will be important for the UK's international reputation that the regulator is seen to have a constructive approach.

One area that we believe needs further emphasis and clarification is in the inclusion of consumer responsibility as a key principle of 'have regard' for the regulator. We were disappointed that there was no discussion of how the FCA will carry forward this responsibility in the FCA Approach document published in June. Although there must be clear safeguards of protection and information especially for retail consumers, it is key for the FCA to make clear that consumers will be responsible for some aspects of the decisions they make.

The Panel is concerned that a broad definition of consumers along the line that has been proposed does not make sufficient distinction between retail and professional consumers of financial services. Although we welcome partial assurances that different types of consumers will still receive different regulatory protection and treatment, there are great concerns around ensuring that this is the case in practice. It is vital to recognise that retail consumers need much higher levels of protection than professionals, the latter having much greater understanding of risk and the nature of the products they propose to buy. A failure to ensure such a distinction could have serious implications for innovation and efficiency in wholesale markets. As a Panel, we have often challenged the FSA on a tendency towards "one size fits all" regulation. We are concerned that this universal definition of consumer will further encourage such an approach.

We are generally supportive of the proposed competition powers, although we are concerned about price intervention powers for the FCA. For instance, we would like to see strict, set criteria for the FCA taking action on price when there is significant evidence that competition is impaired. The FCA Approach document reads: "The FCA will thus consider exercising its powers to take action where costs or charges are excessive". There are concerns around when and how such judgements would be made, and are keen to see greater detail on how this is proposed to work in practice before giving it our full support.

We continue to maintain that the regulators should each have the duty to coordinate set in their regulatory principles. Although there is an overall statutory duty, we believe it is the

[3] FCA Approach, published by the FSA June 2011 pages 7 and 25.

objectives and principles which will be used to guide the day to day operations of the regulators. An example of this is in the FCA Approach document, published in June – this considers how the FCA will approach its objectives and the regulatory principles, but does not consider the statutory duty to coordinate.

7. Do you have any views on the proactive regulatory approach of the FCA, detailed in paragraphs 2.91 to 2.110 and in Chapters 3 and 4?

The new product intervention powers being proposed for the FCA should be considered as just one of the range of tools which the regulator will have at its disposal in achieving its objectives. We have concerns around how this power will be used and the liabilities that could arise. The Government needs to clarify the implications for the regulator and firms should the regulator approve a product which is subsequently proven to be unsafe, or restrict the use of a product that is subsequently shown to be safe. In cases where either firms or consumers suffer detriment as a result of the regulator's actions, it is unclear what the regulator's liabilities and legal obligations would be.

We are concerned that product intervention is being promoted as the new "magic bullet" answer to improved consumer protection. We acknowledge that it will be useful for the FCA to have tighter powers to control any product that can and does do harm, through greater regulation at source with the product provider, However, this should not risk the FCA deciding to discard all the investment that the industry has made in previous regulatory initiatives such as Treating Customers Fairly(TCF). Often it is not the product which is wrong but the fact that it is sold beyond the target audience for which it was designed. In this regard, the Retail Distribution Review, itself a very substantial change across industry and the regulatory regime, aims at improving the product/customer outcomes and further product intervention would seem inappropriate without first bedding in the investment made in the RDR.

In terms of ensuring value for the money, the Panel recognises the increased costs of keeping a large number of firms relationship-managed moving forward, but believes relationship management can be a key component of effective regulation. We do not believe that the plans for the FCA to use business analysts and call centres, in place of much of the direct supervision of firms currently undertaken by the FSA, will lead to an improvement in regulation. We believe that it could result in lower quality staff and regulation, as the supervisors have less direct contact with firms and less practical knowledge of the industry and its clients.We appreciate that a balance has to be struck between relationship management and costs depending on the size and complexity of firms.

The Panel would recommend the FSA conduct a cost benefit analysis on the merits of sustaining the current level of relationship managed firms going forward to ensure that the balance is struck at the right level. Our Biennial survey of regulated firms, published in February 2011, showed that firms understand and appreciate the FSA's policies and objectives much better when they have direct contact.[4] We believe that strong and proactive supervision can only be built on supervisors' ongoing knowledge of firms, their people and the sectors in which they operate. We believe that the benefits in terms of effective supervision are greater than the costs. We would advocate stripping back the central resources and theoretical business analysis, in favour of greater quality of direct supervision.

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[4] Financial Services Practitioner Panel Sixth Survey of the FSA's Regulatory Performance, February 2011.

We also believe that the Government should encourage the FCA to set out its risk appetite in public as a key part of its operational model. The White Paper states that the FCA will have a 'lower risk threshold for potential consumer detriment'. In order to assess its own effectiveness over the longer term, the regulator will need to more closely define what type of risk it would be willing to take, and the type of risk that it would find unacceptable. This would provide the FCA with a yardstick with which to measure its own performance, allowing it to refer to its risk appetite in intervening (or choosing not to intervene) in particular cases. It would also enable the Government, Parliament, and the wider public, to understand the target level of protection being set by the regulator. We note that the PRA has made clear that it will not be a "zero failure" regime. However, this has not been made so clear for the FCA, and yet there needs to be clear understanding of the level of consumer protection that the FCA is hoping to achieve in the event of any future crises.

We continue to be concerned about the Government's proposals for early publication of disciplinary action. We acknowledge that there will not be a duty on the regulator to publish, and the power will be subject to certain safeguards. However, we nevertheless are sceptical of how the safeguards will be operated, and whether all the implications will be considered. It may be that the publication of a warning notice may mislead consumers and result in detriment if they decide to exit a firm's product or service early, when in fact no issues are proved to exist. There is also the possibility of legal hazards for the regulator if the publication of a warning notice has led to losses for consumers, shareholders and staff. One example is the publication in 2010 of the FSA investigation into the activities of Gartmore fund manager Guillame Rambourg. There was a resultant outflow of assets and reduction in the share price of Gartmore, following which it was acquired at a lower price by the rival asset manager Henderson .

It will be essential that at the very least, the safeguards on consultation and fairness on the publication of warning notices are complied with fully by the regulators. We would also like to see a commitment to a public review of the use of this power by the regulator, after a number of cases have been publicised.

8. What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?

The Panel is supportive of the intentions behind allowing nominated parties to refer to the FCA issues causing mass detriment, and can see advantages to both consumers and industry in having a set system in referring issues that have been identified as causing consumer detriment in the market.

We would be interested in exploring this further, particularly as it is suggested that the FCA Panels may have a role here. We would be interested in engaging in further discussion on whether this would be an appropriate form of whistle blowing from the Practitioner Panels if they felt that the regulator was not taking appropriate action in areas of potential or actual consumer detriment.

However, it is key that any consumer redress powers are implemented in the right way. The FCA must have robust processes in place to ensure that referrals from nominated parties are dealt with fairly according to set criteria, transparently and that there is an informal mechanism for appeal for firms. From a resource perspective, it will also be vital for the FCA's own efficiency and effectiveness that it has clear systems and criteria in place to deal with referrals, in order not to get overwhelmed by requirements to look into a large number of complex products in minutiae. It is also important to consider how the FCA might measure detriment, as potential detriment may be difficult to assess and vary at different points in a product's life cycle.

9. What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?

The Panel supports this proposal subject to the caveats highlighted in question 8. As in the discussion on warning notices (see question 14), it would oppose any proposal to prejudice ongoing specific investigations.

10. Do you have any comments on the competition proposals for the FCA set out in paragraphs 2.111 to 2.119 and in Chapters 3 and 4?

The Panel supports the competition powers currently proposed for the FCA. Giving the FCA powers to refer competition matters to the OFT where appropriate seems sensible. The Panel agrees with the decision not to provide FCA with concurrent competition powers, as we believe this could raise concerns around duplication and coordination between multiple regulatory competition authorities.

11. Do you have any views on the proposals for markets regulation by the FCA, described in paragraphs 2.120 to 2.123 and in Chapters 3 and 4?

We welcome that the listing authority will remain within the FCA. However, we are concerned that the listing authority will come under the general framework of the FCA - and therefore lose its requirement to have regard to the international competitiveness of the UK. We suggest that either the listing authority retains its separate framework and objectives, or the FCA should have a fourth operational objective to "have regard to the relative attractiveness of the UK's markets" (as a replacement for "competitiveness"). We believe that the UK could be put at a serious competitive disadvantage to other global financial centres if this is not done.

We welcome the Government's decision not to proceed with its original plans to dismantle the tailored regime for regulating exchanges and CCPs ("Recognised Bodies") and instead to carry forward the Recognised Body regime in the Financial Services Bill. 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 and have provided an effective framework for the maintenance of fair and orderly markets.

It is important to remember that this 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.

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 have run counter to those established international standards and would have raised 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.

Whilst we therefore welcome the Government's decision to retain the Recognised Body regime, we also note that the Financial Services Bill includes amendments to the regime (e.g. powers to fine and publicly censure Recognised Bodies, increased rule making powers and changes to the existing power of direction over Recognised Bodies). Such changes could, depending upon how they are operated in practice, radically alter the nature of the cooperative relationship between Recognised Bodies and the statutory regulator, whereby the statutory regulator and the Recognised Bodies are currently partners in regulation. Changing the nature of the relationship between the statutory regulator and Recognised Bodies could prove to be counterproductive if it were to undermine the ability of the statutory regulator and the Recognised Bodies to work together effectively – making use of their respective knowledge, powers and regulatory reach - in the interests of the efficacy of the regulatory system as a whole.

We therefore do not see the justification in the proposals both to simplify the process for issuing directions to RIEs, and also making it easier for the FCA to abbreviate the process altogether. It is not reasonable to do both, and suggest that if there is a change to allow a shorter process, then the rest should be retained as currently worded in s.296 and 298 of FSMA.

We also do not believe that the FCA being given new powers to impose disciplinary measures on RIEs, including public censure and financial penalties is justified. As with RCHs (Question 2), we do not support this, and we do not see what failures have occurred that would justify this increase in power. If the powers must be introduced, they must come with adequate checks and balances that are **at least equivalent** to those that currently exist for those firms authorised under Part IV of FSMA.

We also do not see any historic justification or evidence of market failure that would support the proposal to allow the FCA to request Skilled Person Reports (s166 reports) from both RIEs and listed issuers. The Government must be careful not to over-burden the UK's wholesale markets in comparison with other competitors in the global arena.

In conclusion, the Financial Services Bill must avoid undermining the basis on which legitimate business is conducted today. There is a danger that technical modifications to the current FSMA regime will inadvertently remove the legal basis for some of this business. For example, as a consequence of moving from a unitary regulator to a "twin peaks" regime, the Financial Services Bill would remove the FSMA provision (section 285(2)(b)) under which exchanges currently operate "cleared only" services. The legal basis for the future operation of such services is therefore unclear as a result of the Financial Services Bill (e.g. whether such services can continue to be operated by an exchange or whether they can only be operated by an entity which has CCP status). Clarification is needed before the Financial

Services Bill enters the legislative process in order to avoid damaging unintended consequences.

12. Do you have any comments on the governance, accountability and transparency arrangements proposed for the FCA, as described in paragraphs 2.124 to 2.132 and in Chapters 3 and 4?

The Panel welcomes the proposed statutory roles of the four Panels going forward under FCA. It further believes this could be complemented not only be statutory Practitioner Panel representation in the PRA (see answer to question 5), but also a Practitioner Advisory Body to look across the FCA, PRA and the FPC. This would comment even more effectively on the coordination between the regulatory bodies and pick up read-across from regulation in the prudential, conduct and macro-economic areas.

The Panel welcomes transparency in the regulatory bodies, and is happy to publish its minutes for the purposes of transparency.

PROCESSES

13. Do you have any comments on the general coordination arrangements for the PRA and FCA described in paragraphs 2.138 to 2.149 and in Chapters 3 and 4?

The Panel is fully supportive of the proposed duty for the FCA and PRA to ensure co-ordinated exercise of functions in FSMA going forward, as well as the references to the need for each regulator to use their resources in the most efficient and economic way, ensuring that burden and restrictions that are imposed are proportionate to the benefits. It is vital that the UK is able to present a united front in European negotiations, and this will need a coordinated effort, as the split of UK regulators is not mirrored in the European structures,

We support the requirement for the two authorities to publish a MoU on the topic of coordination, as well as the new requirement that the PRA and FCA must include in their annual report an account of how they have coordinated during the year. We suggest that this could be strengthened by a requirement to include, or respond to commentary from, the Independent Panels (both Practitioner and Consumer) on their views as to whether coordination is effective, and any problems that have been identified over the year.

In addition, given the importance of ensuring effective coordination between the two authorities going forward, the Panel believes that there need to be further provision for joint working on a day-to-day level. The Panel recommends that the proposed coordination measures are supplemented by a statutory duty to coordinate to be included in the regulatory principles. The aim of this would be to ensure that processes are streamlined as much as possible. We strongly welcome proposals to streamline such processes in relation to firm authorisation and individual approval, and believe that similar coordination should also be extended to processes in the areas of handbooks, assessment of firms' systems and controls, and assessment of firms' business models.

14. Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described in paragraphs 2.150 to 2.195 and in Chapters 3 and 4?

The Panel strongly supports any proposal that is aimed at reducing any conflicting requirements coming from the two regulators in future. Therefore, we support the new proposal for the PRA to lead on firm authorisation for dual regulated firms, and plans to align the timetable of authorisation of a new firm and approval of persons conducting controlled functions in that firm for efficiency reasons. The Panel further welcomes the requirement for the regulators to consult each other before making new rules in order to ensure that each is aware of the potential prudential/conduct implications of such rules.

The Panel does however have serious reservations around the publication of early warning notices, although it welcomes the additional safeguards proposed in the new FCA document and the Bill. Our concern is that even with the requirement to consult the relevant person before publication, there are serious potential regulatory and legal, as well as moral, implications of proposals to publish such notices before a person has been proven guilty.

Whilst we remain sympathetic to the supposed rationale behind the proposal – to ensure that consumer detriment is minimised in cases where the regulator suspects a person/product of being not being up to standard – this could have significant negative implications for both firms and consumers. In cases where consumers hold a given product and then see a warning notice, they may feel compelled to sell at a fire-sale price. Should the product subsequently be shown to be safe, consumers may have suffered financial detriment, in addition to the detriment of restriction of product choice (since the product is then unlikely to be able to be sold in any case).

COMPENSATION, DISPUTE RESOLUTION AND FINANCIAL EDUCATION

15. Do you have any comments on the proposals for the FSCS and FOS set out in paragraphs 2.196 to 2.204 and in Chapters 3 and 4?

Although we support the continuation of the overall operating model for FSCS, we are concerned that the funding requirements for FSCS have the potential to cause systemic risks for certain sectors of the industry which are called on to fund significant levies. We believe that the FCA should not keep the arms length approach that the FSA has taken on the impact of FSCS funding on the viability of firms. The FSA is due to review FSCS funding once EU plans for compensation are clearer. This review will be significant, and key lessons need to be learned and taken on board from previous regulatory failure (including KeyData and PPI) by the new regulators.

In terms of Financial Education, the Panel has highlighted the lack of cost control on the set up of the Money Advice Service with the FSA. We agree that informed and educated consumers are better consumers and provide better consumer outcomes. However, any initiatives to educate consumers must be created in the context of providing value for money. As the funding will be from industry, we believe there must be public discussion of the costs and benefits of the Money Advice Service. This should be made much clearer in this new legislation.

APPENDIX 1

ROLE AND REMIT OF THE PRACTITIONER PANEL

1. The role of the Practitioner Panel is to advise the Financial Services Authority on its policies and practices from the point of view of the regulated community. It has statutory status under the Financial Services and Markets Act 2000 (FSMA). As such, the Practitioner Panel is given access to the FSA's plans for new regulatory policies, and so is able to provide an important sounding board for the FSA before the ideas have been made public.

2. Members of the Practitioner Panel are drawn from the most senior levels of the industry, with the appointment of the Chairman being formally approved by the Treasury, to ensure independence from the FSA. The members are chosen to represent the main sectors of the financial services industry as regulated by the FSA. The Panel currently has senior practitioners from the retail and investment banks, building societies, insurance companies, investment managers, financial services markets, custodians and administrators.

3. The Chairman of the FSA's Smaller Businesses Practitioner Panel (SBPP) sits ex officio on the Practitioner Panel to ensure co-ordination, but debate on issues specifically affecting smaller firms are covered by that Panel. The SBPP is submitting a separate response to this Consultation.

4. The names of the members of the Practitioner Panel as at 1st September 2011 are as follows.

Russell Collins (Chairman)	Partner, Deloitte LLP
Graham Beale*	Chief Executive, Nationwide Building Society
Joe Garner *	Head of UK Retail Bank & Deputy Chief Executive, HSBC Bank plc
Paul Geddes*	Chief Executive, RBS Insurance
Colin Grassie	CEO, Deutsche Bank UK
Mark Harding	Group General Counsel, Barclays Bank PLC
Simon Hogan	Managing Director, Institutional Equity Division, Morgan Stanley
Garry Jones	Group Executive Vice President & Head of Global Derivatives, NYSE Euronext
Guy Matthews	Chief Executive, Sarasin Investment Funds (SBPP)
Helena Morrissey	Chief Executive Officer, Newton Investment Management
John Pollock*	Group Executive Director, Protection & Annuities Legal & General
Andrew Ross	Chief Executive, Cazenove Capital Management
Malcolm Streatfield	Chief Executive, Lighthouse Group
Paul Swann	President & Chief Operating Officer, ICE Clear Europe
Doug Webb	Chief Financial Officer, London Stock Exchange Group

* Member from 1st September 2011

APPENDIX 2

THE FINANCIAL SERVICES PRACTITIONER PANEL

Smaller Businesses Practitioner Panel
Financial Services Authority

JULY 2011

THE NEED FOR A STANDING BODY OF PRACTITIONER REPRESENTATIVES AT THE PRA

INTRODUCTION

This briefing is written on behalf of both the Practitioner Panel and Smaller Businesses Practitioner Panel, the current practitioner panels for the FSA. It is based on our knowledge and understanding of the contribution that the Panels make to regulatory policies, and we would like to contribute further to the ongoing debate concerning the need for statutory standing bodies for the proposed PRA. We recognise that these opinions might be viewed as being self serving; however, we do not believe that we have particular vested interests in the Panels continuing: members of the Practitioner Panel serve to make a personal contribution to the regulation of financial services and are unpaid (while the members of the SBPP receive only a small fee) and normally serve a maximum of two terms of three years each.

THE CURRENT PROPOSALS

The White Paper on regulatory reform published in June 2011 ("A new approach to financial regulation: the blueprint for reform") correctly distinguishes accountability (for example, to Boards/Court and Parliament) from engagement with stakeholders (for example, to Practitioners, Consumers). The White Paper is clear on the need for statutory Practitioner, Smaller Business Practitioner and Markets Panels for the FCA. However, whilst the White Paper proposes to give the PRA a statutory duty to put in place arrangements for engaging with practitioners, as drafted there will be no specification of what those arrangements might be. Therefore the arrangements would be at the discretion of the PRA and the Bank of England. The White Paper also indicated that the Government will continue to consider these arrangements in the light of further consultation and PLS.

As the current statutory practitioner panels of the FSA, we wanted to set out what our experiences indicate are the advantages of having a statutory standing body of practitioners with strong links to the FCA Practitioner Panels, possibly in the form of a statutory Panel, and also what we see as the disadvantages of not having such a forum for the PRA.

We believe that engagement with the industry at an early stage of policy development has significant benefits for regulators as well as firms. The Government has recognised this in the proposed structure for the FCA, but not in the PRA, although the reasons for the distinction are not articulated clearly and the distinction seems to us to be misguided , particularly as each body has the same policy-making functions. We believe that such a structure for industry consultation via a standing body is not relevant only to the FCA: it should also be incorporated into the set up of the PRA.

We do not accept that setting up a standing body for the PRA would increase the risk of "regulatory capture" given the powers and responsibilities of the regulators enshrined in the legislation. In this regard, we welcome the comments of Hector Sants in his speech to the PRA conference on 19 May 2011: "Avoiding regulatory capture does not mean, however, that the PRA will not engage with the firms it regulates. In particular in making its rules, the PRA should do so in full understanding of both their impact and the industry's perspective. It will accordingly set up the necessary consultation mechanisms to ensure the right people in industry are involved. Where necessary this could include standing advisory committees. Furthermore when it makes its rules it will set out their purpose in a clear and straightforward manner."

DISADVANTAGES OF NO STATUTORY STANDING BODY/PRACTITIONER PANEL

We believe that there are distinct disadvantages in not having a statutory Practitioner Panel with strong links to the FCA Panels at the PRA, even if there were to be either standing bodies or ad hoc groups gathered together for specific aspects of PRA regulation at the discretion of the PRA and the Bank. The main disadvantages of non statutory ad hoc groups or standing bodies are as follows:

- Groups drawn together for specific issues will only be focussed on that part of regulation and so may not recognise the impact that such an action may have on other aspects of the system, its interaction with other rules already in place or in prospect or the opportunities for coordination and economies of scale in implementing different changes at the same time. For example, there has recently been considerable debate about the fit between Basel III (and its requirement for banks to lengthen the maturity of their liabilities) and Solvency 2, which may make holdings of bank term debt more expensive, and hence less attractive, to insurance companies. These linkages could well be missed by two single sector groups.
- The division of regulatory issues into Conduct and Prudential at the FCA and PRA, whilst it may be a useful construct for supervisory purposes, is somewhat artificial: from the viewpoint of practitioners (and government), it is the cumulative impact of regulation that matters, especially in regard to maintaining financial stability, protecting consumers and ensuring the UK has an internationally competitive financial services industry.
- The 'corporate memory' of the Panel means that they may recognise links and repetitions that may not be obvious to ad hoc groups, and would be able to look at the impact of proposals when combined with FCA rules or proposals if there was strong linkage, or even some common membership with the FCA Panels. Although standing bodies might achieve this, we believe that a statutory basis with a link to the FCA Panels would make the standing bodies much more effective.
- Deciding when an ad hoc body is needed or not could result in not having industry input precisely when it could be most beneficial, for example in making the case to the European Union regulatory bodies for regulations which can be properly applied

in the UK, given its unique financial markets which is evidenced at the moment in the debate on maximum harmonisation of bank capital rules;

- Setting up various bodies will be time consuming and potentially inefficient. It also runs the risk of "missing the boat" insofar as engagement with EU policymaking is concerned.

REMIT OF A STATUTORY PRA STANDING BODY/PANEL IN THE NEW REGULATORY STRUCTURE

There are particular areas in the PRA's remit which would provide opportunities for engagement with a Practitioner Panel as follows:

- The PRA's future approach documents set out PRA responsibilities in regard to policy making. It says that the PRA will seek to ensure, wherever possible, that its policies and rules are straightforward, clear in intent, robust and support timely interventions. The PRA's policy documents will explain the underlying purpose of its policies and rules. And the PRA will, wherever possible, include clear statements of purpose when setting rules to ensure that firms and the market more generally understand the reasons behind the policy. All these commitments would benefit from a regular and informed dialogue with a specific group of practitioners who also have links to the FCA Panels.
- The PRA's (new) policyholder objective with regard to insurers gives the PRA a broader remit which needs to be considered and may require wider debate on the implications of proposed policy changes.
- The PRA's responsibility for designating Significant Influence Functions (SIFs) would benefit from debate with practitioners.
- The PRA will be the gateway to European and international regulation, and practitioner engagement on negotiating issues could be useful to the PRA.
- The PRA Panel could assist in providing feedback on the practitioner experience of coordination between the two regulators, particularly if it was set up with close links and some common membership with the FCA practitioner panels.

POTENTIAL REMIT REGARDING THE FPC AND BANK OF ENGLAND

The potential for engagement directly or indirectly with the FPC on financial stability issues as they impact on the PRA should also be considered. We believe this is particularly important in respect of the proposed macro-prudential policies. It can be illustrated by considering those in the interim FPC's first minutes of June 2011. The FPC made several recommendations including specific ones on banks' forbearance practices and on funding structures such as collateral swaps employed by exchange traded funds. In our view, the assessment of the impact of such policies in advance, but more importantly ensuring the implementation of such policies, would benefit from the expertise and knowledge of practitioners, especially understanding the transmission mechanisms and indirect effects, which will be crucial to their success.

In a speech at the British Bankers' Association's Annual Banking Conference on 29 June 2011, Paul Tucker (Deputy Governor for Financial Stability), talked of the broad approach of the PRA. He said that the supervisor will not "... treat firms as islands. They are part of a system. So, at the very least, supervisors will need to look laterally across peer groups of firms for oddities, and stress test firms' resilience against short-term and longer-fuse threats from the environment. They will, therefore, need to draw on market intelligence on industry trends from the Bank's Markets area; insights from the operators and overseers of the clearing, settlement and payment systems; and analysis from the finance and monetary researchers in the Bank. Conversely, the Financial Policy Committee will – and already has – drawn on briefings from the supervisors as well as the Bank's existing staff. In other words, this is going to be about making connections, pulling together a varied range of inputs. A measure of the Bank's success when prudential supervision transfers will be how well we knit them together".

We believe that "pulling together a varied range of inputs" is precisely what the FSA Panels have done over the years and that input from a standing body of senior practitioners linked also to the work of the FCA Panels, would contribute to this market intelligence and industry expertise.

ADVANTAGES TO A PRACTITIONER PANEL

We propose a single Practitioner Panel for the PRA – which would also incorporate the views of smaller firms who will be swept into regulation by the PRA. Such a Panel would have the following advantages:

1. Consideration of practical impact of policy changes

The Panel provides an overview from those who will have to implement any policy changes, and if it were also linked to the FCA Panels, would be able to give feedback in the light of FCA policy debates as well. The Panel would be able to review potential areas for misinterpretation of judgement-based regulation requirements on both sides. It would also be able to help the regulator to understand what is required to implement policy proposals successfully, whilst avoiding any unreasonably detrimental impact or unintended consequences on firms, and so assess costs versus benefits in accordance with regulatory principles. The Panel would also be able to look at how prudential requirements interact with conduct requirements from the firms' perspective and the impact on businesses and consumers more widely. We also feel that, adding smaller businesses representation into a PRA Panel would enable discussions about proportionality of application of rules and requirements across different sizes of firm.

2. Ability to review cumulative impact of PRA and FCA on firms

A vital area of concern in the new system is to see that there is effective coordination of regulatory requirements between the PRA and FCA. The PRA Panel should have a strong link to the FCA Panels to enable it to provide commentary and appropriate advice on the coordination of regulatory requirements between the two new regulators.

3. A forum with a remit to help the regulator to look ahead

With a regular forum, the members can look ahead to the impact of regulatory developments and initiate its own enquiries of the regulator if it sees a potentially adverse impact or prudential risk. There is no wish to 'capture' regulators through this system, but to provide forward looking advice on issues to look out for. Decisions on how to use these insights are unambiguously for the regulator alone.

4. Well informed and quality membership

If the Panel is statutory, it is given an authority and credibility which enables CEO level people to be persuaded to give up valuable time to become members. Such individuals are more likely to be able to see the wood for the trees than specialists with a narrower focus. Cross sectoral membership provides a focus on effective regulation rather than the sectoral interests of trade associations, which have a separate and important place in discussions with the regulator (and incidentally seemed to support the role of a standing body of practitioners in some of their comments). The members can sign confidentiality requirements, allowing early debate on the pros and cons of new policy developments. They also build up a knowledge of regulatory policy developments through membership over a period of 3-6 years which helps them to bring regulatory perspective to the debates. In addition, individual and high level advice can be given to the regulator on specific subjects through ad hoc sub groups with Panel chairmen and members outside the formal meeting process.

5. Transparency and public accountability

Although we recognise that the Government has said that the PRA's arrangements for consulting practitioners should be transparent, it will be simpler and more practical for a regular Panel to achieve these transparency requirements: the Panel can be required to produce an annual report (as the FSA Panels do currently) and possibly report to the Treasury Select Committee on the PRA (and FCA) engagement with firms. In addition, the PRA Panel could join the FCA Panel in continuing a similar project to the Practitioner Panel's biennial survey of regulated firms which has proved a useful tool for the FSA and provides feedback on perceptions of the regulator's performance against its objectives.

6. Contribution to EU and international negotiations

Such a Panel could additionally contribute to effective EU and international representation for PRA, by providing a means of facilitating proactive and early involvement of the industry in EU developments. Panel members could provide advice on ensuring that EU rules deliver the desired objectives in as efficient and effective way as possible, such as the precise way in which stress tests are conducted, the different options to increase prudential capital or the interactions between the market structure and payment mechanisms and individual firms. Directives and regulations, even on capital and liquidity matters, include a wide range of specific measures on which industry input is extremely useful to ensure they achieve their intended effect and avoid adverse unintended consequence.

CONCLUSION

We believe that it will be crucial for the PRA to have a statutory standing panel of independent practitioners who regularly engage with the PRA in policy formulation and implementation. The group should have strong links to the FCA Panels. An alternative but less welcome structure would be for the FCA Practitioner Panels to have a remit and responsibility to look at certain prudential issues from the PRA.

A new approach to financial regulation: the blueprint for reform (Cm8083)

A response paper by the Futures and Options Association

SEPTEMBER 2011

A NEW APPROACH TO FINANCIAL REGULATION: THE BLUEPRINT FOR REFORM (Cm8083)

1. Introduction

1.1 The FOA is the industry association for more than 160 firms and institutions which engage in derivatives business, particularly in relation to exchange-traded transactions, and whose membership includes banks, brokerage houses and other financial institutions, commodity trade houses, power and energy companies, exchanges and clearing houses, as well as a number of firms and organisations supplying services into the futures and options sector (see Appendix 1).

1.2 The FOA welcomes the recognition in the HM Treasury consultation paper "A new approach to financial regulation: the blueprint for reform" (hereinafter "Cm8083"):

(a) that *"financial services is one of the key sectors of the UK economy"* and *"as an employer and contributor of tax revenues, as an exporter of UK services to the rest of the world, and as a vital part of the economic infrastructure, a healthy financial sector is an important driver of growth in the UK"* (para 1.1);

(b) that the potential for significant risks posed by such a financial service sector and the severe impact of the recent financial crisis calls for the kind of *"targeted policy responses"* identified in para 1.5 and a fundamental strengthening of the system *"by promoting the role of judgement and expertise"* (para 1.13); and

(c) that, in order to develop an appropriate and workable programme of reform, the Government must *"work closely with all stakeholders"* (para 1.15).

1.3 With regard to the burden of regulation, the FOA would reiterate the Government's assertions in its previous consultation paper "A new approach to financial regulation: building a stronger system" (Cm8012), namely:

(a) that a key priority will be *"reducing the burden of regulation and improving the quality of regulation"* (paras 3.66-7);

(b) that policy-makers must *"think carefully about the case for regulation"*, and where intervention is required, to explore in full the opportunity for non-regulatory and self-regulatory approaches before considering regulatory measures (paras 3.66-7);

(c) that the new regulators must be *"rigorous in their analysis of the impact of regulation on industry"* (para 3.67);

(d) that it will be part of the FCA's role to remove regulatory barriers, where possible, to facilitate greater efficiency and choice and that this is *"clearly an issue of primary importance along the whole financial value chain and for all consumers of financial services"* (paras 4.15);

(e) that regard should be paid to the *"potentially negative effects of excessive regulation on market efficiency and consumer choice"* (para 4.9); and

(f) that the new infrastructure must be able to operate in a way that delivers coherence, efficiency, effectiveness and *"the best value-for-money solution for the financial services sector"* ("A new approach to financial regulation: judgement, focus and stability" (Cm7874)).

The FOA hopes and anticipates that these key expressions of regulatory policy and proportionality will be properly reflected "on the ground" by both the PRA and the FCA as they develop their regulatory policies and practices. Unfortunately, however, there seems to be little real recognition of the Government's intention that the new approach to regulation should avoid excessive regulation and constitute a "value-for-money" proposition in FSA's recent Discussion Paper "The Financial Conduct Authority: Approach to Regulation" (June 2011). There is, clearly, an inherent conflict between the policy objectives expressed above and the drive for closer, higher cost and more interventionist regulation. Hence, the FOA's emphasis on facilitating competitiveness, as set out in para 1.4 in this response.

1.4 The FOA strongly supports the six statutory regulatory principles set out in the draft Bill, but in order to deliver the financial service sector contributions and the regulatory objectives set out in paras 1.2 and 1.3 respectively in this response, the FOA would urge the Government to reconsider its position regarding the importance of competitiveness and include its facilitation as a factor required to be taken into account by the PRA/FCA (see further paras 3.4 and 4.13 in this response).

1.5 The FOA welcomes the Government's firm intention to ensure that there is full and effective co-ordination between the various bodies that have macro- or micro-supervisory responsibilities. This means:

(a) the development of "bright lines", where possible, in terms of scope, responsibilities and decision-making – all of which are critical to ensuring the delivery of regulatory efficiency and the avoidance of unnecessary regulatory duplication, particularly for dual-regulated firms;

(b) that the decision-making process and the individual objectives and responsibilities and how the common regulatory principles are applied by the different authorities are properly understood and taken into full consideration by each of them (recognising the failures in the pre-crisis Tripartite arrangement) – as required by s.9E(2) of the draft Bill to the FPC in relation to its objectives.

1.6 The FOA strongly supports the view that, irrespective of the category of customer, financial service providers should be required to act fairly and honestly, but believes that expectation of high behavioural standards should not result in wholesale business being subjected to inappropriate, high-cost retail-style protections.

The FOA welcomes, therefore, the observation in HM Treasury's Cm8012, that *"there are wholesale and market activities which do not directly form part of the transaction chain of products and services sold to retail customers. The scale and importance of these activities makes it imperative that they are effectively and proportionately* *regulated in a way which recognises the particular characteristics of participants in these markets"* (para 1.39).

This view is reflected by the FSA in its recent Discussion Paper (referenced in para 1.3 above), insofar as it recognises that there are important differences between wholesale and retail markets and that financially sophisticated consumers do not require the same degree of protection as retail consumers (paras 3.5 and 3.6 in the DP), but the FOA remains concerned that there may still be some retail scope-creep into the regulation of wholesale business.

1.7 Statutory immunity removes the inherent legal right of persons to be able to bring civil proceedings for damages in the event of negligence.

In view of the potentially very high reputation and commercial consequences for firms that could flow from a significantly more commercially interventionist regulatory authority (e.g. in relation to product intervention, the issuance of notices warning of disciplinary action, powers to intervene in the commercial strategy and operation of regulated firms and FCA's new role in competition, etc.), the FOA believes:

(a) that the current scope of application of statutory immunity applicable to FSA should be reviewed, to ensure that it continues to be fair and proportionate in the context of the FCA and these new powers;

(b) that the powers of the Complaints Commissioner should be strengthened in order to serve as a more effective discipline on the exercise of these new powers; and/or

(c) that there should be some form of independent oversight of the exercise of the FCA's decision-making processes in highly sensitive commercial areas to ensure there is no undue significant commercial detriment and that FCA decisions in this area are viewed not just through a "consumer prism" (see para 4.1 in this response), but also an economic prism.

1.8 The FOA strongly supports the intention to review the funding methodology that lies behind the compensation regime of the Financial Services Compensation Scheme (FSCS), bearing in mind that some firms bear a disproportionate level of contribution when measured against the risk of claim that they pose to the scheme.

1.9 The FOA has commented on the draft Bill in the sections below and also in Appendix 2.

2. Responses to White Paper Questions on the Financial Policy Committee (FPC)

Q1. Do you have any specific views on the proposals for the FPC as described above and in Chapters 3 and 4?

2.1 The FOA supports the Government view:

(a) that the FPC's primary objective is to identify, monitor and take action to remove or reduce systemic risk that could threaten the UK financial system;

(b) that this objective should take into full account the need to avoid any adverse impact on the ability of the financial sector *"to contribute to the UK economy in the medium or long term"* (para 2.8);

(c) that the factors to be taken into account by the FPC should include proportionality, openness and international law (as set out on Clause 3 of the draft Bill);

(d) that HM Treasury should be empowered to suggest other factors that might be considered by the FPC in the exercise of its functions (but questions whether the FPC's ability *"to reject any recommendations with which it does not agree"* (para 2.12) creates a conflict here and, if so, how that conflict will be resolved?);

(e) that in principle, *in extremis,* HM Treasury should have the power to bring into force new tools expediently but that this power enabling Parliament to be bypassed (as set out under 9L(2)) should be more tightly circumscribed than by "*reason of urgency*", to reflect that Parliamentary scrutiny should occur in all except the most necessary of situations.

(f) as observed in para 2.17, that the FPC should have appropriate *"discretion in the use of macro-prudential tools"* but would note that the exercise of individual state discretions in this area could be in conflict with the powers exercisable by the new European Authorities and could create problems for regional coherence on actions required to reduce regional systemic risk; and

(g) that the FPC will be required to take economic growth into account in pursuing financial stability, but would emphasise that actions taken in pursuance of sustaining financial stability should also take into account their social impact and consequences.

NB As a general observation, these factors do not appear to apply to the Bank of England when considering the recommendations of the FPC.

2.2 The FOA would reiterate its view, as noted in para 2.18 of Cm8083, that governance of the FPC is *"too heavily weighted"* towards the Bank and that this must be offset by having an adequate number of external members with appropriate expertise. The FOA welcomes the Government's intention to give this concern further consideration over the period of pre-legislative scrutiny and notes that the Bank's governance will be adjusted by the amendments proposed in para 2.31. In particular, we would highlight that we are not of the view that the CEO of the FCA should not be regarded as an external member.

The FOA would also propose that to avoid duplicative requests for information being made to firms, the FPC should be under an obligation, as is the European Systemic Risk Board, to first take into account information held by the FCA and PRA, prior to making the request. Such a requirement could be framed in a form consistent with Article 15, *Collection and exchange of information,* of the ESRB's founding Regulation (No 1092/2010) which sets out safeguards with regard to collecting information to avoid such duplication.

Q2. Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payment systems as described above and in Chapters 3 and 4?

2.3 With regard to the regulation of RCHs, the FOA supports the measures set out in para 2.35 and:

(a) anticipates that the checks and balances, accountabilities and factors that apply to the PRA in terms of its regulation and supervision of systemically-important institutions, will apply equally (adjusted for relevance) to the Bank of England; and

(b) welcomes the requirement for the Bank and for FCA to enter into an MOU as set out in s.25 of the draft Bill and assumes that the methodologies and processes for PRA co-ordination with the FCA as the licensing authority of exchanges will apply with equal measure to the Bank of England, taking into account that CCPs are now largely integrated within exchanges – generating for exchanges the cost and burden of dual recognition.

Q3. Do you have any comments on:

- *the proposed crisis management arrangements; and*
- *the proposals for minor and technical changes to the Special Resolution Regime as described above and in Chapters 3 and 4?*

2.4 With regard to the crisis management arrangements, we would reiterate our previous comments that, as the PRA will have responsibility for triggering a failing firm's entry into the BoE's special resolution regime and for investigating and reporting to Treasury where there has been a possible regulatory failure, we are concerned that these roles potentially represent a structural conflict in the PRA's operation: the PRA may be hesitant to trigger the special resolution regime or report on a possible failure as having to take either step may represent a supervisory failure on the PRA's part. Similarly, as the draft Bill also requires the FCA to investigate and report on possible regulatory failures, we would highlight that the same potential conflict exists for the FCA in that it could conceivably hesitate to investigate for fear of generating criticism.

3. Responses to White Paper Questions on the Prudential Regulation Authority (PRA)

Q4. Do you have any comments on the objectives and scope of the PRA, as described above and in Chapters 3 and 4?

3.1 With regard to the Treasury's power to set additional specific objectives in future, the FOA believes that this may be driven by experience in terms of the operation, policy and processes of the PRA and not just *"as a result of the future widening of the responsibilities of the PRA"* (para 2.47). The FOA believes this is an undesirable constraint on this proposed power of HM Treasury.

3.2 The FOA welcomes the additions made to the PRA objective as set out in para 2.48, which acknowledges the importance of recognising diversity in firms and regulated activities, but would emphasise that this recognition of the need for differentiation should be extended to products and not just restricted to firms and services.

3.3 The FOA supports:

(a) recognition in Cm8083 of the need for regulatory policy and processes to be appropriately tailored to different types of firms; and

(b) rejection of a *"zero-failure"* approach to regulation, which would have to be so restrictive in terms of risk, innovation and choice as to undermine the Government's recognition in para 1.1 that *"a healthy financial sector is an important driver of growth in the UK"*.

This rejection of a "zero failure" approach has been emphasised by Hector Sants, Chief Executive, FSA, in his speech to the British Bankers Association on 7th March 2011, in which he stated that:

"The FCA will not be a "no failure" institution. Removing all risk-taking from consumers would remove individual freedom of choice and considerable benefits to society."

3.4 With regard to competitiveness, the FOA agrees with the view expressed in para 2.51 that financial stability is the platform for sustainable growth and success, but not that this obviates the need for a specific statutory principal requiring the regulatory authorities to pay due regard to the need to facilitate competitiveness. Indeed, an unduly prescriptive approach to sustaining financial stability could reduce the competitiveness of the sector.

As the Government has rightly observed in the Introduction to Cm8083, the financial services sector is *"one of the key sectors of the UK economy"* and *"an exporter of UK services to the rest of the world"*. Both these objective are heavily dependent on the industry being allowed to be strongly competitive in what is a highly competitive economic sector. While it is recognised that the degree to which systemically important institutions can be competitive must be tempered by the fact that they are systemically important, the PRA should be required to pay proper regard to the need for firms regulated by it to be internationally competitive.

It is difficult to see how both the PRA and the FCA can perform the more commercially judgemental and interventionist role that is expected of them – and which will involve taking decisions on commercial matters, reviewing business models and products and judging growth strategies – without being required to take into full account the need for those same institutions to maintain not just their international, but also their domestic, competitiveness.

3.5 The FOA:

(a) agrees that the PRA's ability to designate firms that will fall within its scope should be subject to a number of procedural safeguards including (as stated in para 3.26 of Cm8012), obligations to consult with the FCA in making this determination, providing firms with an opportunity to make representations and subjecting a designation decision to a right of appeal by a designated firm; and

(b) believes that the *“designation criteria”* should be transparent and applied and implemented consistently.

The FOA would, however, highlight a key concern with regard to its understanding that members of the same group will not necessarily be prudentially supervised by the same regulator. We strongly support an approach whereby there is one prudential supervisor for a group so that where one group firm is PRA authorised, the PRA is the prudential regulator for all firms within that group. A single prudential regulator for all group firms will ensure consistent prudential oversight, minimise the regulatory burden for firms and is particularly desirable given that HM Treasury has confirmed the PRA and FCA will have separately drafted prudential rulebooks.

Q5. Do you have any comments on the detailed arrangements for the PRA described above and in Chapters 3 and 4?

3.6 The FOA welcomes the adoption of a *“judgement-led”* approach to regulation, but would reiterate the importance of recognising:

(a) that all such judgements should be *“rigorously evidence-based”*;

(b) that judgements should be made according to criteria that facilitate consistency of decisions in comparable sets of circumstances;

(c) that the establishment of transparent and predictive criteria would enable firms to better understand the consequences of their actions;

(d) the importance of effective information-sharing with the FCA, where judgement-led decisions of the PRA are or could be relevant, or applicable in similar sets of circumstances which fall within the scope of the FCA, which has affirmed its intention to continue to be a principles-based, as well as a rules-based authority.

3.7 The FOA welcomes the Government’s decision not to narrow the grounds of appeal to the Tribunal as regards its scope in reviewing supervisory decisions. With regard to the Government’s decision not to allow the Tribunal to substitute its opinion for that of the regulator in the event of an appeal, the FOA believes that this should be subject to a requirement that the PRA give full and reasonable consideration to any directions issued by the Tribunal and the provision of a statement of reasons where it does not accept those directions, in order to ensure that the Tribunal is not perceived as a “toothless tiger”.

NB. These observations on the role of the Tribunal apply equally to the FCA (See para 4.14 in this response).

3.8 The FOA welcomes the Government’s assurance that *“the PRA board must provide a robust challenge to the executive”* and that means that the same standards of challenge that are expected of non-executives sitting on commercial boards should apply with equal rigour to their role on regulatory boards.

NB. This Board obligation applies equally to the FCA (see para 4.18 in this response).

3.9 The FOA supports the proposal that the National Audit Office should undertake value-for-money studies of the PRA and other authorities, including the FCA (see para 4.20 in this response). However, this audit function should cover the setting of fees by the CPMA and the PRA to avoid unnecessary regulatory duplication or a disproportionate impact on the economic delivery of financial products and services, particularly applicable in the case of dual-regulated firms. This would also help to ensure that sufficient regard is paid by the PRA and the FCA to the cost-effectiveness and "value-for-money" priority for regulation, which was identified by HM Treasury in Cm7874 and Cm8012 (see para 1.3 in this response).

3.10 With regard to the proposals for a PRA complaints scheme, the FOA would reiterate its observations that the proximity between the role of the Bank of England and the PRA could raise perceptions about a lack of independence in dealing with complaints – even in the area of operational matters. The FOA welcomes the Government's assurance that the complaints scheme run by the Bank of England will be *"suitably transparent and robust"*, but it must also demonstrate a satisfactory degree of independence. For this reason, the FOA would argue that complaints about the PRA should fall within the jurisdiction of the Complaints Commissioner, as is currently the case with the FSA and will be the case as regards the FCA – particularly since no clear reason is given in Cm8083 as to why complaints against the PRA should be handled any differently.

3.11 The FOA continues to feel strongly that the PRA should work with a Practitioner Panel that is comparable to the existing Panel set up under the FSMA, albeit comprising panellists with expert knowledge and experience relevant to the scope and objectives of the PRA, e.g. particularly in the area of prudential regulation of systemically-important institutions.

The FOA would emphasise that the current establishment of the existing Practitioner Panel by the FSMA 2000 was to compensate the regulated community for the fact that, while they were paying for regulation, they would no longer have the same policy input as they did in the time of self-regulation and therefore it should be represented by a high level statutory panel. That same argument is equally applicable in the case of the establishment of the PRA. In other words, in the view of the FOA, it is not acceptable that the PRA should have sole discretion, as described in para 2.77, as to *"what kind of arrangements it wants to establish for engaging with industry"*. The assurances and objectives (and, indeed, the rights of the industry which continues to pay for regulation) underpin the purpose of establishment of a statutory Practitioner Panel and apply with equal force to the PRA as they did to the FSA and as they will do to the FCA.

While the FOA supported the Government's position not to establish a PRA Consumer Panel, largely because of the obligation on the PRA to consult with the FCA where any of its decisions will have a material impact on consumers, the FOA would continue to urge the Government to give fresh consideration to the importance of establishing a Practitioner Panel in relation to the role of the PRA and use more forceful language in s. 2J(2) than the PRA "may include" the establishment of such a panel.

3.12 The FOA believes that the power of review by an independent person should include the additional factors set out in relation to the FCA at the end of para 4.1.8 in this response.

4. Responses to White Paper Questions on the Financial Conduct Authority (FCA)

Q6. Do you have any views on the FCA's objectives – including its competition remit – as set out above and in Chapters 3 and 4?

4.1 The FOA welcomes the Government's renaming of what is now the Financial Conduct Authority and the importance of clarifying what was meant by *"a strong consumer champion"*. However, since the FSA has repeatedly emphasised that it will be assessing its role through a *"consumer prism"* and the FSA's DP appears to address *"judgemental offsets"* in the context only of consumers, there is a risk that a proper balance might not be preserved as between the interests of consumers and regulated service providers. For this reason, the FOA would urge HM Treasury to ensure that there is a continuing and objective balance in the role and processes of the FCA with regard to both regulated firms and customers. This is not to state that the FOA quarrels with the fact that investor protection and consumer interest should be a priority, but rather that it should not become the sole perspective of the FCA to the point where it may, even inadvertently, result in the unfair treatment of regulated firms.

4.2 The FOA welcomes the proposal that the FCA will have a strong new role in promoting competition, efficiency and choice and notes the Government's recognition of *"the importance of competition as the best driver of good consumer outcomes"* and its intention to *"increase the profile of competition issues in a regulatory system"* (paras 1.8 and 1.41).

In particular, the FOA notes the Government's intention:

(a) to empower the Office of Fair Trading to consider to what extent competitive inefficiencies in specific markets are generated by structural barriers or other anti-competitive elements (paras 1.8 and 1.41);

(b) to give the FCA a wide-ranging competition mandate *"which will place competition concerns at the heart of the new conduct regime"*;

(c) to empower the FCA to initiate *"an enhanced referral to the OFT where it has identified a possible competition issue"*, including issues that may be generated by structural market features or anti-competitive business practices (identified in relation to Q10).

4.3 Increasing consolidation in the financial services sector means that fewer participants are providing key products and services. In this environment, it is vital for regulators to ensure that market dominance (wherever the source) is not anti-competitive and does not result in abuse of consumers. The FOA is supportive of the FCA being given a specific obligation to discharge its general functions in a way that promotes competition, including focussing on market power and prices. Empowering the FCA to independently monitor the behaviours of market players relevant to market competitiveness and (as set out in s.1E of the draft Bill) efficiency and choice in market services will be a critically important discipline on entities with considerable market power, and will play a key role in delivering on FCA objectives of market integrity and efficiency. However, we strongly support statements from both HM Treasury and the FSA that the FCA should not be a pricing regulator.

4.4 In this context, the FOA notes that the FCA will be assuming a more commercially interventionist and economic and competition-related role, in terms of monitoring remuneration and intervening in the development, distribution and pricing of products.

In addressing the BBA Annual Conference on 29th June 2011, Hector Sants, Chief Executive, FSA, noted that, while the Government is not expecting the FCA to become an economic regulator, it *"is expecting it to utilise its powers to make judgements on pricing issues where they relate to fairness. Delivering on this mandate will require a step-change relevant to the FSA and the FCA's technical skills and philosophy."*

Further, the FSA, in its June 2011 publication "Approach to Regulation", stated that the FCA will be focussing more directly on the workings of the markets *"including market power"* and that the regulatory options which will be available to it will include *"measures which reduce market power"* and *"price intervention"* (paras 3.14-5)

4.5 The FOA welcomes the Government's assurance that it will keep this requirement under consideration as part of *"this phase of pre-legislative scrutiny"*.

4.6 In the matter of the FCA being required to facilitate competitiveness as a factor to be taken into account in fulfilling its objectives, the FOA would repeat all the observations made by it in urging that a similar factor should be applied to the PRA in terms of fulfilling its objectives (see para 3.4).

While the prudential regulation of international systemically important institutions by the PRA should be required to consider the need to sustain international competitiveness, this is also a key factor that should be taken into account by the FCA, firstly, because it is setting the business conduct rules of those same international institutions; and, secondly, it will be responsible for the business conduct and prudential regulation of small firms, the competitiveness of which, in a domestic context, will be equally important insofar as they are often associated with the "green shoots of recovery".

Q7. Do you have any views on the proactive regulatory approach of the FCA, detailed above and in Chapters 3 and 4?

4.7 The FOA supports the need for a more proactive approach to conduct regulation with a *"clear focus on consumer outcomes"*, but subject to standards of proportionality which would reflect:

(a) the category of consumer, e.g. retail or wholesale; and

(b) the need for firms to be competitive and pro-active in terms of service and product innovation in what is a highly competitive environment.

4.8 The FOA supports the proposed new powers of intervention to be given to the FCA in relation to products.

However, in view of the potentially significant impact that their exercise could have on firms, consumers and markets, they should:

(a) only be exercised where there is a real and demonstrable risk of *"significant consumer detriment"* and this is demonstrated by the examples given in the DP of retail consumer detriment in Chapter 5, insofar as they represent large-scale losses, indicating that the scale of anticipated detriment will be key to justifying use of the FCA's product intervention powers;

(b) *"strike the right balance between consumer protection… and the risks of restricting consumer choice and product innovation"* (para 1.24 of FSA's Discussion Paper "Product Intervention" (DP11/1));

(c) be subject to safeguards to ensure due consideration is given to conflicting public policy interests, i.e. that *"an appropriate balance is struck between the interests of consumers and regulated firms"* (para 4.76 in DP11/1);

(d) be exercisable only in accordance with clear and transparent policy criteria to enable firms to have a reasonable degree of certainty over the regulatory position as regards the development of new products; and

(e) not become, as it is put in Cm8083, *"a substitute for regulation of the sales process"* (para 2.99), i.e. when a product is sold it is a business conduct, not product quality, issue, yet FSA continues to state that one justification for banning a product could be the level of perceived risk of mis-selling.

The FOA notes and supports the Government's observation in Cm8012 that such interventionist powers are *"unlikely to be appropriate in relation to professional wholesale consumers"*. However, the FOA also notes the observations by the FSA in in its "Approach to Regulation" that product intervention must still be considered *"to the extent that wholesale products filter down or are distributed to retail consumers"* (para 5.26). The FOA understands this qualification, but would urge that it does not undermine the Government's view that this should not normally be applicable to professional wholesale customers.

The FOA also notes that the draft Bill enables the FCA to immediately ban a product without consultation for up to 12 months where "*necessary or expedient*" which it considers too wide a test and that the normal process of consultation should be bypassed in emergency situations only. The FOA also believes that a process should be established to enable firms to appeal against a ban and would suggest the Bill to be amended accordingly.

4.9 With regard to early publication of disciplinary action, while the FOA welcomes the Government's recognition of the need for safeguards, it would nevertheless urge the Government to reconsider its position on this issue. At the very least, the proposed safeguards should:

(a) not just allow a firm that is to be the subject of any such notice to comment on its wording prior to publication, but require the FCA to take any such comments into full consideration;

(b) require the FCA to set out in any notice, however briefly, the firms' defence to the allegation in question, recognising that there has been no finding of guilt, and that there is an overriding obligation for fairness in public disclosures of this nature.

NB. It should be remembered that the issuance of such notices, no matter how much reputational damage may be caused and no matter how inadequate the evidence founding the allegation in question, will be protected by statutory immunity (see para 1.7 in this response) and that this should place a very high duty of care on the FCA in terms of taking actions that could generate serious commercial loss and loss of reputation to firms.

While the FOA supports the obligation on the FCA to publish, as appropriate, a Notice of Discontinuance, this will do little to correct any damage that may have been caused to the reputation, jobs and share price of the firm in question. The FOA believes strongly that there should be some form of independent scrutiny to ensure that conflicts of interest between the public and private interest are properly addressed, including analysis of the evidence supporting the decision – as well as the decision itself – to issue a notice.

Q8. What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?

4.10 The FOA agrees that the FCA's powers of early intervention will, as is stated in Box 2.H, *"reduce the occurrence of the types of mass detriment seen over the past decade"*. However, it is important that the proposal to allow nominated parties to raise issues with the FCA of potential mass detriment are subject to a number of checks and balances, e.g. that the power is confined to credible and properly accountable groups:

(a) bearing in mind the potential for unjustifiable reputational risk to any named firm;

(b) to prevent the FCA being locked into a series of potentially costly, protracted and controversial procedures and processes without good cause;

(c) to reduce the risk of reporting abuse, the submission of vexatious reports and unwarranted attacks on the reputation of firms.

Q9. What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and, in the case of referrals from nominated parties, to do so within a set period of time?

4.11 The FOA has no particular concern over the procedural requirements following a report of possible mass detriment, providing, where a firm or group of firms is involved, they are given a full right of response before any public steps are taken, and that the FCA is under an obligation to take that response into full consideration in deciding what action, particularly if it is of a public nature, is to be taken. In terms of establishing time limits, it is essential that compliance with a timetable does not take precedence over the need for a full and proper investigation into the merits of a report.

Q10. Do you have any comments on the competition proposals of for the FCA set out above and in Chapters 3 and 4?

4.12 The FOA refers to its response to Q6 and, in particular, paras 4.2-4.4 in this response.

4.13 The FOA repeats its opposition to the Government's view that the FCA should not be subject to a "competitiveness" factor (see para 4.6 in this response) for reasons set out in relation to the PRA (see para 3.4 in this response).

4.14 The FOA repeats its observations about the role of the Tribunal in para 3.7 in this response, insofar as they should apply not just to the PRA, but also to the FCA.

Q.11 Do you have any views on the proposals for markets regulation by the FCA, described above and in Chapters 3 and 4?

4.15 The FOA welcomes the fact that the approach to the supervision of markets by the FCA will largely be a continuance of the same approach currently adopted by the FCA, and that its primary focus will be on the integrity and efficiency of markets and providing a level playing field for market participants.

4.16 The FOA notes that the primary focus will be on market infrastructures, but would emphasise the importance of the provision of technology services, not just to the markets, but also to financial intermediaries and their customers in terms of assuring market integrity, market connectivity and risk mitigation.

Q12. Do you have any comments on the governance accountability and transparency arrangements proposed for the FCA, as described above and in Chapters 3 and 4?

4.17 The FOA welcomes the proposals put forward by the Government, including particularly the proposed six principles of good regulation to which the FCA must have regard, i.e. efficient use of resources, regulatory proportionality, consumer responsibility, senior management responsibility, openness and transparency.

The FOA also supports the mechanisms for FCA accountability to Government and Parliament, the role of the FCA Board in terms of providing a robust challenge to the Executive (see also para 3.8 in this response) and the requirement on the FCA Board (and the PRA Board) to observe good corporate governance standards as set out in s.3C of the draft Bill.

The provision for review by *"an independent person"* into the economy, efficiency and effectiveness with which the FCA has used its resources to fulfil its obligations under s.1N of the draft Bill should be extended to include (a) the extent to which it has utilised cost-benefit, market and other analyses to justify its decisions; and (b) the extent to which the principles for good regulation have been observed in discharging its responsibilities.

4.18 The FCA has provided the assurance that its judgements will be *"reasonable and proportionate"* (para 4.18 in FSA's "Approach to Regulation"), but the FOA supports the fact that its regulatory decisions will nevertheless be subject to an effective appeals mechanism, e.g. the scrutiny of an Independent Tribunal.

4.19 The FOA would repeat its observations about the scope and role of the National Audit Office as playing a key part in ensuring regulatory efficiency, not just for the PRA, but also the FCA (see para 3.9 in this response).

4.20 The FOA welcomes the provisions in s.17 of the draft Bill covering the investigation of complaints against the FCA, but believes that s.17(6) of the draft Bill should require the FCA to give a statement of reasons where it decides not to follow a recommendation.

Q13. Do you have any comments on the general co-ordination arrangements for the PRA and FCA described above and in Chapters 3 and 4?

4.21 The FOA would reiterate observations made earlier in this response regarding the need for effective co-ordination and welcomes the fact that the Bank and FCA will be publishing a document later this year setting out more fully their plans to deliver *"operational co-ordination"* and that a key purpose of the general duty to co-ordinate is to *"minimise unnecessary overlap, duplication and regulatory burden"*.

The FOA would emphasise that operational co-ordination and the avoidance of unnecessary overlap is as much in the interest of the regulatory authorities themselves and the customers of regulated firms as it is of the regulated firms and that, in a climate of escalating regulatory cost (which will be borne essentially by consumers of financial services), this should be a particularly important objective.

4.22 The FOA agrees that there should be a *"high threshold"* for the use of the PRA veto and that there should be clear and transparent criteria surrounding its use.

5. Responses to White Paper Questions on other issues

Q14. Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described above and in Chapters 3 and 4?

5.1 The FOA generally supports the regulatory processes set out in this section of Cm8083, but

(a) with regard to para 2.183, if PRA/FCA powers to retain original documents result in them being retained by the regulatory authority for excessive periods of time, the authorities should be required to provide a statement of reasons to the owner of the documents – and this would act as an essential discipline to ensure that the authorities' own procedures are appropriately expedited and that the documents are retained for no longer than is necessary;

(b) with regard to the issue of enforcement, there is a clear tension between the FSA's understandable drive to develop credible deterrence sanctioning, the principle that the punishment should fit the crime, i.e. sanctioning proportionality, and the right of individuals to be able to reasonably predict the consequences of their actions. This means that there should be transparent governing criteria around the sanctioning policy and process of the FSA to ensure that these issues are properly addressed in a balanced way and that any significant increase in sanctions should be made only on reasonable and public notice of an increase.

5.2 The FOA believes that the reduction in the minimum period for representations to be made from 28 days to 14 days would be acceptable in very straightforward cases, but:

(a) the Government should also pay attention to the regulator's own protracted processes, which have contributed significantly to slowing down *"the enforcement process unnecessarily"*, i.e. there needs to be even-handedness in this area;

(b) while the relevant authority will be able to exercise discretion in specifying a longer period on an individual basis, respondents should be able to apply for longer periods of time and the relevant regulatory authority should be required to give full and fair consideration to any such application, bearing in mind that it is the respondent who will be best-placed to determine how much time may be necessary in order for it to make individual representations.

5.3 The safeguard set out in para 2.188 of Cm8083 regarding the publication of information should be extended beyond the avoidance of undermining *"consumer interests or financial stability"* to include the legitimate interests of a regulated firm.

The FOA remains concerned that the proposed processes for approved persons' applications are unclear and require further development. In particular, the Blueprint refers to "*the Government remains of the view that one authority should have a deciding say in the application process*" (pg 43); however, the draft legislation indicates that applications for approval should go to the two Regulators separately. The FOA would seek further clarity regarding this matter.

We also note the new section 166A ('S166A) (inserted by schedule 11 to the draft Bill) which will enable the PRA and the FPC to require a firm to appoint a skilled person to "*collect and keep up to date*" information where an authorised person has contravened a rule which requires it to collect and update information. Although the FOA surmises that s166A has most obvious application to recovery and resolution plans, it is concerned that as it is drafted widely, the power could provide for a skilled person to be appointed to collect and maintain data on an <u>ongoing</u> basis. Consequently, the FOA seeks additional clarification and safeguards regarding the purpose and use of this proposed power.

5.4 With regard to information gateways and information-sharing, it is important that the UK regulatory authorities seek a full statement of reasons, prior to disclosure, as to the basis on which information is being sought:

(a) to avoid "fishing expeditions";

(b) to know by what authority the requesting organisation is demanding disclosure;

(c) to ensure that the requesting authority is seeking information for itself and not as agent for an associated organisation which does not have the authority to obtain the information in question;

(d) to ensure that the disclosure of the information in question will not put companies or individuals at unacceptable levels of risk in jurisdictions with questionable human rights and/or legal safeguards.

Q15. Do you have any comments on the proposals for the FSCS and FOS set out above and in Chapters 3 and 4?

5.5 The FOA has no comments, other than its support for the concern of some of its members over the extent of their liability to contribute to the FSCS, which should be, but is not, linked to the claims risk of each contributor. The FOA welcomes, therefore, the intended review of the FSCS.

APPENDIX 1

LIST OF FOA MEMBERS

FINANCIAL INSTITUTIONS
ABN AMRO Clearing Bank N.V.
ADM Investor Services International Ltd
Altura Markets S.A./S.V
Ambrian Commodities Ltd
AMT Futures Limited
Bache Commodities Limited
Banco Santander
Bank of America Merrill Lynch
Banca IMI S.p.A.
Barclays Capital
Berkeley Futures Ltd
BGC International
BHF Aktiengesellschaft
BNP Paribas Commodity Futures Limited
BNY Mellon Clearing International Limited
Capital Spreads
Citadel Derivatives Group (Europe) Limited
Citigroup
City Index Limited
CMC Group Plc
Commerzbank AG
Crédit Agricole CIB
Credit Suisse Securities (Europe) Limited
Deutsche Bank AG
ETX Capital
Fortis Bank Global Clearing NV - London
GFI Securities Limited
GFT Global Markets UK Ltd
Goldman Sachs International
HSBC Bank Plc
ICAP Securities Limited
IG Group Holdings Plc
Investec Bank (UK) Limited
JP Morgan Securities Ltd
Liquid Capital Markets Ltd
Macquarie Bank Limited
Mako Global Derivatives Limited
MF Global
Marex Financial Limited
Mitsubishi UFJ Securities International Plc
Mizuho Securities USA, Inc London
Monument Securities Limited
Morgan Stanley & Co International Limited
Newedge Group (UK Branch)
Nomura International Plc
ODL Securities Limited
Rabobank International
RBS Greenwich Futures
Royal Bank of Canada
Saxo Bank A/S
S E B Futures
Schneider Trading Associates Limited
S G London
Standard Bank Plc
Standard Chartered Bank (SCB)
Starmark Trading Limited
State Street GMBH London Branch
The Bank of Nova Scotia
The Kyte Group Limited
Tullett Prebon (Securities) Ltd
UBS Limited
Vantage Capital Markets LLP
Wells Fargo Securities International Limited
WorldSpreads Limited

EXCHANGE/CLEARING HOUSES
APX Group
Bahrain Financial Exchange
CME Group, Inc.
Dalian Commodity Exchange
European Energy Exchange AG
Global Board of Trade Ltd
ICE Futures Europe
LCH.Clearnet Group
MEFF RV
Nord Pool Spot AS
NYSE Liffe
Powernext SA
RTS Stock Exchange
Shanghai Futures Exchange
Singapore Exchange Limited
Singapore Mercantile Exchange
The London Metal Exchange
The South African Futures Exchange
Turquoise Global Holdings Limited

SPECIALIST COMMODITY HOUSES
Amalgamated Metal Trading Ltd
Cargill Plc
ED & F Man Commodity Advisers Limited
Engelhard International Limited
Glencore Commodities Ltd
Koch Metals Trading Ltd
Metdist Trading Limited
Mitsui Bussan Commodities Limited
Natixis Commodity Markets Limited
Noble Clean Fuels Limited
Phibro GMBH
RBS Sempra Metals
Sucden Financial Limited
Toyota Tsusho Metals Ltd
Triland Metals Ltd
Vitol SA

ENERGY COMPANIES
ALPIQ Holding AG
BP Oil International Limited
Centrica Energy Limited
ChevronTexaco
ConocoPhillips Limited
E.ON EnergyTrading SE
EDF Energy
EDF Trading Ltd
International Power plc
National Grid Electricity Transmission Plc
RWE Trading GMBH
Scottish Power Energy Trading Ltd
Shell International Trading & Shipping Co Ltd
SmartestEnergy Limited

PROFESSIONAL SERVICE COMPANIES
Actimize UK Ltd
Ashurst LLP
ATEO Ltd
Baker & McKenzie
Barlow Lyde & Gilbert
Berwin Leighton Paisner LLP
BDO Stoy Hayward
Clifford Chance
Clyde & Co
CMS Cameron McKenna
Complinet
Deloitte
Dewey & LeBoeuf LLP
FfastFill
Fidessa Plc
FOW Ltd
Freshfields Bruckhaus Deringer
Herbert Smith LLP
Hunton & Williams LLP
International Capital Market Association
ION Trading Group
JLT Risk Solutions Ltd
Katten Muchin Rosenman Cornish LLP
KPMG
Mpac Consultancy LLP
Norton Rose LLP
Options Industry Council
PA Consulting Group
Progress Software
R3D Systems Ltd
Reed Smith LLP
Rostron Parry Ltd
RTS Realtime Systems Ltd
Sidley Austin LLP
Simmons & Simmons
SJ Berwin & Company
SmartStream Techologies Ltd
SNR Denton UK LLP
Speechly Bircham LLP
Stellar Trading Systems
SunGard Futures Systems
Swiss Futures and Options Association
Traiana Inc
Travers Smith LLP
Trayport Limited

APPENDIX 2

COMMENTS ON THE DRAFT BILL

Comments on the Draft Bill

NB. The FOA anticipates that law firms and other legal experts will be commenting in detail on the draft legislation and the comments that follow are largely driven by general rather than legal / constitutional concerns over the drafting.

1. In view of the fact that the Financial Policy Committee will be advising the Bank of England on the Bank's Financial Stability Objective, the FOA questions the degree to which the Bank will itself be influenced by the various factors which the FCA is required to take into account, e.g. avoiding a significant adverse effect on the capacity of the financial sector to contribute to the growth of the UK economy (clause 9C(4)) or prejudicing the objectives of the FCA or the PRA (clause 9E(2)). If the Bank is not itself subject to similar constraints, it will be free to reject any FPC recommendations that take them into account. This seems to break the chain of accountability and the obligation to take into account proportionality and other statutory principles of good regulation.

2. The FOA notes the restriction on the scope of recommendations that may be made to the Bank by the FPC, namely, that they may not be made *"in relation to a particular financial institution"* (clause 9M(3)(a)).

   The FOA believes that this constraint will impair the ability of the FPC to fulfil its role in terms of identifying, monitoring and tacking action to remove or reduce systemic risks, or to protect the resilience of the UK financial system, including addressing systemic risks *"attributable to structural features of financial markets, or to the distribution of risk within the financial sector"* (clauses 9C(2) and (3)), in which certain CCPs have a critical part to play in the whole financial system.

3. Clause 1B(8) outlines the general functions of the FSA, which do not, but in the view of the FOA, should expressly cover the key regulatory functions of supervision and enforcement, i.e.:

   (i) it cannot be implied that they are covered because they are carried out pursuant to made rules under clause 1B(8)(a);

   (ii) the functions described largely in this sub-paragraph are more *"legislative functions"* than *"general functions"* (cf. para 1(2) of Schedule 1ZA on page 200 of the draft Bill); and

   (iii) supervision and enforcement are functions carried out pursuant to the arrangements described in para 9 of Schedule of 1ZA on page 202 of the draft Bill, but they are not the arrangements themselves.

4. Clauses 1I and 1K provide for the establishment of a Practitioner Panel and a Markets Practitioner Panel, but the FOA would emphasise that the preponderance of individuals appointed to each panel should be drawn from the specific interests represented by each panel, i.e. the majority of members of the Practitioner Panel should be drawn from authorised persons and those of the Markets Practitioner Panel should be drawn from market infrastructures.

It is noted that CCPs are not, but clearly should be, included in the list of eligible persons under clause 1K(5)) – and not left to the discretion of the FCA under clause 1K(6). It should make no difference that clearing houses will now be regulated by the Bank of England, insofar as there is a strong integration between the functions of clearing and execution.

5. Clause 1N provides that the Treasury may appoint an independent person to *"conduct a review of the economy, efficiency and effectiveness with which the FCA has used its resources in discharging its functions"*, but specifically excludes *"the merits of the FCA's general policy or principles in pursuing its strategic objective and its operational objectives"*. While it is not clear exactly what is covered by the words *"the merits of…"*, any review of the *"economy, efficiency and effectiveness"* of FCA's discharge of its functions cannot be comprehensively addressed, unless it includes how it has implemented the principles of good regulation in relation to the discharge of those functions.

   The FOA would urge HM Treasury therefore to consider revising (3) to read *"the review is not to be concerned with the merits of the FCA's general policy or principles in pursuing its strategic objective and its operational objectives, other than where and how they have taken into account in the discharge of any functions that are the subject of the review"*.

6. With regard to clause 2B, the FOA notes:

   - that the definition of *"PRA-regulated activities"* may be the subject of an Order made under s.22A of FSMA 2000 (see s.6 on page 91), but would emphasise the importance of Parliament being able to set the scope of the PRA and assumes, therefore, that any such Order will be the subject of affirmative Parliamentary oversight and believes that such Orders may be necessary to bring clarity to the scope of the PRA; and

   - that there is no equivalent definition of *"FSA-regulated activities"* and, while it is presumed that this is because it will cover all regulated activities, other than those to be covered by the PRA, believes that this should be stated expressly in the legislation.

7. Clause 2J(2) states that the PRA's arrangements for consulting PRA-authorised persons *"may"* include the use of such panels as the PRA thinks fit, but does not believe it is appropriate or desirable that the PRA should have absolute discretion in this matter. The FOA would emphasise the importance of establishing a Practitioner Panel on the same terms as the draft Bill requires the establishment of a Practitioner Panel to interface with the FCA for reasons set out in para 3.11 in this response). It continues to be unclear as to why a differentiated approach in this matter should be adopted as between the PRA and the FCA. The FOA believes that reasons for this kind of differentiation should be given, bearing in mind the circumstances surrounding the establishment of the existing Practitioner Panel, as mentioned in para 3.11 in this response.

8. With regard to clause 2L(3), the FOA would repeat its observations in para 5 above in relation to the FCA, and believes that it is entirely appropriate for the PRA's general policy or principles to be taken into account when determining whether or not it has discharged its functions with *"economy, efficiency and effectiveness"*.

9. The FOA believes strongly that clause 3B should include, as a regulatory principle, recognition of the need for firms to be competitive for reasons set out in paras 1.2 to 1.4, 3.4 and 4.13 in this response.

10. Clause 138J provides for PRA consultation in relation to the *"making"* of any rules by the FCA. Depending on how the word *"making*" is defined, it may not necessarily cover the disapplication or withdrawal of any rules, and while it can be assumed that most amendments would be achieved through newly *"made"* rules, it is possible that may not always be the case. For this reason, the FOA believes that the term should be extended to include *"making, amending or withdrawing"* any rules of the FCA.

11. It is noteworthy that the definition of *"market in the United Kingdom"* in clause 140A defines such issues as what is meant by its location and what is meant by references to a *"feature of the market in the United Kingdom for goods or services"* (which is construed as any structural or conduct issue). It does not actually define what is meant by a *"market"* which, in general terms, is an organised and regulated centre or network for the trading, in this context, of regulated financial instruments.

12. The FOA notes and welcomes the checks and balances outlined in clauses 312E to 312K on the power of the FCA to set and issue financial penalties on recognised bodies, but is concerned that no such checks and balances seems to apply in relation to regulated firms. For example, the obligation to publish a statement of sanctioning policy in draft form in order to allow representations to be made as regards any such proposed statement of policy is particularly welcome, but should surely be relevant to the sanctioning policy of regulated firms.

13. The FOA notes in clause 42 the listing of those "cases" under which the Bank of England must notify the Treasury of a possible need for public funds to cover financial institutions but makes no reference to CCPs, which are clearly going to become organisations of systemic importance and which, in the event of a significant default, may well require public funding to a comparable or even greater degree.

14. With regard to clause 17(6), the FOA would urge that, if the FCA decides not to adopt any recommendations of an investigator looking into a complaint against the FCA, it should be required, in addition to the matters set out in sub-para (6), to provide the investigator and the complainant with a statement of reasons as to why it has come to that decision.

15. Should the reference to *"the FCA's functions"* in clause 25(1), read *"the FCA's general functions"* or all its functions beyond those general functions, in which case have those other *"functions"* been clearly defined in order to determine the scope of statutory immunity?

16. In clauses 23 to 25, the FOA believes the observations made on the importance of maintaining the existing complaints scheme to cover complaints against the FCA, are

equally applicable to complaints against the PRA. Each scheme should reflect exactly the same level of independence, in terms of both appointment of investigators, functions and processes, as will apply to complaints against the FCA (and no reason for differentiated treatment appears to have been given).

The FOA also repeats the point made in para 14 above about the PRA providing a statement of reasons if it decides not to follow any of the recommendations of the investigator (in parallel with similar observations made as regards the situation pertaining to the FCA in the same circumstances).

17. With regard to clauses 29 to 35, the FOA repeats the points made in relation to the FCA as regards its approach and policy towards the issuance of penalties.

18. With regard to clause 166A, bearing in mind the potentially significant costs that may have to be borne by an authorised person, particularly in the case of a protracted investigation or in the context of small and medium sized enterprises, the FOA believes it is appropriate to have a reasonableness test that will have to be observed by the FCA in requiring a firm to appoint an external skilled person to gather information.

8 September 2011

Financial Regulation Strategy
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By email to:
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Dear Sirs

GC100 response to HM Treasury's Consultation and White Paper: "A new approach to financial regulation: the blueprint for reform"

I am writing on behalf of the GC100 in response to HM Treasury's Consultation and White Paper, "A new approach to financial regulation: the blueprint to reform" (Cm 8083: June 2011). As you may be aware, the GC100 is the association for general counsel and company secretaries of companies in the FTSE100. There are currently more than 120 members of the group, representing some 90 issuers.

In April 2011, the GC100 submitted its response to HM Treasury's Consultation: A new approach to financial regulation: building a stronger system (referred to respectively as the "April Response" and the "February Consultation") and welcomes the opportunity to respond to this consultation. We have limited our response to question 11 and our observations to matters relating to Listing and the UKLA.

We are pleased to note that the UKLA is to remain part of the FCA. However, as noted in our April Response, we are both surprised and concerned to discover potentially far reaching and onerous changes being proposed in relation to the statutory framework surrounding primary and secondary market activity in Part VI of FSMA described (in the February Consultation) in the language of 'minor technical improvements'. As a general observation we do not consider there to have been market or regulatory failure in the listed markets and we fear that changes justified as technical changes could have a significant and adverse impact and such changes are not justified on regulatory grounds or as a result of any actual market failure. Indeed we believe that all the empirical evidence is that the listing regime stood up well during times of extreme stress during the financial crisis and therefore we do not see that there is a need to change, for change's sake, the supervision or regulatory framework of the existing listing regime. We also believe that to increase the regulatory burden without any fact based evidence of market failings is likely to lead to unnecessary and increased company costs at a time when there is a severe economic downturn, and is incompatible with the Government's stated aim of regulatory simplification and the cutting of needless "red tape", as well as making London a less competitive location for international listings.

In particular, in the February Consultation, certain changes were justified on the grounds of alignment with other aspects of FSMA or FSA/FCA responsibilities. We are very concerned by this approach as we believe that the role of the UKLA as competent authority for listing and prospectuses is, by its very nature, fundamentally different from the prudential, supervisory, conduct and consumer aspects of the FSA/FCA. This is explored more fully below in relation to statutory objectives and also limitation periods.

Listing and the UKLA

We believe that the Government's central policy objectives as outlined in the February Consultation, namely, to enhance the UK's financial stability and to avoid regulatory failure contributing to another financial crisis, are sound.

However the draft Financial Services Bill deals not only with the regulatory structure for banks and other financial institutions, but also with the structure of primary and secondary market regulation for equity and debt in the UK. This is quite a different issue, as the structure of UK markets affects the attractiveness of those markets for investors and therefore the capability of all companies (not just financial institutions) to raise finance competitively and efficiently, as well as being relevant to the competitiveness of the UK as a centre for investment and a market for capital raising by international companies. Strong and effective UK market regulation is a key ingredient for the continued strength and efficiency of the UK capital markets as a source of capital for business.

Bringing the listing regime and other primary market regulation under the general legislative framework of the FCA (rather than being solely contained in a discrete part of the statute), including by extending the application of the objectives and regulatory principles to the general functions under Part VI

As outlined in our April Response, although we consider that the FCA is a more appropriate home for the UKLA than a separate regulator, we do believe that the regulatory focus and priorities of the UKLA are, and should remain, different from those of the rest of the FCA. Primary and secondary market regulation is based strongly on market transparency designed to enable investors to make decisions in an appropriate timeframe and based on the correct information (via prospectuses, RIS disclosures or annual/interim

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reports). This ties into market abuse regulation but has very little linkage to supervisory, prudential or conduct regulation which will be the main focus of the FCA.

On this basis we believe that the decision to try and bring the UKLA and Part VI within the general legislative framework of the FCA rather than retaining a discrete Part VI regime is misguided and unlikely to lead to any positive benefit in terms of protecting or enhancing confidence in the UK financial system. We believe a function like the UKLA needs to have a UK competitiveness focus in terms of objectives and that, whilst possibly appropriate for a prudential and conduct regulator, the FCA objectives are not appropriate for a market/transparency type regulator. We believe that the 'have regards to' duties set out in section 73 of FSMA remain appropriate for the different kind of regulatory function the UKLA carries out which is neither prudential nor conduct based.

We appreciate that the FSA and HM Treasury may feel this kind of approach to statutory objectives and responsibilities may in some way be responsible for regulatory failures over the past few years. In a supervisory and prudential context this may be the case. However we do not believe it is appropriate to take this approach with primary market regulation. The general role and obligation of the UKLA is to ensure appropriate disclosure by issuers at the correct time and then the market and securities holders can make decisions, including decisions to take legal action against issuers if they believe the information is lacking in any material respect, based on such information.

In short we think the listed markets and UKLA would benefit from the FCA, in its capacity as UKLA, having objectives and 'have regard to' factors more closely aligned to those set out in section 73 of FSMA than those proposed for the FCA which do not appear appropriate to us to a market and disclosure based regulator.

Allowing the FCA to discontinue or suspend a listing at the request of an issuer without following the statutory notice procedure (clause 14)

We welcome the changes that have been made to put this regime on a more practical and understandable footing.

Extending powers to impose sanctions on sponsors in relation to certain contraventions subject to the normal procedural mechanisms in FSMA and the right to refer the matter to the Tribunal (clause 15)

This is not a matter on which the GC100 has specific views. We would be concerned if this led to an increase in fees for sponsors if they anticipate additional risk or cost in listed transactions. Again we are not aware of specific failings in sponsor firms which justify this new proposal.

Increasing the limitation period for imposing penalties for breaches of Part VI rules from two to three years (clause 16)

As set out in our April Response, we feel the current approach to Part VI and UKLA has worked well and we see no reason why it should be considered correct to read across any aspects of the UKLA powers to other parts of FSMA, the FSA or the FCA. Any change has to be justified on market failure and cost benefit analysis. Justifying changes on the basis of housekeeping and alignment with the rest of the FSA/FCA (as per the February Consultation) are in our mind fundamentally incorrect.

Allowing the FCA to require an issuer to appoint a skilled person to prepare a report in respect of a matter on which the UKLA could require information to be provided (clause 18)

As set out in our April Response, we see this as a significant increase in the powers and regulatory toolkit of the FSA/FCA without any real justification or understanding of any supposed market failure or cost benefit analysis which has led to this significant policy development. This power could materially alter the whole approach of the listed market and the FCA/UKLA to each other and does not appear justified in our minds. We are worried that such powers, once in existence, will be used frequently and for matters which may be considered immaterial. We would suggest that rather than being a 'less onerous' way of dealing with enforcement or pre-enforcement matters this regulatory tool is much more likely to be used regularly to deal with matters which are dealt with through dialogue and correspondence presently.

We do not believe that this will 'strengthen the listing regime and maintain London's reputation as a leading centre for capital raising and primary markets'. Instead, we see this as adding to the regulatory burden and cost of being listed in the UK, specifically for debt and specialist securities issuers. This may be appropriate power, if used sparingly and sensibly, in relation to authorised firms but we do not consider this to be an appropriate tool for listed issuers and markets. It also appears to be the kind of tool which prudential and conduct regulators are becoming increasingly attracted to – the benefits of this are less clear.

The area where the FCA will want to use these powers is to establish whether the Listing Principles are being complied with. When the Listing Principles were introduced the market was assured by the UKLA that they had no intention of enforcing the principles independently of a substantive breach of one of the other rules. We do not see any change in relation to the functioning of listed issuer markets which suggests this radical and costly change is justified and the FCA has no need for these powers.

One of the consequences of this procedure is that a firm may be guilty of no misconduct but still have to pay, sometimes very large amounts, to consultants to review and report on the way they achieve compliance. That may be appropriate for authorised firms where compliance with general requirements for systems and procedures are fundamental to their ability to comply with the rules but such a power is disproportionate when applied to listed issuers.

Allowing the FCA to make and enforce requirements on persons approved as primary information providers (clause 19)

We have no specific comment to make in relation to this matter but would again be concerned to understand the justification for the increased regulation and that this be balanced against an inevitable increase in cost arising from regulation/overregulation.

Summary

We strongly urge HMT reconsider the approach to try and shoehorn listing and the UKLA into the mainstream of FCA process, procedure and regulatory approach. Listed issuers do not have to deal with customers for whom special protections are appropriate and to whom special duties should be owed, the supervision and enforcement of which may involve a detailed examination of the business of the firm concerned. Instead, the regulatory regime for which the UKLA is responsible is much more a "rules of the road" system where those who transgress should be brought to account through a process of enforcement. This should be reflected in distinct statutory objectives and 'have regards' to factors and a clear recognition that skilled persons reports are not appropriate for the listed issuer environment. The balance which ensures that London remains an attractive environment for equity and debt capital raisings is delicate, is only tangentially and in a minor way linked to the financial crises, and competitiveness can only be threatened by this kind of unjustified regulatory creep.

Please note that the views expressed in this letter do not necessarily reflect the views of each and every member of the GC100 or their employing companies.

If you have any questions, please do not hesitate to contact me.

Yours faithfully,

Mary Mullally
Secretary, GC100

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Genworth Financial

Response to HM Treasury Consultation Paper
"A New Approach to Financial Regulation – The Blueprint for Reform"

August 2011

List of Questions

Question 1: Do you have any specific views on the proposals for the FPC as described in paragraphs 2.6 to 2.24 and in Chapters 3 and 4?

We would like to reiterate our comments made in our written submission to the last consultation: The Financial Policy Committee needs to ensure that the wholesale and investment banking sectors are not overrepresented. We welcome the government's intention to consult further on this during the period of pre-legislative scrutiny.

Question 2: Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payments systems as described in paragraphs 2.32 to 2.40 and in Chapters 3 and 4?

Not applicable to our sector.

Question 3: Do you have any comments on the proposed crisis management arrangements and the proposals for minor and technical changes to the Special Resolution Regime as described in paragraphs 2.46 to 2.61 and in Chapters 3 and 4?

We find the draft provisions on crisis management appropriate and await further details in due course.

Question 4: Do you have any comments on the objectives and scope of the PRA, as described in paragraphs 2.46 to 2.61 and in Chapters 3 and 4?

We welcome the fact that the government recognises that insurance is different from banking and that it proposes to insert a separate insurance objective into the PRA's remit (as per clause 2C of the draft Bill). We find the insurance objective itself to be appropriate and also support the intention to grant the PRA additional powers over time, as and when market developments warrant such an addition.

However, we remain concerned about the fact that competitiveness has been dropped as a principle. The consultation paper notes that sustainable growth in the UK financial services sector will come about as result of a "rigorous and effective regulatory framework", but this should not be mutually exclusive. Regulation must also be proportionate so as not to stifle product innovation. For such a balanced regulatory culture to be embedded it is necessary for a top-level objective linked to competitiveness to be retained in the overarching legislation and regulatory framework as it will serve as a high-level reference point.

Question 5: Do you have any comments on the detailed arrangements for the PRA described in paragraphs 2.62 to 2.78 and in Chapters 3 and 4?
The proposed provisions on governance and accountability seem fair and balanced to us.

Question 6: Do you have any views on the FCA's objectives – including its competition remit – as set out in paragraphs 2.80 to 2.90 and in Chapters 3 and 4?
We agree with the government that the proposed competition duty for the FCA is the right approach.

We also fully support the regulatory principles for the FCA, as contained in the draft Financial Services Bill, and hope that clause 1.2 f) in particular – the general principle that consumers should take responsibility for their decisions – remains in the draft Bill. It is important for consumers to make decisions based on accurate and transparent information. However ultimately they cannot be absolved completely from any responsibility for having taken decisions.

We note the recent consultation about the proposed re-allocation of responsibility for the regulation of consumer credit from the OFT to the FCA. In our view this will have quite profound consequences for the credit industry and ancillary operators and should be considered carefully: the shift from rule-based to principles-based regulation may result in an increased and disproportionate regulatory and cost burden, which may ultimately result in higher costs for consumers and/or business.

Question 7: Do you have any views on the proactive regulatory approach of the FCA, detailed in paragraphs 2.91 to 2.110 and in Chapters 3 and 4?
We are broadly supportive of the FCA's proactive regulatory approach, as outlined in paragraph 2.95 – 2.110 of the consultation document.

However, we would expect this power to be used only as a last resort when earlier attempts to rectify any identified shortcomings have been exhausted. When this power is finally used, we would expect the FCA to establish a strict timetable in order to review this prohibition periodically throughout the maximum 12-month period to establish whether the measure remains valid and justified. Furthermore, we believe that a statutory reference to the right of appeal against the temporary measure should be included in the Bill.

We support the FCA's powers to ban financial promotions which are misleading and unfair etc. We also agree with the proposal that such decisions should be made public – though we hope that these powers will be used mainly in relation to serious issues, not minor transgressions.

Lastly, we remain concerned about the FCA's powers for early publication of disciplinary action: This implies a certain "guilty until proven innocent" approach, which goes against the principle of natural justice. The danger of this approach has been evident in recent media headlines surrounding criminal cases, and we firmly believe the FCA should not go down this route – even if this power is not a duty.

Question 8: What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?
The possibility of launching a super-complaint already exists via the OFT, so it would seem only logical to extend this also to the FCA. We welcome the contribution consumer groups make, but believe that an important safeguard needs to be put in place: namely, the Regulator needs to make sure that any super-complaint lodged by nominated parties is evidence-based and not of a merely anecdotal nature.

Question 9: What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?
The proposals under this heading seem fair: the existing super-complaints procedures have worked well and are transparent; including the 90-day period.

Question 10: Do you have any comments on the competition proposals for the FCA set out in paragraphs 2.111 to 2.119 and in Chapters 3 and 4?
We believe that granting the FCA referral powers to the OFT is fair, and that a joint scrutiny of cases by both bodies is the right way forward.

Question 11: Do you have any views on the proposals for markets regulation by the FCA, described in paragraphs 2.120 to 2.123 and in Chapters 3 and 4?
No.

Question 12: Do you have any comments on the governance, accountability and transparency arrangements proposed by the FCA, as described in paragraphs 2.124 to 2.132 and in Chapters 3 and 4?
These proposals seem entirely fair and proportionate to us.

Question 13: Do you have any comments on the general coordination arrangements for the PRA and FCA described in paragraphs 2.138 to 2.149 and in Chapters 3 and 4?
We would like to emphasise again the need for tight coordination between PRA and FCA, especially in the area of information gathering, to avoid duplication. Businesses should not be faced with simultaneous demands for information and scrutiny by two regulators and supervisors at the same time.

Question 14: Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described in paragraphs 2.150 to 2.195 and in Chapters 3 and 4?
We support the government's proposals on permissions, but would expect further clarity on the approved person's regime: we would hope that only one specific authority is responsible for it – otherwise it would lead to a duplication of requirements and responsibilities.

We are happy that passporting rights and rules will be the responsibility of the PRA and welcome the clarity that this provides. The same should be the case for systems and controls.

Question 15: Do you have any comments on the proposals for the FSCS and FOS set out in paragraphs 2.196 to 2.204 and in Chapters 3 and 4?
The new proposals are helpful and a step in the right direction, but a lot depends on the detail contained in the Memorandum of Understanding. We remain concerned about the consistency and quality of decisions by the FOS, which in the past have often been very different in respect of different players in the industry – and despite being based on similar facts.

Background to Genworth Financial

Genworth Financial is a leading financial security company serving the lifestyle protection, retirement income, investment and mortgage insurance needs of more than 15 million customers, with operations in 25 countries.

In the UK, Genworth focuses on two product lines – Lifestyle Protection insurance for individual consumers and Mortgage Insurance for lenders. These products play a valuable role in providing long-term stability for borrowers and lenders and expanding sustainable homeownership.

Genworth's expertise gives a clear perspective on some of the most critical global economic trends, their impacts and how they might best be mitigated in the UK.

Genworth has embedded the FSA's principles of Treating Customers Fairly into all aspects of our business. We believe in providing customer choice and customer service. We are committed to transparency and furthering consumer education. We also believe in playing by the rules and strongly endorse any regulation that eradicates misselling.

For more information please contact Jürgen Boltz, Senior Government Relations Manager on 020 8380 2164

To see more about our business, visit www.genworth.co.uk

Emil Levendoglu
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14 September 2010

Dear Mr Levendoglu

Thank you for your e-mail of 8 September. I'm afraid I do not have the time to answer the consultation questions set out in Appendix A to HM Treasury's July 2010 publication entitled "A new approach to financial regulation: judgement, focus and stability", but, nevertheless, enclose for your interest three recent publications of mine which address most of the issues raised from a personal perspective. My main concern regarding the proposed "structural" changes is that there is no guarantee that returning prudential regulation and supervision to the Bank of England from the FSA will raise the cost-effectiveness of regulatory and supervisory policy. I concede that the FSA performed poorly in the run-up to and during the recent financial crisis but, I would argue, it seems to have already "raised its game" considerably since then under new leadership; and the same charge could be levied against the Bank. Accordingly, I, for one, would be willing to give the FSA the chance. The Bank of England's previous "failings" with respect to Johnson Matthey Bankers, BCCI and Barings, although evident some time ago, do not inspire confidence that the policy *volte face* will necessarily prove productive. I remain unconvinced that the required changes in culture at the Bank to promote sound regulation and supervision will emerge; I look forward to being proved wrong. Moreover, the dramatic increase in responsibilities to be given to the Bank raise concerns about its future credibility (because of the inevitability of future bank failure) and independence (because of Parliament's increased scrutiny).

As for the switch to a "twin peaks" type structure, it is not self-evident that "performance" will improve. I believe the criticism of the FSA's alleged pre-occupation with "conduct of business" rules, to the detriment of its other supervisory duties, is somewhat overdone.

In summary, given the enormous "costs" associated with the proposed changes, I am not convinced that either the cost-effectiveness or the effectiveness of financial regulatory and supervisory policy will improve vis-à-vis the current, post-crisis operating environment should the current reform proposals be implemented. This is not to argue necessarily in favour of the status quo – my own structural reform proposals are set out in my "UK Financial Reform" publication – but some cost-benefit analysis might usefully be undertaken of alternative structures.

With best wishes.
Yours sincerely

Maximilian J. B. Hall, Professor of Banking and Financial Regulation Encs

Dear Sirs,

In continuation to previous replies I again like to take the opportunity to comment on the latest stage of this consultation – as before solely on the FCA part being the only within my remit. My comments will hence also be applicable on the FCA approach document I only now became aware of. I equally would like to be included into further consultation of the same.

1. Both consultations acknowledge the "mass detriment seen over the past decade" and rightly conclude to put measures in like the FCA's intervention and redress powers place to avoid repetition. This no doubt is a significant move in the right direction.
   While referring to past examples and related loss of customer confidence in regulation both yet seem to be worded mostly forth looking only, i.e. addressing future potential incidents of detriment, but not expressively covering redress of past misconduct.
   In my view it is paramount to re-establishing customer confidence in regulation that there is a firm and specific commitment that the FCA will address past shortcomings of regulation having in itself contributed to "mass detriment seen over the past decade".
   The FCA approach document on page 19 mentions the subject of "pricing" especially in retail banking.
   Despite the substantial public campaign on this matter in recent years little has changed in principle and only very limited redress has been paid solely as a matter of "goodwill" while legal pressure in form of the eventually failed OFT case was on.
   Most customers would clearly see the FCA failing if it was to solely intervene forth going without demanding firms to redress past misconduct on the same matter not sufficiently intervened to by the FSA in the past (as acknowledged). While this has happened with PPI and other examples given in the FCA approach document it is not clear enough that this will continue following the replacement of the FSA with the FCA.

2. With regards to consultation question 8 I believe that the ability to refer concerns to the FCA should be open to everyone, not just nominated parties. While clearly and rightly it is not the FCA's role to handle individual complaints, individuals clearly should be able to raise concerns about conduct likely to affect large numbers of customers and as such. for the FCA to investigate. In the past both FSA and FOS have refused to act on such concerns leaving customers without any option to be heard.
   Again as a matter of re-establishing confidence in regulation the FCA should not go down the same road.

3. With regards to consultation question 9 I believe that it will be vital as a means of deterrence and customer protection for the FCA to act timely and transparent by publishing its activities whether it is warnings or decisions. Additionally, this also will greatly help re-establishing confidence in regulation.
   The fact that firms continue to argue the risk of reputational damage caused by such disclosures clearly shows that they have a long way to go in regards to their attitude to customer relations. There is quite obviously a misperception on their side as to what causes the reputational damage: it is the firms' conduct, not the fact to publish investigations and their outcome. No other industry would get away with this and nor should the financial industry – not to talk of trying to imagine anything similar in criminal justice.
   Finally, it is important to re-iterate that firms have the whole range of PR instruments at their hand to make their view heard while especially retail

customers generally have no such means. Publication of FCA activities will significantly narrow that gap.

4. With regards to consultation question 10 it is my view that the proposed approach to competition seems appropriate, however only its application over time will tell whether customers at long last will be able enjoy more real choice than currently when firms widely operate unison in way that clearly would be deemed as collusion in other industries.

Regards
Martin Holzke

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A new approach to financial regulation: the blueprint for reform

Q1: Do you have any specific views on the proposals for the FPC as described above and in chapters 3 and 4?

The FPC: broad points of principle

As currently drafted, the objective for the FPC is too narrowly focused on the avoidance of negative outcomes, without an overriding objective related to supporting the proper functioning of the economy; in part this is because it is based on an insufficiently clearly defined concept – "financial stability". The objective should more closely parallel that of the Monetary Policy Committee, and should focus on ensuring a stable and sustainable supply of finance to the economy.

The FPC's accountability requirements should also parallel those of the MPC, and should include cost benefit analysis and economic impact assessment of the Committee's recommendations and directions.

Conceptual framework

A financial crisis is not defined by the failure of any particular financial institution, but by the actual or perceived cost of withdrawal of the supply of credit from the economy. Withdrawal of credit supply can often be the direct result of the failure of an institution and the ensuing evaporation of liquidity arising from collapse of confidence in the system. Measures to avert financial crisis should therefore be focused primarily on maintaining the appropriate supply of credit to the economy – and the ability to achieve this without additional recourse to the taxpayer – rather than on managing down the risk of institutional failure.

In this respect, we believe the objective of the Financial Policy Committee is insufficiently clear, not least because it rests on an insufficiently clear definition of "financial stability". We would like to propose that a financial system could be defined as stable when it is delivering

- A stable and sustainable supply of finance to the economy
- at a stable and sustainable price, and
- with broadly stable exchange rates.

Since the stable price of finance is the responsibility of the Monetary Policy Committee, we believe stable supply should be the responsibility of the Financial Policy Committee, and the objective of the Committee and relevant legislation should state this clearly. **Credit supply is not stable if it is supported by inadequate capital; and it is not sustainable if regulators demand an inappropriately high ratio of capital to risk weighted assets.**

For this reason, we believe the amendments to the 1998 Banking Act in respect of the Financial Policy Committee should more closely parallel the provisions relating to the role and objectives of the Monetary Policy Committee.

The FPC's objective

"Financial stability" is not sufficiently clearly defined in the legislation to provide an appropriate objective for the FPC. An unclear financial stability objective could build a bias to risk-aversion into the system, which is likely to be at the expense of the economy; and if written into legislation will render government and parliament powerless to regain control of the financial forces which drive economic growth.

The FPC's objective should parallel that of the MPC. Where the MPC is responsible for maintaining a stable price for finance, the FPC should be responsible for maintaining a stable and sustainable supply of finance to the economy. Stable and sustainable supply is defined as a flow of credit for which the supporting capital is both adequate and appropriate to match the associated risk. The FPC's objectives might therefore be redrawn as:

a) to maintain a stable and sustainable supply of finance to the economy, and
b) subject to that, to support the economic policy of Her Majesty's Government, including its objectives for growth and employment.

In this context, financial stability might be defined as a situation in which the economy enjoys a stable and sustainable price for finance, and a stable and sustainable supply of finance. To this might be added the importance of stability in exchange rates.

Macroeconomic policy

The new amendments to the 1998 legislation will establish a third arm of macroeconomic policy – financial policy – alongside monetary policy and fiscal policy. Under the legislation, two of these arms will be placed under the control of the Bank of England.

Governance and accountability are therefore key, and in general terms those for the FPC should parallel the governance and accountability arrangements for the MPC.

That said, we agree that the FPC should be established as a sub-committee of the Court, with the Court therefore responsible for ensuring that the FPC fulfils its mandate as defined by HM Treasury.

We would also recommend that the FPC's accountability to the Chancellor should parallel that of the MPC. In the case of the FPC, this would require that any policy action it recommends or directs should be the subject of a letter from the Committee Chairman to the Chancellor, copied to the Chairman of the Treasury Select Committee, explaining the background and reasons for any such recommendations or directions, **and providing both a cost benefit analysis and an economic impact assessment of such recommendations or directions**.

The interaction between macro-prudential policy and monetary policy

The MPC assesses inflation risks and responds by setting interest rates. The FPC should assess levels of systemic risk in the financial system and respond by adjustments to capital requirements, particularly through the risk weightings on specific asset classes. These two activities should in most cases be complementary, but in rare instances where this may not be the case, the Governor of the Bank of England, who chairs both Committees, should be the arbiter, and should, in consultation with the Court, provide a full explanation for any subsequent policy decision, in writing, to the Chancellor. An additional option might be occasional joint meetings of the two Committees.

Shadow banking

It should be an objective of regulatory reform to keep the majority of credit formation and maturity transformation inside the regulated sector, rather than driving it outside, and attempting to pursue it through extension of the regulatory boundary. This is more likely to be achieved if the FPC is set the objective of maintaining a stable and sustainable supply of finance to the economy. A financial stability objective which became focussed on risk aversion would be more likely to constrain the regulated sector and drive credit formation, credit intermediation and maturity transformation into the shadow sector.

Q2: Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payment systems as described above and in Chapters 3 and 4?

We support the BBA position on this issue. We agree that the Bank should assume responsibility for the regulation of settlement systems and recognised clearing houses, alongside its existing responsibility for recognised payment systems, but recommend that possible overlaps with the FCA should be addressed through an MOU.

Q3: Do you have any comments on:

- **The proposed crisis management arrangements; and**
- **The proposals for minor and technical changes to the Special Resolution Regime as described above in Chapters 3 and 4?**

We also support the BBA position on this issue.

Q4: Do you have any comments on the objectives and scope of the PRA, as described above and in chapters 3 and 4?

We broadly support the PRA's objectives and believe they are appropriate. We support the emphasis given to the importance of financial stability as an objective of the regulatory system and the operational objective of promoting the safety and soundness of PRA authorised persons. We further welcome the clarity of the 'efficiency' and 'proportionality' principles. While we agree that the 'responsibilities of senior management' principle properly holds senior management accountable for securing compliance with the regulatory framework, we believe that this could usefully be expanded to encompass the role of the Board in conducting oversight over senior executive management.

We also welcome the decision by Government to add a specific statutory insurance objective which recognises the range of firms the PRA will regulate.

Q5: Do you have any comments on the detailed arrangements for the PRA described above and in chapters 3 and 4?

We broadly support the detailed arrangements for the PRA, but believe that its accountability and governance arrangements could be strengthened in three important respects. These are:

- While we welcome the requirement for the PRA to make a report to HMT in the event of a significant regulatory failure, we believe that provision should be made in the legislative framework to guard against disclosure of confidential information that may be contained in such reports. There is a real risk that there is pressure to disclose matters which are simply of interest to the public and not of genuine importance to the matter in hand or future policy;

- We are also concerned about the remit of the Upper Tribunal. Under Clause 20(6)(b) of the Bill, if the Tribunal decides not to uphold the regulator's *(i.e.* the PRA or FCA) decision on appeal it must:

  > '[remit] the matter to the decision-maker with a direction to reconsider and reach a decision in accordance with the findings of the Tribunal.'

  We believe that this represents a weakening of the power of the Tribunal and a diminution of the appeals process. The phrase 'in accordance with the findings of the Tribunal' is broad enough to allow the PRA or FCA to depart from the Tribunal's findings. We believe that the Government should reconsider the provisions and maintain the current arrangements. It is essential that there is an effective, robust appeals process in place against regulatory decisions that accords with due process. To be effective, we believe that the Upper Tribunal, as an independent appellate body, must be able to overrule the decision of a regulator, rather than simply remit it back for reconsideration;

- Like the FCA, the PRA should be subject to similar statutory accountability requirements and therefore should be required to hold an annual public meeting with stakeholders, as the FSA is required; and to strengthen the requirement for the PRA to engage with practitioners, we believe that it should have a statutory practitioner panel with which it is required to consult on proposed rule changes.

Q6: Do you have any views on the FCA's objectives – including its competition remit - as set out above and in Chapters 3 and 4?

We are broadly supportive of the FCA's objectives. We welcome the fact that the FCA's strategic objective is focused on 'protecting and enhancing confidence in the UK financial system'. We believe that having a single strategic objective, complemented by three operational objectives, provides a framework that is both narrow enough to provide clarity of purpose but broad enough to be flexible.

We believe, however, that the Government has set out a very ambitious remit for the FCA, as well as an equally ambitious timetable for the transition to the FCA. There is a risk that the FCA will be required to take on too many functions too rapidly, which could, in turn, lead to regulatory overstretch. We believe the Government should therefore ensure that there is a suitable and manageable transition period.

Operational Objectives

We support the FCA's proposed operational objectives, in particular 'securing an appropriate degree of protection for consumers'. We believe, however, that how the FCA defines 'an appropriate degree of protection' will be of critical importance. In this regard, we welcome Section 1C which sets out the factors that the FCA must 'have regard to' when considering what degree of protection for consumers may be appropriate. In particular, we welcome that the FCA must have regard to 'the differing degrees of risk involved in different kinds of investment or other transaction'; we believe that this will be important if the FCA is to achieve its aim of improving the focus on wholesale matters. In addition, we welcome that the

FCA will recognise ‘the differing degrees of experience and expertise that consumers may have’. We believe that this should allow the FCA to take a flexible and balanced approach to consumer protection.

We also welcome the fact that the FCA, in considering what degree of protection for consumers may be appropriate, must have regard to ‘the general principle that consumers should take responsibility for their decisions.’

UK competitiveness

We believe, however, that the FCA’s operational objectives should be expanded to include reference to ‘maintaining the competitive position of the UK’. We believe that maintaining the UK’s competitiveness is vital to encouraging and supporting enterprise and to the overall health of the UK financial services industry. It is also important to avoid activities migrating to jurisdictions outside the regulatory footprint of the FCA.

Competition

We agree with the Government that a single overarching objective, complemented by a general duty to discharge its regulatory functions so as to promote competition where this is not incompatible with its strategic and operational objectives, provides the right competition mandate for the FCA.

We do not believe that the FCA should have a primary competition objective, as suggested by some, as this would expand the FCA’s remit and inevitably distract it from its other responsibilities. The FSA has been accused of being spread too thinly as a result of its wide remit of financial stability, consumer protection, public awareness, market confidence and reduction of financial crime. A narrower remit for the FCA, which the Government has set out, will lead to better clarity of purpose, avoid conflicts of interest and create a more focused approach, which in turn should lead to better outcomes for consumers.

In addition, a primary competition objective would require technical expertise that the FSA does not currently hold. It could also lead to duplication and potentially less effective regulation, as the OFT (to be succeeded by the Competition and Markets Authority) already has a primary objective to promote competition. We believe that any decision to afford a primary competition objective to the FCA would run the risk of a piecemeal, disjointed approach to the application of competition law.

Price Regulation

We are concerned about the adverse impact possible price controls could have on competition, innovation and choice for consumers. If products are transparent and easily comparable, competition between providers should keep prices low, without the need for price interventions. We find it difficult to square the statement that the FCA will not be a price regulator with the suggestion that powers will be exercised following an assessment of prices and charges. It will be critical that the FCA makes clear how and when prices and charges would be assessed and what powers might be used.

Q7: Do you have any views on the proactive regulatory approach of the FCA, detailed above and in Chapters 3 and 4?

We broadly support the proactive regulatory approach of the FCA proposed by the Government. We believe, however, that the draft safeguards in the Bill require strengthening and we offer some detailed suggestions below.

Product Intervention Power

We agree that protecting consumers from detrimental products is an essential part of a conduct regulator's role. We believe that this must be balanced against the need to provide firms with the "safe harbour" certainty they need to undertake their business. We therefore welcome the Government's view that the FCA's new product intervention power should only be used 'where it is appropriate and proportionate, and where it will provide clarity to consumers and firms.' We note with concern, however, that this wording has not been reflected in the draft Bill and we believe it should be.

We welcome the fact that the FCA will consult on and publish a statement of policy governing the circumstances in which it may make temporary product intervention rules. We also welcome that the FCA will not be able to automatically 'renew' any temporary product intervention rules when they expire. In addition, we support the flexibility that the legislation gives the FCA in terms of the length of time a temporary product intervention rule can last. We think it is important that where the FCA believes a ban of less than the maximum 12 months is appropriate, or where it believes that as a result of changing circumstances a ban should end earlier than planned, that it has the ability to do so. Lastly, we support the recognition in the White Paper that the new power is unlikely to be appropriate in relation to the protection of professional or wholesale customers.

We do not believe that these safeguards go far enough, however, and believe they need to be strengthened in the following ways.

Scope of the power

The circumstances in which the FCA may exercise the product intervention power are very broad. The legislation states that the FCA may make rules appearing 'necessary or expedient' to advance not just its 'consumer protection' operational objective but also its 'efficiency and choice' operational objective. We do not believe that the FCA should be able, under normal circumstances, to exercise this power under its 'efficiency and choice' operational objective. The White Paper makes clear that the purpose of this power is to protect consumers from products that are causing or are likely to cause mass detriment. We believe therefore that it makes sense that the power should only be exercised under the FCA's 'consumer protection' operational objective. We believe that it would be sensible for the 'efficiency and choice' operational objective to be treated in the same way as the 'market integrity' objective as set out in Section 137C(b). Namely, that the FCA could only exercise the product intervention power under its 'efficiency and choice' objective if the Treasury by order authorised it to do so.

In addition, the actions that the power allows the FCA to take in relation to a product are also extremely broad, such as prohibiting entry into any agreement whether or not it relates to a product or service provided to a customer. Given the scope of this power, we believe that provision should be made in the Bill requiring the FCA to exercise its power in a way that is appropriate and proportionate to the circumstances of the case and the objectives it is seeking to achieve both as to the manner and length of the intervention. Although the Government has stated that it expects the FCA to use the power ‘where is it appropriate and proportionate’, there is currently no provision to this effect in the Bill.

Representations and Appeals

We believe that firms should have the right to make representations to the FCA on a decision to exercise the product intervention power before it takes effect and that the FCA should be required to take those representations into account (as opposed to ‘have regard’ to them). We also believe there needs to be a right of appeal to the Upper Tribunal for firms against a decision by the FCA to exercise the product intervention power. We believe that it is essential that the appeals mechanism has the ability to consider the underlying merits of cases and should not be restricted to judicial review grounds; the Competition Appeals Tribunal provides an effective model. We believe these additional safeguards are justified by the potential impact a decision to ban a product could have on firms, consumers and the market. We believe that these safeguards should be incorporated into the legislation.

Consultation and Cost-Benefit Analysis

Sections 138N(5) and 138N(6) set out how the FCA cannot make further product intervention rules containing the same, or substantially the same, provision as in the initial rules until the ‘prohibited period’ has ended. We believe that given the ‘prohibited period’ is just one year, this could give rise to a situation in which the FCA could ban a product for 12 months, wait a further 12 months (the ‘prohibited period’), then ban the same product again without consultation or cost-benefit analysis. We believe that this could, in some instances, be tantamount to the permanent product intervention power being exercised but without the same safeguards.

We therefore believe that a more effective system for the exercise of the temporary product intervention power is necessary. We believe that when the FCA issues a temporary product intervention rule, it should be required to consult and perform a cost-benefit analysis during the initial period for which the product is banned to determine whether the ban should be made permanent. If the FCA determines that it does not intend to make the temporary ban permanent, the temporary ban should be discontinued even if it has not yet reached the length of time set out in the initial rule. The FCA should only then be permitted to reintroduce a temporary ban on a product that has already been subject to a previous ban where there has been a material change in circumstances. This would effectively make the ‘prohibited period’ set out in Sections 138N(5) and 183N(6) redundant.

Financial Promotions Power

We welcome the fact that the FCA will be free to revoke or amend any direction it gives under this power following representations from a person to whom notice is given. We also welcome that the FCA will be able to exercise discretion over the information it includes in the publication of the direction.

However, we believe that these safeguards need to be strengthened in order to make them fully effective and balanced. We believe that it should be made a formal requirement in he legislation for the FCA to consider and take into account the representations made by the person to whom the notice is given.

We are also concerned about the circumstances in which the FCA will give directions under this power. As currently drafted, Section 137P(1)(b), provides that if a financial promotion has not yet been published, the FCA will be able to give a direction if it considers that the promotion 'is likely to' contravene financial promotion rules. We believe that this formulation is too broad and the Bill should be amended so that the FCA can only give a direction in relation to a financial promotion that has not yet been published if it 'would' contravene financial promotion rules. Furthermore, we believe that a direction under this power should only be given in relation to a promotion that has not yet been published if the FCA considers that it likely to be published if the direction is not given.

Clause 137P(11) would require the FCA to publish information about a direction even if, after hearing representations, the direction is revoked. We consider this to be illogical and unfair given that it would cause unjustified reputational damage. We believe that the legislation should be amended to prohibit the publication of information relating to a direction that has been revoked.

Early publication of disciplinary action

We continue to believe that the power to publish an early enforcement warning notice poses major risks to firms which could suffer unjustified reputational damage before having had the opportunity to challenge the accuracy of the facts. We also believe that the design of this power carries the real risk that individuals and firms will be dissuaded from making representations to the FCA as the reputational damage will have already been done, and could be viewed as a barrier to due process.

We welcome the safeguards provided for in the Bill, but believe that they should be strengthened. We welcome the fact that the new power will not be expressed as a 'duty', giving the FCA discretion over the power's use. We also welcome that the FCA will, when deciding whether to disclose, have to consider whether the publication of information would be unfair to the person with respect to whom the action was taken (or was proposed to be taken).

We believe, however, that firms must have the express right to comment on the notices and whether publication is appropriate (as opposed to simply being consulted) and the FCA should be required to consider and take into account those comments. We also believe that if the FCA publishes a notice in spite of comments that it is not appropriate to do so, it should be required to explain why it is not unfair to proceed with publication. We believe that when determining the fairness of publication, the FCA should be required to take into account indication of a challenge to the notice as well as reputational impact. Finally, we believe that provision should be made in the Bill which requires the FCA to state in any information that it publishes that it is an early warning notice and the right to dispute has not yet been exhausted.

Q8: What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?

We believe that it is essential that the Government specify in the legislation which 'nominated parties' will be allowed to refer issues that may be causing mass detriment to the FCA. We believe that these 'nominated parties' must have proper and established standing on the issues on which they may make a referral. In addition, we believe that the legislation must establish a clear process for parties impacted by the issues to make representations to the FCA to either challenge or provide evidence on the issues that have been drawn to its attention.

The FOS

We agree with the Government, as set out in Box 2.H, that the FOS has an important role to play in processing individual complaints on a case-by-case basis. This was the initial role for the FOS envisaged when FSMA was consulted on in the 1990s. We further agree that it should not be for the FOS to lead the way on issues that are thought to be causing mass consumer detriment. Nonetheless, our strong view remains that the FOS has mutated into a mass claims body, making decisions that go far beyond individual complaints, acting as a regulator without any of the accountability mechanisms that a regulator would normally be subject to.

We therefore believe that the FOS requires more fundamental reform to deal with the lack of an effective appeals mechanism for FOS decisions, which we believe is a significant flaw in its accountability. While firms are able to challenge FOS decisions by judicial review, this process only allows firms to challenge the process by which the FOS reached a decision, not the basis for the decision itself. There is no mechanism to challenge what the Ombudsman has decided is a 'fair and reasonable' outcome; a judgement that is wholly subjective.

We believe there is an urgent need for the creation of an independent appeals mechanism, capable of determining what is 'fair and reasonable in all the circumstances of the case' (i.e. the basis on which the FOS reached a decision). One option would be to provide for an appeals mechanism through the existing Upper Tribunal, if it is specifically given the power to review the facts and merits of a dispute, i.e. the substance of the underlying issues, not simply the form of the decision. We have made further comments about the Government's proposals to reform the Upper Tribunal in our response to Question 5. We consider that the availability of an independent review of decisions on a merits basis in those cases where FOS decisions have much wider implications is imperative.

We believe that the structural reform process currently being undertaken by the Government, of which the FCA forms part, represents an ideal opportunity to address this issue and to greatly improve FOS decision-making and accountability. We urge the Government to take this forward.

Q9: What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?

We support the proposal to require the FCA to set out its decision on whether a particular issue or product is causing mass detriment and its preferred course of action. We believe that if 'nominated parties' are to be given the power to refer issues to the FCA for consideration, then it makes sense that the FCA should set out its response to that referral. Furthermore, it makes sense that the FCA should be required to do this within a set period of time.

Q10: Do you have any comments on the competition proposals for the FCA set out above and in Chapters 3 and 4?

We are broadly supportive of the proposal to give the FCA the power to initiate an enhanced referral to the OFT where it has identified a potential competition issue that may benefit from technical competition expertise. We believe that this power will reinforce the FCA's ability to deliver on its competition duty and to meet its primary objective.

We also support the retention of the regime for scrutinising the regulation of financial services by the competition authorities, and we support the reforms that the Government proposes to make to this regime. We believe that leaving competition expertise and competition law powers to the competition authorities will avoid any unnecessary and potentially detrimental overlap of regulatory responsibilities. It will also ensure that all the procedural safeguards which exist within the competition law process – where firms have the right to challenge decisions made by competition authorities by referral on judicial grounds to the Competition Appeals Tribunal – are maintained.

Q11: Do you have any views on the proposals for markets regulation by the FCA, described above and in Chapters 3 and 4?

We are broadly supportive of the proposals for markets regulation by the FCA. We welcome the fact that the existing arrangements will largely continue under the new regime. In particular, we support the Government's decision to place the UK Listing Authority (UKLA) within the FCA.

We believe that it is important to ensure that the new regulators distinguish between retail and wholesale customers, and that they avoid allowing retail regulatory approaches to 'leak' into wholesale regulation where they are not appropriate.

Q12: Do you have any comments on the governance, accountability and transparency arrangements proposed for the FCA, as described above and in Chapters 3 and 4?

We are broadly supportive of the proposed governance, accountability and transparency arrangements for the FCA. We welcome the statutory consultation requirements on both the PRA and the FCA which we believe will be important accountability requirements. In addition, we welcome the Government's decision to take forward the proposal to require the FCA to investigate and make a report on possible regulatory failure. We further welcome that the Treasury will have the power to direct the FCA to do this even if the FCA has determined that the two triggers for such an investigation have not been met.

We are also supportive of the retention of statutory panels, which provide an essential external challenge to policy proposals and bring invaluable insight into the practical impacts, costs and benefits of those proposals.

We believe, however, that for the governance, accountability and transparency arrangements for the FCA to be effective they must include appropriate safeguards on the FCA's actions. As we discussed in our response to Question 5, we believe that the Government's proposal to limit the course of action available to the Upper Tribunal will substantially weaken the appeals process and as a result will weaken the accountability of the FCA. We believe that the Government should reconsider this proposal and maintain the existing arrangements. We believe it is essential that the Tribunal has the power to overrule the regulator, rather than to simply remit the decision back for reconsideration as Clause 20(6)(b) currently states.

In addition, as we discussed in our response to Question 7, we believe that when the FCA exercises its powers (such as the product intervention power) there must be effective mechanisms in place to allow firms to make representations to the FCA and launch appeals against FCA decisions. We believe that these mechanisms need to be incorporated into the legislation. We understand that the Government is keen to avoid rendering the FCA's powers un-usable through overly onerous safeguards. However, we believe that it is perfectly possible to create a mechanism that would give firms the ability to challenge FCA decisions, but would still give the FCA the latitude it needs to exercise its powers.

Q13: Do you have any comments on the general coordination arrangements for the PRA and FCA described above and in Chapters 3 and 4?

We believe that effective coordination between the PRA and the FCA is of paramount importance to the successful operation of the new regulatory architecture. It is required to ensure that unnecessary regulatory overlap and duplication is avoided, particularly for dual-regulated investment firms.

We support the PRA and FCA's proposed requirement to coordinate as well as the requirement to draw up a Memorandum of Understanding (MOU). We welcome the acknowledgement by the Government that the FCA and PRA should, when conducting their annual review of the MOU, consult with regulated firms, consumer groups and others. We would stress the importance of ensuring that this consultation is meaningful and that the views of the industry are fully taken into consideration. We also welcome the new requirement for the PRA and FCA to include in their annual reports an account of how they have coordinated during the year.

We also support the proposal to give the PRA the power to prevent the FCA from taking actions where it considers that these may lead to the disorderly failure of a firm, or wider financial instability. However, as the legislation currently stands the PRA is not under an obligation to exercise this power, even if it has identified an FCA action that would meet the criteria set out in Section 3H. We believe that the PRA should be under such an obligation. We therefore believe that Section 3H(1) should be amended to read as follows:

'Where the first, second and third conditions are met, the PRA ***shall*** give a direction under this section to the FCA.'

Dual-regulated firms

We believe that there is scope to improve the arrangements for coordination between the PRA and FCA in relation to dual-regulated firms. We would support the creation of a Single Point of Contact for dual-regulated firms as we believe this would avoid the duplication that would likely be caused if those firms had to liaise with both the PRA and FCA separately. We believe that this should take the form of a Supervisory Team that would sit between the FCA and PRA and would interact with the various departments within a dual-regulated firm (such as Compliance, Legal and Finance), much as the specifically assigned supervisory teams in the FSA currently operate. We believe this arrangement would be more efficient and would be particularly important in crises, as well as resolution and recovery and day to day enforcement matters.

In addition, we would support the creation of a joint rule book for dual-regulated firms as we believe this would greatly simplify and streamline the regulatory framework within which these firms will operate. We believe a joint rule book would help to ensure a consistent regulatory culture between the PRA and FCA and would prevent them from diverging over time. We also believe that it would be particularly helpful where competences overlap, for example in relation to systems and controls issues. In addition, we believe the UK should be moving in this direction regardless of the regulatory restructure currently under way given the increasing importance of EU requirements that are limiting the UK's ability to issue separate guidance. Therefore, we feel this is an idea that should be given serious consideration by the Government.

Q14: Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described above and in Chapters 3 and 4?

Our overall view on the regulatory processes involving the PRA and FCA is that to the greatest extent possible they should be simple, streamlined and should avoid unnecessary and potentially detrimental duplication and overlap.

On authorisation, we support the Government's decision to proceed with the 'alternative approach' as set out in the February consultation. We believe that it is sensible for the authority that would be responsible for an applicant's prudential regulation to manage the application process and ultimately grant permission.

We are concerned, however, about the proposed arrangements for the approval of approved persons as there is, we believe, the potential for confusion between the PRA and the FCA. The Government wishes to give primary responsibility for defining a Significant Influence Function (SIF) requiring approval to the PRA, with the FCA being able to designate a SIF if the PRA has not done so. The FCA then appears to have the power to remove approval from a SIF, or any other approved person, for 'egregious conduct.' We believe that consultation between the PRA and the FCA will be essential if they are to avoid confusion and contradictory decision-making in this area.

Q15: Do you have any comments on the proposals for the FSCS and FOS set out above and in Chapters 3 and 4?

FSCS

We support the Government's proposal to make the PRA and FCA jointly responsible for the FSCS, whilst retaining it as a separate scheme.

The FOS

We support the Government's proposals to improve coordination between the FCA and the FOS.

We are supportive of the proposed requirement for the FOS to pass information to the FCA which 'would or might be of assistance to the FCA in advancing one or more of its objectives' (Schedule 10, Section 232A). However, we believe that this requirement is extremely broad and thus could give rise to a situation in which the FOS passes information which leads the FCA to take interventionist action which could have wide-ranging effects for firms and the market. We believe, therefore, that this reinforces the argument for a robust appeals mechanism against both FCA and FOS decisions. We have set out in our response to Questions 5 and 8 our position on this matter.