



HM Treasury

Financial Services Future Regulatory Framework Review: Proposals for Reform

Financial Services Future Regulatory Framework Review: Proposals for Reform

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



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Foreword

Financial services is one of the UK's most vibrant, innovative and important industries. As Economic Secretary, my role is to deliver on the government's vision for an open, green, and technologically advanced financial services sector. A sector that is globally competitive and acts in the interests of communities and citizens, creating jobs, supporting businesses and powering growth across the UK.

The UK's leadership and innovation in financial services goes back over 400 years: the first paper banknotes, the first regulated stock exchange, and even the first ATM. And following the global financial crisis in 2008, the UK was instrumental in driving the reforms to improve the global financial system and has demonstrated an ongoing commitment to high regulatory standards.

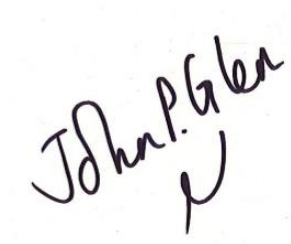
Taking advantage of the UK's new freedoms now we have left the EU, the government wants to build upon our historic strengths to renew the UK's position as the world's pre-eminent financial centre.

The Future Regulatory Framework (FRF) Review will therefore play a critical role in delivering the vision for the sector set out by the Chancellor in his speech at Mansion House in July 2021. The FRF Review provides a once-in-a-generation opportunity to ensure that, having left the EU, the government maintains a coherent, agile, and internationally-respected approach to financial services regulation that is right for the UK.

The previous consultation on the FRF Review, issued in October 2020, received over 120 responses and has been the subject of significant engagement with stakeholders over the last 12 months. I am extremely grateful to everyone who engaged with the previous consultation, and would like to thank Parliamentary colleagues, market participants, consumer groups and other interested stakeholders for their enthusiastic response.

This consultation builds on the previous one, sets out the government's proposals for important changes to the UK's financial services regulatory framework, and seeks to build on the strengths of the UK's existing model of regulation established by the Financial Services and Markets Act 2000 (FSMA). The proposals include changes to the regulators' statutory objectives and enhanced mechanisms for accountability, scrutiny and oversight of the regulators by Parliament, HM Treasury and stakeholders. It also sets out how we intend to return responsibility for designing and implementing regulatory requirements to the UK regulators, a break from the approach under EU law.

This is an important moment for financial services regulation in the UK. I believe that these proposals will support our ambition to ensure that, at home and abroad, the UK's financial services sector is recognised as the most trusted and competitive in the world. I would urge all interested stakeholders to continue to share your views, and I look forward to further engagement on these important issues.

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

John Glen MP

Economic Secretary to the Treasury

Executive summary

Overall approach

1. The Future Regulatory Framework (FRF) Review was established to determine how the financial services regulatory framework should adapt to the UK's new position outside of the European Union (EU), and how to ensure the framework is fit for the future. In particular, the FRF Review provides an important opportunity to ensure that the UK maintains a coherent, agile, and internationally-respected approach to financial services regulation that delivers appropriate protections and promotes financial stability.
2. The current model of regulation was introduced by the Financial Services and Markets Act 2000 (FSMA). The FSMA model delegates the setting of regulatory standards to expert, operationally-independent regulators, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA), that work within an overall policy framework set by government and Parliament.
3. The FSMA model was adapted to address the regulatory failings that contributed to the 2007-08 global financial crisis. The Financial Services Authority was split into the PRA and the FCA. The FCA was given the strategic objective to ensure that the relevant markets function well. The PRA was given the general objective to promote the safety and soundness of PRA-authorized persons. In addition, there were reforms to the Bank of England, most notably the creation of the Financial Policy Committee.¹
4. The government believes that this model remains the most appropriate way to regulate financial services in the UK. It ensures that the regulators' real-world, day-to-day experience of supervising financial services firms is central to the regulatory policymaking process. It also provides flexibility for the regulators to update standards efficiently in response to changing market conditions and emerging risks. Responses to the *Future Regulatory Framework Review (FRF): Phase II Consultation*² published in October 2020 demonstrated that establishing a comprehensive model of regulation based on FSMA, with the appropriate enhancements, is overwhelmingly supported by stakeholders. Consultation respondents agreed with the government's view that the UK's FSMA model is world-leading and that no alternative model provided a preferable approach to financial services regulation.

¹ These reforms were primarily delivered through the Financial Services Act 2012, Financial Services (Banking Reform) Act 2013, and Bank of England and Financial Services Act 2016.

² *Financial Services Future Regulatory Framework Review: Phase II Consultation*, HM Treasury, 2021.

5. The UK's approach to regulation is internationally respected with the UK continuing to be a thought leader in the development of international standards for financial services. As observed by IMF studies,³ when independent regulators make judgements on the design of regulatory standards, they are likely to deliver more predictable and stable regulatory approaches over time.
6. As set out in the previous consultation published in October 2020, the PRA and the FCA remain the right institutions to deliver the UK's financial services regulatory framework. In addition, the government is not proposing to alter the macroprudential elements of the UK's regulatory framework, so the Financial Policy Committee is not within scope of the changes proposed in this document.⁴

Objectives and principles

7. In the strategy document published alongside the Chancellor's Mansion House speech in July 2021,⁵ the government affirmed that the UK will continue to promote high international standards. Robust regulatory standards are the cornerstone of the attractiveness of the UK's markets, and the stability and soundness of the UK's financial system is an important priority for the government.
8. However, the FRF Review provides the opportunity to ensure that, having left the EU, the government establishes a coherent, agile and internationally-respected approach to financial services regulation that is right for the UK.
9. While the UK was a member of the EU, the government was able to ensure that matters of wider public policy, such as growth and international competitiveness, were considered as part of the negotiations to agree regulations at an EU level. As the regulators take on greater responsibility for setting detailed rules across a larger portion of the UK's financial services landscape, the government recognises the need to ensure that their objectives reflect the importance of the financial services sector as an engine of growth for the wider economy and the need to support the future strength and viability of the UK as a global financial centre.
10. The government therefore intends to provide for a greater focus on growth and competitiveness by introducing new, statutory secondary objectives for the PRA and the FCA.
11. The government also proposes to amend the existing regulatory principles to ensure that sustainable growth should occur in a way that is consistent with the government's commitment to achieve a net zero economy by 2050.

³ *Should Financial Sector Regulators be Independent?*, Marc G Quinyn, 2004.

Financial Regulators Need Independence, Udaibir S. Das, Marc Quintyn and Michael W. Taylor, 2002.

⁴ Actions taken by the regulators to implement directions and recommendations made by the FPC will therefore have specific carve-outs from both the overarching and activity-specific accountability mechanisms proposed here, as they are already subject to the FPC's existing framework of objectives and accountability.

⁵ *A new chapter for financial services*, HM Treasury, July 2021.

Retained EU law

12. In the years since FSMA was introduced, and in particular following the global financial crisis and the growth of the single market in the EU, EU financial services regulation has expanded into new areas, and become significantly more detailed, which has affected the operation of the FSMA model. In particular, EU regulations complicated the split of responsibilities established by FSMA. They constrained the regulators' ability to determine the most appropriate regulatory requirements for UK markets, and required them to apply EU regulations and operate within the EU framework.
13. The body of EU legislation that applied directly in the UK at the point of exit was transferred onto the UK statute book by the European Union (Withdrawal) Act 2018. This is known as "retained EU law".
14. This approach to retained EU law has left the UK with detailed regulatory requirements in primary and secondary legislation, which should under a FSMA approach primarily be in the regulators' rules. The effect of having these regulatory requirements in legislation is that it is difficult and time-consuming to update, and places substantial resource pressures on Parliament which is asked to consider a large volume of highly technical provisions. For example, the Markets in Financial Instruments Regulation sets percentage caps on how much trading volume can happen outside of a trading venue.
15. The government intends to move to a comprehensive FSMA model of financial services regulation, with the appropriate enhancements to ensure that the regime remains fit for the future, and can support the UK's high standards of regulation. This means that the financial services regulators will take responsibility for setting many of the direct regulatory requirements which are currently set out in retained EU law. Direct regulatory requirements are the obligations that firms are expected to follow, with the framework within which the regulators must operate being set by Parliament and the government. Regulation in financial services is evolving all the time, with new developments and technologies requiring regular amendments. Empowering the regulators to set the direct regulatory requirements will allow for the necessary evolution of the rulebook, in a way that maintains the UK's high standards of regulation. Transferring that responsibility to the regulators will require the government to gradually repeal significant amounts of retained EU law so that the regulators can replace it with the appropriate regulatory requirements in their own rulebooks.
16. FSMA already gives the regulators extensive rulemaking powers, and in many cases deleting the relevant retained EU law will allow the provisions to be replicated in the regulators' rulebooks. However, the regulators' existing rulemaking powers are not sufficiently broad to allow them to make rules covering all areas of financial services regulation currently in retained EU law. This is because many activities, particularly since the financial crisis, were brought into regulation through direct EU legislation rather than by expanding the regulators' powers under FSMA. Where this is the case, the government proposes to provide the regulators with the necessary additional powers to make rules relating to those matters currently in retained EU law.

17. As part of this, the government is considering granting the Bank of England general rulemaking powers over central counterparties (CCPs) and central securities depositories (CSDs), where they currently have only limited rulemaking powers. This will be accompanied by appropriate enhancements to the Bank of England's current framework of objectives and accountability in relation to the regulation and supervision of these entities. The government will set out further details in due course.
18. In many instances, the government would expect the regulators to initially replace the repealed provisions with rules that are similar to those which are currently in place. However, this approach will allow the regulators to ensure that the rules are properly tailored for the UK markets, and appropriately reflect their objectives. It will also mean that the rules can be more efficiently updated in the future, for example in response to new global standards, or to take account of new business models.
19. Delivering these changes will be a significant undertaking, and each piece of relevant retained EU law will need to be addressed individually in order to move to an approach that is consistent with the FSMA model of regulation once the necessary primary legislation is in place. That means that many of the necessary changes will be delivered through an extensive programme of secondary legislation, which is likely to take several years. This means that Parliament will have the opportunity to scrutinise the legislation which enables these changes, and subsequently the statutory instruments giving effect to the changes.

Accountability, scrutiny and engagement

20. With the regulators taking on these significant new regulatory policymaking responsibilities, it is important that both the mechanisms by which Parliament hold the regulators to account, and the mechanisms underpinning the regulators' relationship with HM Treasury, are strengthened. This will ensure there continues to be appropriate democratic input into, and public oversight of, the regulators' activities.
21. The government considers that Parliament has a wide range of powers to request information and conduct effective scrutiny of the regulators, including through the select committee system. To support this work, the government proposes formalising through statute the mechanisms through which the regulators provide information to Parliament to ensure they have the information they need to undertake that scrutiny.
22. The government also proposes to strengthen the engagement mechanisms that exist between HM Treasury and the regulators. This will be achieved through a new requirement for the PRA and the FCA to respond to the recommendations letters issued by HM Treasury, and a new power for HM Treasury to require the regulators to review their existing rules where the government considers that it is in the public interest.
23. In addition, the government considers that there is now a case for ensuring the regulators consider the potential impacts on deference arrangements and assess compliance with relevant trade agreements, as a matter of course when

making rules and when setting general policy on supervision, where relevant and proportionate. The government therefore proposes introducing new accountability mechanisms requiring the regulators consider to the impact of exercising their powers to make rules and set general approaches and policy on supervision upon the UK's deference arrangements, and to assess compliance with relevant trade agreements with overseas jurisdictions.

24. These measures seek to ensure that, as the independent regulators take on more responsibility for regulatory policymaking under the proposed approach, they can continue to be held to account by Parliament and HM Treasury for how they are advancing their objectives.
25. It is vital that there are opportunities for consumers, relevant stakeholders and firms to engage with and scrutinise the development of regulatory proposals. Any policymaking process risks being deficient if it does not draw sufficiently on the views, experience and expertise of those who may be impacted by regulation. The government considers that the existing primary method for this engagement, the regulators' requirement to consult publicly on their draft rules, remains the key mechanism for this engagement.
26. The government also acknowledges that the regulators' statutory panels – an important part of the process through which stakeholders can feed in views on proposals – will be able to provide earlier input into the regulatory policymaking process now that the UK is responsible for all regulatory policymaking outside the EU. The government therefore also proposes to require the regulators to publish a statement on their approach to the recruitment of panel members, to ensure that their membership represents a truly diverse range of stakeholder views. In addition, the government proposes to put the FCA's Listing Authority Advisory Panel and the PRA Practitioner Panel's insurance sub-committee on a statutory footing, in line with the PRA's and FCA's other panels. The purpose and structure of these panels is summarised later in this document.
27. To support these existing avenues for engagement, the government is also introducing proposals to support greater transparency of the regulators' processes, and to strengthen their approach to cost-benefit analysis (CBA). CBA is an important part of the regulators' policymaking process. It helps the regulators to understand the likely impacts of a policy, and to determine whether a proposed intervention is proportionate. The government is therefore proposing the creation of a new statutory panel designed to review, and make recommendations on, the regulators' production of CBA in order to improve the processes. The focus on greater transparency will also be delivered through new requirements for the regulators to publish and maintain public frameworks that set out their approach to reviewing their rules and conducting CBA. These frameworks will offer stakeholders an opportunity to familiarise themselves with, and input into, these important processes, introducing greater transparency of when and how the regulators review their rules and conduct CBA.

Previous consultation

28. The approach set out in this consultation meets the objectives of the FRF Review outlined in the previous consultation from October 2020, which are:
- **clear, coherent and effective allocation of regulatory responsibilities** – The proposed approach will provide a clear split of responsibilities. The proposal will allow the government and Parliament to set the overall policy framework and hold the expert regulators to account for how they advance these objectives and operate within that framework
 - **appropriate policy input by democratic institutions** – The proposed approach aims to build on the existing structures and improve accountability. Moving to a comprehensive FSMA model of financial services regulation in the UK, with the appropriate enhancements to the framework, the government and Parliament will be able to ensure that relevant policy issues must be considered by the regulators when they design their regulatory requirements
 - **clearer basis for effective accountability and scrutiny** – The proposed approach is designed to support more effective accountability, scrutiny and engagement of the regulators by Parliament, HM Treasury, and relevant stakeholders. This includes proposed measures to ensure greater transparency at each stage of the regulatory process and appropriate democratic oversight of the regulatory framework
 - **agile regulatory regime** – Moving to a comprehensive FSMA model of financial services regulation will ensure that direct regulatory requirements which apply to firms will be set through regulator rules, which can be updated in an agile and responsive way to take account of changing market conditions, address emerging risks, and facilitate innovation
 - **coherent and more user-friendly regime for end-users** – Following our departure from the EU, the direct regulatory requirements which apply to firms are set out in a number of places, including retained EU law. This approach aims to bring about, as much as possible, a single source of requirements for firms – the regulators’ rulebooks
 - **internationally-respected approach** – As a global hub for financial services, a regulatory approach which commands confidence internationally is a priority for the UK. The proposed approach of delegating responsibility for regulatory requirements to regulators operating independently from government is supported by the IMF and OECD
29. This approach for financial services regulation is consistent with the government’s broader vision for Better Regulation, set out in its consultation of 22 July 2021⁶, which builds on the recommendations of the Taskforce for Innovation, Growth, and Regulatory Reform.

⁶ *Taskforce on Innovation, Growth and Regulatory Reform independent report*, Taskforce on Innovation, Growth and Regulatory Reform (TIGRR), June 2021.

Chapter 1

Introduction

Context

- 1.1 The Future Regulatory Framework (FRF) Review was announced by the then Chancellor of the Exchequer at Mansion House on 20 June 2019, with the objective of reviewing the UK's financial services regulatory framework to ensure it is fit for the future. The Review represents an important opportunity, following the UK's departure from the European Union (EU), to ensure that the financial services regulatory framework reflects the UK's new position and supports delivery of the government's vision for the financial services sector.
- 1.2 The UK's regulatory framework sets the overall approach to regulation of financial services, and establishes the institutional architecture needed to operationalise the regulatory regime.
- 1.3 The operation of the UK's financial services regulatory framework was heavily influenced by the UK's membership of the EU. Now that the UK has left the EU, it is necessary to consider how important policy and regulatory functions previously carried out at the EU level will be exercised, and to ensure a standalone UK regime is fit for the future.

Vision for the financial services sector

- 1.4 In his speech at Mansion House on 1 July 2021, the Chancellor of the Exchequer set out the government's vision for an open, green, and technologically advanced financial services sector that is globally competitive and acts in the interests of communities and citizens, creating jobs, supporting businesses, and powering growth across all of the UK. The Chancellor also reaffirmed the government's commitment to maintaining high regulatory standards. Alongside the Chancellor's speech, the government published a document, *A new chapter for financial services*,¹ setting out the vision in detail.
- 1.5 A key part of this vision is the government's commitment to maintain and build on the UK's attractive and internationally-respected ecosystem for financial services across both regulation and tax. The government intends to tailor its approach to reflect the UK's new position outside the EU, while ensuring it supports and promotes the interests of UK markets and maintains

¹ *A new chapter for financial services*, HM Treasury, July 2021.

high regulatory standards in the face of new and evolving risks. The FRF Review is a key pillar of delivering this vision, as it considers the UK's overall approach to financial services regulation. It also complements a number of further reviews and initiatives that are underway on specific areas of financial services regulation intended to support and encourage growth in the UK as a global financial services hub, while maintaining high regulatory standards. These include the government's reviews looking into the prudential regime for insurers, wholesale capital markets and the UK funds regime.

Previous consultation and debate on the FRF

- 1.6 The first stage of the FRF Review in 2019 examined coordination between the UK authorities that have responsibility for the regulation of the financial services sector. The government published its response on 11 March 2020, announcing that the regulators would set up the Financial Services Regulatory Initiatives Grid and Financial Services Regulatory Initiatives Forum. This was intended to provide a clear picture of expected regulatory activity to help regulators, firms and consumer stakeholders plan ahead, and improve proportionality, co-ordination and transparency across the regulatory landscape for financial services, reducing the operational burden on industry. The Regulatory Initiatives Forum has now published four iterations of the Regulatory Initiatives Grid.
- 1.7 The government also stated in its response to the first stage of the FRF Review that there is a broader set of issues concerning the regulatory framework that need to be addressed. Operation of the UK framework had evolved to accommodate the UK's membership of the EU. The UK's withdrawal from the EU means that it needs to decide how important policy and regulatory functions carried out at the EU level will be exercised in a standalone UK regime. Leaving the EU means that the UK has taken back control of the rules governing our world-leading financial services sector, so the FRF Review is an opportunity to adapt our regulatory approach to meet the specific needs of the UK.
- 1.8 The government published an initial consultation² exploring these key issues in October 2020 and set out an overall approach to financial services regulation, focusing on the split of responsibilities between Parliament, the government and the financial services regulators, and seeking to build on the strengths of the Financial Services and Markets Act 2000 (FSMA) model.
- 1.9 In addition to the government's consultation on the FRF Review, which closed in February 2021, there has been continued debate among interested stakeholders including:
 - Debate in Parliament throughout the passage of the Financial Services Act 2021 (FS Act 2021), where Members of both Houses endorsed a model for the prudential regulation of banks and investment firms where the regulators set direct regulatory requirements which apply to

² *Financial Services Future Regulatory Framework Review: Phase II Consultation*, HM Treasury, 2021.

firms, within the overall FSMA framework set by Parliament. This is in line with the proposed approach set out in this consultation

- Throughout passage of the FS Act 2021, Members of both Houses debated the regulators' accountability mechanisms – particularly in relation to Parliament – as well as the regulators' statutory objectives and regulatory principles. The government's position throughout these debates was that the appropriate forum to consider such issues was through the FRF Review, which looks at the question of financial services regulation in the round, rather than the FS Act 2021
- Reports from the Treasury Select Committee (TSC)³ and the All-Party Parliamentary Group (APPG) for Financial Markets and Services,⁴ which considered the approach outlined in the government's October consultation and made recommendations to government and Parliament
- Lord Hill's report on the UK's listings regime,⁵ which included (amongst other issues) a recommendation for the government to consider the case for amending the Financial Conduct Authority (FCA)'s statutory objectives to include a 'competitiveness' or 'growth' requirement
- The report from the Taskforce on Innovation, Growth and Regulatory Reform (TIGRR)⁶ and its recommendations to ensure that the UK's regulatory framework effectively supports innovation and growth

Financial services legislation

The FSMA model

1.10 The UK's financial services system is underpinned by the framework set out in FSMA, and in the previous consultation the government consulted on the proposal to move to a comprehensive FSMA model of financial services regulation.

1.11 As described in the previous consultation, the FSMA model has changed over time. The financial crisis of 2007-08 revealed serious flaws in the UK's system of regulation, particularly in the allocation and coordination of responsibilities across the 'tripartite' institutions – HM Treasury, the Bank of England, and the Financial Services Authority (FSA). The Bank of England had inadequate tools to play its role in ensuring financial stability; the FSA's responsibilities were too broad to allow for sufficient focus on the stability of firms; and no part of the framework had responsibility for monitoring the

³ *The Future Framework for Regulation of Financial Services*, House of Commons Treasury Committee, July 2021.

⁴ *The Role of Parliament in the Future Regulatory Framework for Financial Services*, All-Party Parliamentary Group on Financial Markets & Services, February 2021.

⁵ *UK Listing Review*, Lord Hill, March 2021.

⁶ *Taskforce on Innovation, Growth and Regulatory Reform independent report*, Taskforce on Innovation, Growth and Regulatory Reform (TIGRR), May 2021.

crucial link between the stability of individual firms and the stability of the financial system as a whole.

- 1.12 The post-crisis reforms were therefore focused on institutional design and allocation of responsibilities, with the FSA abolished and replaced with the Prudential Regulation Authority (PRA) and FCA. The PRA was made responsible for the prudential regulation of firms which manage significant balance sheet risk, and the FCA was made responsible for the regulation of conduct. In addition, there were reforms to the Bank of England, most notably the creation of the Financial Policy Committee.
- 1.13 However, successive governments have always maintained the same approach to setting the framework for financial services regulation, which is referred to in this consultation as the FSMA model. The FSMA model splits responsibilities across Parliament, HM Treasury, and the regulators as follows:
- Parliament, through primary legislation, sets the overall approach and institutional architecture for financial services regulation, including the regulators' objectives;
 - Parliament establishes the parameters within which HM Treasury sets the 'regulatory perimeter' through secondary legislation, specifying which financial activities should be regulated and the circumstances in which regulation should apply;
 - the expert and operationally-independent regulators have the statutory responsibility for setting the direct regulatory provisions that apply to firms which carry out regulated activities, using the powers given to them by FSMA, and following the processes established by FSMA;
 - Parliament, through FSMA, sets the statutory objectives for the regulators, with requirements set in legislation to ensure appropriate accountability to Parliament, HM Treasury, and the general public
- 1.14 FSMA establishes a framework whereby any person (whether an individual or firm) can only carry out a regulated activity if it is authorised by the appropriate regulator (i.e. is an "authorised person") or is exempt. Under this framework, HM Treasury determines which activities are regulated activities, by specifying activities to be regulated in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO).
- 1.15 Firms wishing to carry out a regulated activity must apply to the appropriate regulator for authorisation to do so, and the regulator must assess applications in line with the requirements established in FSMA, such as threshold conditions, which can include considerations of suitability and business models.
- 1.16 FSMA empowers the PRA and the FCA to make rules which apply to authorised persons. The regulators are required to maintain arrangements for supervising authorised persons, and FSMA gives them powers to monitor

and enforce compliance with the rules. Both the FCA⁷ and the PRA⁸ publish their approach to supervision and enforcement.

Regulatory objectives and principles

- 1.17 FSMA sets objectives for the PRA and the FCA and requires them to act in a way that advances their objectives when carrying out their general functions. This determines what the regulators must seek to advance when they make rules, set technical standards, and issue guidance.
- 1.18 The FCA's strategic objective is to ensure that the relevant markets function well. Its operational objectives are to secure an appropriate degree of protection for consumers, protect and enhance the integrity of the UK financial system, and to promote effective competition in the interests of consumers.
- 1.19 The PRA's general objective is promoting the safety and soundness of PRA authorised persons; it also has an insurance-specific objective of contributing to the securing of an appropriate degree of protection for those who are, or may become, policyholders. The PRA also has a secondary objective to facilitate effective competition in the markets for services provided by PRA-authorised persons in carrying on regulated activities.
- 1.20 The FSMA regulatory principles aim to promote regulatory good practice across the range of the regulators' policymaking. The regulators must take into account 8 regulatory principles when discharging their functions, which are:
- **efficiency and economy** - the need to use the resources of each regulator in the most efficient and economic way
 - **proportionality** - the principle that a burden or restriction which is imposed on a person, or on the carrying on of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction
 - **sustainable growth** - the desirability of sustainable growth in the economy of the UK in the medium or long term
 - **consumer responsibility** - the general principle that consumers should take responsibility for their decisions
 - **senior management responsibility** - the principle that a regulated firm's senior management is responsible for ensuring that its business complies with regulatory requirements imposed by or under FSMA, including those affecting consumers
 - **recognising differences in business** - the desirability where appropriate of each regulator exercising its functions in a way that recognises

⁷ *FCA Mission: Approach to Enforcement*, Financial Conduct Authority, April 2019.

⁸ *The Prudential Regulation Authority's approach to enforcement: statutory statements of policy and procedure*, Bank of England, September 2021.

differences in the nature of, and objectives of, different businesses subject to requirements imposed by or under FSMA

- **openness and disclosure** - the desirability in appropriate cases of each regulator publishing information relating to persons on whom requirements are imposed by or under FSMA, or requiring such persons to publish information, as a means of contributing to the advancement by each regulator of its objectives
- **transparency** - the principle that the regulators should exercise their functions as transparently as possible

Parliamentary oversight

1.21 As Parliament sets the regulators' objectives and gives them the powers to pursue those objectives, Parliament rightly has a unique and special role in relation to the scrutiny and oversight of the financial services regulators. The regulators, when exercising these powers, make regulatory decisions independently from government and Parliament. However, Parliament has the right to require the regulators to explain and justify those decisions.

1.22 The system of Parliamentary select committees is particularly important in financial services policy and in relation to the scrutiny of the work of the regulators. Relevant select committees, and the Treasury Select Committee (TSC) in particular, provide scrutiny of financial services policy in the following ways:

- **Select committee inquiries** – Committees choose their own subjects of inquiry and decide the duration and approach that will be used for each inquiry. The committees have the power to send for "persons, papers and records" which they decide will be relevant. Witnesses asked to give evidence to an inquiry relating to financial services can include Treasury ministers and senior officials as well as senior officials from the financial services regulators. The TSC has undertaken many high-profile and influential inquiries, and senior representatives from the regulators frequently appear before the TSC in the course of its inquiries. Other committees, such as the former House of Lords EU Financial Affairs Sub Committee and the House of Commons European Scrutiny Committee, have also played a key role in scrutinising financial services policy, and the government expects that the recently formed Industry and Regulators Committee, part of whose remit is to scrutinise the work of UK regulators, will play an increasingly important role.
- **Regular hearings to scrutinise the work of the financial services regulators** – the TSC routinely examines the regulators' approach to policy and administration. As part of this work, senior officials from the regulators attend general accountability hearings - for instance the FCA Chair and Chief Executive appear before the TSC biannually and the PRA appears before the TSC after the publication of each annual report. The regulators also provide both written and oral evidence to select committees in both the Lords and Commons on the wide range

of issues that they cover, and routinely provide evidence and expertise to Bill committees and in policy meetings with MPs and Peers.

- **Pre-commencement hearings** – Parliament, through the TSC, conducts these pre-commencement hearings following the appointment of the Chair and Chief Executive of the FCA and the Chief Executive of the PRA. Where the Committee does not wish to recommend the appointment of the FCA Chief Executive, it can recommend that it be put to a vote on the floor of the Commons.

1.23 There are also long-established scrutiny arrangements in place for Parliament to hold Ministers of the Crown accountable for the work of HM Treasury and the UK’s financial services regulators.

Accountability to HM Treasury

1.24 Treasury ministers have overall responsibility for the UK’s financial services regulatory framework and the continued effective operation of the financial services regulators as part of that framework. Treasury ministers can therefore be regarded as having a constitutional duty to ensure the regulators operate effectively and in accordance with framework. Acting within their FSMA statutory powers, and in accordance with relevant provisions in other financial services legislation, judgements on rulemaking and supervision are for the regulators to make. Ministers and officials therefore meet regularly with the regulators to discuss policy issues and areas of joint work or interest, while recognising the regulators’ operational independence.

1.25 Existing legislation already provides a number of formal accountability mechanisms between the regulators and HM Treasury in specific circumstances:

- HM Treasury is responsible for appointing the Chair and the Chief Executive of the FCA, and at least three members of the FCA’s governing body, two of whom are appointed jointly by HM Treasury and the Secretary of State⁹
- the Chancellor appoints “at least” six members of the Prudential Regulation Committee (PRC),¹⁰ the governing committee of the PRA
- HM Treasury may also remove appointed members from the FCA body on certain specified grounds,¹¹ and the Chancellor’s consent is required for the removal of members of the PRC by the Bank¹²

⁹ FSMA, Schedule 1ZA, paragraph 2.

¹⁰ Bank of England Act 1998, section 30A.

¹¹ FSMA, Schedule 1ZA, paragraph 4.

¹² Bank of England Act 1998, schedule 6A, paragraph 9.

- HM Treasury may appoint an independent person to conduct a review of the economy, efficiency and effectiveness of the FCA's use of resources¹³
- HM Treasury may direct the PRA or FCA to carry out investigations into specific events if that is in the public interest¹⁴
- HM Treasury may direct the PRA or FCA to take action, or refrain from taking action, in relation to specified matters in order to ensure that the UK meets its international obligations¹⁵
- HM Treasury may require the FCA or PRA to comply with certain statutory provisions on the keeping of accounts and audit¹⁶

1.26 In addition, FSMA provides HM Treasury with the ability to make recommendations to the regulators through open 'recommendations letters' on issues related to matters of economic policy which the regulators should take into account when discharging certain statutory duties.¹⁷ The most recent recommendations letters for both the PRA¹⁸ and FCA¹⁹ were issued on 23 March 2021.

Rulemaking process

Approach to consulting with stakeholders

1.27 Engagement with stakeholders is embedded in the regulators' policymaking process through the application of statutory requirements and public law principles. The PRA and the FCA are subject to statutory requirements in FSMA which, in general, require them to consult with the public on rule proposals.²⁰ These PRA and the FCA consultations are generally open for three months, though this can change depending on the issue – for example, in case of emergency, consultations can be avoided or run for significantly shorter periods.

1.28 As part of these consultation requirements, the PRA and the FCA must explain why the making of the proposed rules is compatible with their objectives as set by Parliament in legislation. The regulators must also explain how the proposals are compatible with their obligation to take into account the regulatory principles. Consultations on rule proposals must include a draft of the rules, an explanation of the proposed purpose of the rules, and a cost-benefit analysis (CBA).²¹ Before making final rules, the regulators are

¹³ FSMA, section 1S.

¹⁴ Financial Services Act 2012, section 77.

¹⁵ FSMA, section 410.

¹⁶ FSMA, Schedule 1ZA, paragraph 14 (FCA), and FSMA, Schedule 1ZB, paragraph 22 (PRA).

¹⁷ Bank of England Act 1998, section 30B (PRA), and FSMA, section 1JA (FCA).

¹⁸ *Recommendations for the Prudential Regulation Committee: March 2021*, HM Treasury, March 2021.

¹⁹ *Recommendations for the Financial Conduct Authority: March 2021*, HM Treasury, March 2021.

²⁰ FSMA, sections 138I (FCA) and 138J (PRA).

²¹ There are a small number of exemptions set out in FSMA. For example, subsections of the FSMA requirement for compensation scheme rules.

required to publish, in general terms, the representations made and their response to those representations. These requirements are designed to ensure consumers, market participants, and wider stakeholders have a meaningful opportunity to scrutinise and feed into the development of regulator policy, guidance and rules. The government considers that this statutory general requirement to consult remains fit for purpose, and therefore do not propose altering the regulators' duty to publicly consult on proposals.

Stakeholder panels

- 1.29 In addition to the duty to consult publicly on proposals, the FCA has a general duty to “make and maintain effective arrangements for consulting practitioners and consumers.”²² The PRA has a similar general duty to “make and maintain effective arrangements for consulting PRA-authorized persons or, where appropriate, persons appearing to the PRA to represent the interests of such persons”, on the extent to which the PRA’s general policies and practices are consistent with its general duties.²³
- 1.30 As part of these duties, the regulators are required under FSMA to maintain stakeholder panels as part of their general duties to consult. These panels are intended to provide valuable insight, advice and challenge across the regulators’ functions, drawing on the experience and expertise of their respective memberships. Panel members are appointed by the regulators, and the chairs are approved by HM Treasury. The regulators consult the panels at an early stage in policy development to help ensure proposals are designed to meet their policy aims. The PRA and the FCA consult these panels on most major policy and regulatory interventions. The panels also set out their own strategic priorities and share more broadly their views on proposals, for example, through publishing responses to regulator consultations and through their annual reports,²⁴ which collate the key risks and issues the Panels have considered over the previous year.
- 1.31 The FCA works with five independent panels. Four of these are required in legislation²⁵ with a further non-statutory panel (the Listing Authority Advisory Panel) voluntarily maintained by the FCA.
- the FCA Practitioner Panel represents the interests of regulated firms and provides input from the industry’s view. It also works with the FCA to carry out its annual survey of stakeholder views of the FCA’s performance as a regulator

²² FSMA, section 1M.

²³ FSMA, section 2L.

²⁴ *Annual Report, 2020-2021*, FCA Practitioner Panel, August 2021.

Annual Report, 2020-2021, FCA Markets Practitioner Panel, August 2021.

Annual Report, 2020-2021, FCA Smaller Business Practitioner Panel, August 2021.

Annual Report, 2020-2021, FCA Consumer Panel, August 2021.

PRA Practitioner Panel and insurance sub-committee – Annual Report 2020/21, PRA Practitioner Panel, June 2021.

²⁵ FSMA, sections 1N-Q.

- the Smaller Business Practitioner Panel represents the interests of smaller regulated firms
- the Markets Practitioner Panel provides input from the point of view of financial market participants
- the Consumer Panel represents the interests of consumers
- the Listing Authority Advisory Panel (LAAP) advises the FCA on policy issues that affect issuers of securities, and on policy and regulation proposals from the FCA listing function

1.32 The PRA works with one statutory panel, the PRA Practitioner Panel,²⁶ which includes an insurance sub-committee that the PRA maintains voluntarily. The panel represents the interests of industry practitioners from areas of financial services activity that are subject to PRA regulation: deposit taking, insurance and large or complex investment firms. The panel considers the PRA's policies and practices and provides input to help meet the PRA's statutory and operational objectives.

1.33 The regulators have regular meetings and discussions with their panels, in which most major early policy and regulatory proposals are presented for comment. The panels' contributions to policy development as part of this process are confidential to ensure both the regulator and panel members can share ideas and feedback openly. This confidentiality allows the regulators to engage the panels when policy is in the early stages of development ahead of public consultation. This enables the panels to act as a 'critical friend' to the regulator which the government considers should continue. Where panels wish to comment on regulators' proposals publicly, they can and do publish their responses to the regulators' public consultations.²⁷ They also discuss their work across the year in general terms in the panels' annual reports, raise potential issues with regulators, and conduct their own research. They also occasionally set up sub-panels to deal with specific technical issues.

1.34 The practitioner panels tend to be composed of senior executives or similar with experience and a strategic perspective on their sectors which enables the panels to offer strategic and qualitative input on the regulators' high-level proposals. The Consumer Panel is similarly made up of experienced practitioners in the consumer sectors, such as academics, independent consultants, and consumer advocates.

1.35 The regulators are responsible for appointing members and chairs to the panels. The current appointment practices are varied and reflect the different areas of expertise of the panels. The PRA's Practitioner Panel and its insurance sub-committee seek industry nominations. The FCA seeks input from supervisory teams, and others as appropriate, for its appointments to

²⁶ FSMA, section 2M.

²⁷ For example:

Financial Services Consumer Panel response to CP 21/3 – Changes to the SCARTS: Contactless payments, FCA Consumer Panel, February 2021.

SBPP Response to CP21/11: The Stronger Nudge to Pensions Guidance, FCA Smaller Business Practitioner Panel, June 2021.

the practitioner panels. The Consumer Panel has the most involved process, with open recruitment for both the chair and individual members. HM Treasury is required to approve the appointment and dismissal of panel chairs (except for the LAAP and insurance sub-committee, as these are voluntarily maintained by the regulators, and not covered by similar requirements).

Impact of EU membership

- 1.36 In the years since FSMA was introduced, and in particular following the global financial crisis, EU financial services regulation has expanded into new areas and become significantly more detailed, which has affected the operation of the FSMA model. The development of a single market in the EU for financial services, as well as interventions to address regulatory failures of the global financial crisis, resulted in EU legislation covering many key areas of financial services regulation in significant detail. This complicated the split of responsibilities that was established by FSMA, constraining the regulators' ability to determine the most appropriate regulatory requirements for UK markets, as they were required to apply EU requirements and operate within the EU framework.

The UK's withdrawal from the EU

- 1.37 The body of EU legislation that applied directly in the UK at the point of exit was transferred onto the UK statute book by the European Union (Withdrawal) Act 2018 (EUWA). Under the "onshoring" programme, HM Treasury and the regulators undertook a significant programme of legislation to ensure that the body of retained EU law relating to financial services would operate effectively following our withdrawal from the EU, by making the necessary amendments to address any deficiencies arising as a result of exit or the end of the transition period. As part of the onshoring programme, responsibility for making some types of delegated legislation was transferred to the regulators – but the majority of financial services regulation now sits on the UK statute book. This approach provided stability and continuity in the immediate period after EU exit, but it was not designed to provide the optimal, long-term approach for UK regulation of financial services.
- 1.38 Retained EU law is defined in section 6(7) of the EUWA and includes "direct EU legislation" which applied automatically in UK law such as Regulations or Delegated Regulations, and both primary and secondary UK legislation which implemented EU legal obligations into UK law. There are also many statutory instruments made under the EUWA as part of the onshoring programme which made substantial changes to retained EU law in order to ensure that it operated effectively in the UK after exit, which this consultation includes in this category. Finally, a number of EU obligations were implemented directly into the rulebooks of the regulators. While these rulebook provisions are also retained EU law, they are out of the scope of

this review as the regulators have responsibility for their own rulebooks, which they are able to amend and update in the normal manner.

- 1.39 While retained EU law has been incorporated into the current framework, it has complicated the current FSMA model, as many of the direct regulatory provisions which apply to firms are now set out in retained EU law, rather than in the rulebooks of the regulators. Much of this retained EU law can only be amended through primary legislation, meaning that it is not possible in many areas to regulate in an agile and flexible way that reflects changing markets, as the FSMA model was designed to do.

Interactions and scope

- 1.40 The FRF Review focuses on how the UK's framework for financial services regulation needs to adapt now that the UK has left the EU. The government has therefore not considered any changes to the current structure or function of the existing complaints and compensation processes as part of this review, including the regulators' complaints scheme and the role of the Independent Complaints Commissioner, the Financial Ombudsmen Service (FOS) and the Financial Services Compensation Scheme (FSCS)
- 1.41 Anti-money laundering rules are also not within scope of the Review. This is because anti-money laundering rules, and other linked areas such as accounting and company law, apply to a much wider set of activities than those captured by FSMA, and are enforced by the FCA along with a number of other authorities, including HMRC, the National Crime Agency, and the Serious Fraud office.
- 1.42 This Review has also not considered payment market participants that are regulated domestically by the Bank of England and Payment Systems Regulator, under the Banking Act 2009 and the Financial Services (Banking Reform) Act 2013, rather than under retained EU law. HM Treasury will be consulting separately on the regulatory perimeter for systemic payments firms in the first half of next year, and will look to ensure coherence with the principles and objectives of the FRF Review with respect to non-EU retained payments legislation.

The purpose of this consultation

- 1.43 This document sets out the government's response to the feedback received in response to the previous consultation, taking into account the public and Parliamentary debate. It sets out a series of proposals for how the government intends to take forward its approach to the FRF Review, including:
- the changes needed to the regulators' statutory objectives and regulatory principles to ensure the government's priorities for the sector are fully reflected across the breadth of the regulators' responsibilities

- the proposals for ensuring that accountability, scrutiny and engagement arrangements with HM Treasury, Parliament, and stakeholders are appropriate given the regulators' responsibilities
- the proposed approach to transferring responsibility for designing and implementing the direct requirements that apply to firms in certain areas of retained EU law to the regulators within a system established by government and Parliament

1.44 The consultation sets out the government's proposed approach to these important issues, and seeks views on a number of key considerations within them.

Chapter 2

Consultation response overview

- 2.1 The previous consultation was issued on 19 October 2020 and closed on 19 February 2021. It set out an overall approach to the regulation of financial services, built on the existing FSMA model. This consultation asked for responses on 9 key questions relating to the government’s proposals for the regulatory regime. These questions requested views on: the operation of the FSMA model and on the government’s proposed blueprint for change; the function and suitability of the existing regulatory principles and statutory objectives; alternative models and international comparisons the government should consider; the government’s focus on updating accountability mechanisms; the role of Parliament in scrutinising financial services policy; how policy work between the regulators and HM Treasury should be coordinated; and, how to ensure stakeholders are sufficiently involved in the regulators’ policymaking processes.
- 2.2 The government is grateful for the 120 responses to the consultation and the constructive engagement with stakeholders during the consultation period. Respondents included financial services firms, consumer groups, independent public bodies/regulatory bodies, legal and accountancy firms, non-governmental organisations and non-profit organisations, trade associations, individual responses, and non-financial services firms. The consultation also received responses from several Parliamentarians.
- 2.3 This chapter provides a breakdown of the key themes raised by respondents in response to the questions posed in the previous consultation.

Question 1- How do you view the operation of the FSMA model over the last 20 years? Do you agree that the model works well and provides a reliable approach which can be adapted to the UK's position outside of the EU?

Question 2- What is your view of the proposed post-EU framework blueprint for adapting the FSMA model? In particular-

What are your views on the proposed division of responsibilities between Parliament, HMT and the regulators?

What is your view of the proposal for high-level policy framework legislation for government and Parliament to set the overall policy approach in key areas of regulation?

Do you have any views on how the regulators should be obliged to explain how they have regard to activity specific regulatory principles when making policy or rule proposals?

- 2.4 The government set out a proposed blueprint for the future regulatory framework which builds on the strengths of the FSMA model. A significant majority of respondents supported the government's proposal to move to a comprehensive FSMA model of regulation as it provides a good foundation that can be adapted to the UK's position outside of the EU. However, respondents noted that proposed changes set out in the initial consultation would increase the regulators' responsibilities, which meant that it would be necessary to strengthen scrutiny and accountability mechanisms.
- 2.5 Respondents supported the proposed division of responsibilities between Parliament, HM Treasury and the regulators. There was general support for a model where the government and Parliament set the overall policy approach, with the independent, expert regulators responsible for designing and implementing the direct requirements that apply to firms.

Question 3- Do you have any views on whether and how the existing general regulatory principles in FSMA should be updated?

Question 4- Do you have any views on whether the existing statutory objectives for the regulators should be changed or added to? What do you see as the benefits and risks of changing the existing objectives? How would changing the objectives compare with the proposal for new activity specific regulatory principles?

- 2.6 The government set out that the overarching statutory objectives for the PRA and the FCA set in FSMA are an effective way of ensuring appropriately strong regulatory focus on the policy priorities of financial stability, consumer protection, the integrity of financial markets and competition. The

government also set out that prioritising these policy aims remain vital to ensure a stable and fair financial system. Respondents noted that the regulators' existing objectives have been broadly effective, with the general view that the objectives of financial stability and consumer protection are vital in maintaining the integrity and strength of the UK's financial services sector.

- 2.7 The government set out the ongoing debate amongst stakeholders and Parliament on whether there should be an objective to support the competitiveness of the UK sector. Many respondents shared their views on having a greater focus on competitiveness within the regulatory framework. Those in favour of a competitiveness objective or principle argued that a greater focus on competitiveness as part of the regulatory framework was necessary to support the ability of the UK financial services sector to compete internationally and continue to contribute to the UK's economic prosperity. Some responses, including from groups representing consumers, suggested that a competitiveness objective could distract from or dilute the regulators' pursuit of their existing objectives. A limited number of respondents argued for objectives or principles relating to innovation or economic growth to improve the ability of the UK market to compete internationally.
- 2.8 Several respondents noted the specific need for a new regulatory objective or principle relating to green or climate change issues. This was articulated in a number of different ways, including requirements to ensure the finance sector aligns with the Paris Agreement, supports wider climate change goals, and contributes to the green finance strategy. This issue was also raised in debates in Parliament during the passage of the Financial Services Act 2021, where the government added the 2050 Net Zero target to the list of 'have regards' in the prudential measures relating to Basel and the Investment Firms Prudential Regime.
- 2.9 A small number of respondents indicated support for amending and strengthening the regulators' existing proportionality principle to reduce regulatory burdens on firms. Some respondent supported inserting new principles relating to financial inclusion and duty of care to increase the regulators' focus on harm to consumers.

Question 5- Do you think there are alternative models that the government should consider? Are there international examples of alternative models that should be examined?

- 2.10 The government set out that the FRF Review will see the regulators take on increased responsibility for direct regulatory requirements which apply to firms. This approach is supported by the academic literature on financial regulation and by the International Monetary Fund (IMF) and the Organisation for Economic Co-operation and Development (OECD). Respondents agreed with the government's view that the UK's FSMA model is world-leading and that no alternative model provided a preferable approach to financial services regulation. However, respondents who argued for a greater focus on competitiveness noted that some other jurisdictions that use a similar model require their regulators to promote the

competitiveness of their markets internationally, in addition to their core regulatory functions of ensuring financial stability and consumer protection. Some respondents also discussed the role of the EU's Committee on Economic and Monetary Affairs (ECON) in providing scrutiny of regulator rules. However other respondents considered that a similar model in the UK would harm the regulators' dynamism and agility.

Question 6- Do you think the focus for review and adaptation of key accountability, scrutiny and public engagement mechanisms for the regulators, as set out in the consultation, is the right one? Are there other issues that should be reviewed?

- 2.11 The government set out the existing arrangements for accountability, scrutiny and public engagement and identified areas where these arrangements might be adapted. There was broad support for HM Treasury's proposed focus on the split of responsibilities between Parliament, the government and the financial services regulators. Some respondents argued for more scrutiny and accountability of the regulators' supervision and a mechanism to challenge supervisory decisions.
- 2.12 A number of respondents noted that the FRF Review could also consider the role of bodies which were not mentioned in the previous consultation, such as the Financial Ombudsman Service (FOS) and the Financial Services Compensation Scheme (FSCS). These respondents noted that the increasingly important role of non-regulatory bodies like the FOS and the FSCS in the financial services regulatory eco-system means they should fall within the scope of the FRF Review. These responses also raised concerns about whether the powers, resourcing, transparency, and accountability of these bodies remain appropriate. Some respondents argued that that these bodies should be included in regulatory co-operation initiatives, given the importance of their roles.

Question 7- How do you think the role of Parliament in scrutinising financial services policy and regulation might be adapted?

- 2.13 The government set out that Parliament should play an important strategic role in interrogating, debating, and testing the overall direction of policy for financial services. Respondents overwhelmingly agreed that the role of Parliament is vital for the effective scrutiny of the regulators. There was broad support for Parliament's existing mechanisms for holding the regulators and HM Treasury to account. Respondents felt that the current approach to scrutiny via select committees is appropriate and effective. Respondents noted that the Treasury Select Committee (TSC) is well-established, well-regarded, and that its scrutiny of the regulators through its reviews and inquiries has been effective. However, some respondents suggested new or altered committee structures citing concerns that the TSC may find it challenging to scrutinise an increased volume of the regulator proposals in depth due to the TSC's broad remit. Suggestions from

respondents included the formation of a new sub-committee of the TSC, a new Joint Committee of both Houses, or a new Parliamentary Select Committee dedicated to Financial Services. Respondents also noted that one of the strengths of the select committee model is its more strategic role in scrutiny. Respondents felt that it would not be appropriate or feasible for Parliament to seek to adopt an ECON style model of line-by-line scrutiny of regulator proposals.

Question 8- What are your views on how the policy work of HM Treasury and the regulators should be coordinated, particularly in the early stages of policymaking?

2.14 The government set out that as part of their general responsibility for the effective operation of the UK's regulatory framework, it is important that HM Treasury ministers are able to assess the implications of regulator proposals for broader government economic and social policy priorities. A majority of the respondents were in favour of the regulators formally consulting HM Treasury on rule changes provided the appropriate governance arrangements were put in place. However, respondents also noted the challenges in achieving the right balance between maintaining the regulators' independence and ensuring appropriate democratic input and coordination. The importance of transparency in the relationship between HM Treasury and the regulators was also noted by respondents who recommended requiring the publication of the regulators' responses to HM Treasury recommendations.

Question 9- Do you think there are ways of further improving the regulators' policy-making processes, and in particular, ensuring that stakeholders are sufficiently involved in those processes?

2.15 The government set out that HM Treasury and the regulators are required to engage with interested stakeholders as part of the policymaking process and are obliged to carefully consider the views of stakeholders before finalising legislative or regulatory proposals. Respondents noted that the regulators already conduct extensive stakeholder engagement and research on their proposed policies, and that the consultation requirement works well. They also noted that the regulators engage in existing good practice that goes beyond their statutory consultation requirement, and there was wide appreciation of their approach to early and open engagement with industry through discussion papers and calls for input. Suggestions for improvements included strengthening and enhancing these practices and their statutory underpinning, rather than an overhaul of the consultation process.

2.16 Respondents showed support for greater transparency in the operation of the regulators' statutory panels, with the regulators doing more to explain how they have taken panel views into account. Earlier involvement for panels in the consultation process was also recommended by some respondents. Respondents suggested more specialised representation in the membership of the panels including industry specialists or consumer groups where

appropriate. Some respondents argued that the panels should provide more technical comment as part of this specialisation. Respondents noted that changes to the appointment process for panel members is a potential route to increased accountability and suggestions included more use of industry nominations for panels and strengthening the relationship between panels and HM Treasury.

- 2.17 The government welcomed views on whether the regulators' cost-benefit analysis (CBA) obligations or practices could be improved. This included how they could better achieve a reliable assessment of the likely impact on affected stakeholders and contribute to high-quality, evidence-based policy. However, it was also acknowledged that changes to CBA should not overburden the financial services sector with information requests. Respondents acknowledged the value of the regulators conducting CBA as part of their policymaking process. However, there were also a significant number of suggestions for how CBA can be made more rigorous, including when and how CBA should be conducted, reviewed, and by whom. Several respondents recommended the creation of an external review function for CBA or that CBA should be submitted to existing bodies such as the Regulatory Policy or Better Regulation Committees. There were also calls for the requirement to conduct CBA to be extended to all interventions, including guidance, which was cited as often having a supervisory effect.
- 2.18 A common theme was that CBA should take a wider range of factors into account. This included suggestions on including non-economic/non-financial impacts, the impact of rules on competitiveness, and increasing the focus on the long-term impact of rules. Some respondents argued that the cumulative impact of regulations (including otherwise low-impact regulations) on firms and/or sectors should be part of CBA, rather than just the impact of the individual measure. There were also calls for clearer articulation of uncertainty in estimates. Some respondents suggested that CBA should include fuller analysis of alternative options, and not just the difference between the proposal and doing nothing. Some industry respondents expressed concerns that regulators' CBA is overly focussed on the expected benefits of intervention and underplays the costs to individual firms and the wider market. For example, the impact of consequential behaviour changes by consumers was felt to be underappreciated by the regulators when assessing the benefits of policies. Some consumer groups, on the other hand, felt that CBA was overly concerned with the cost to firms, and disregarded benefits to consumers from intervention or the impact of intervention (and non-intervention) on groups such as vulnerable consumers.
- 2.19 Industry respondents also made a number of proposals around independent scrutiny of the regulators. These proposals included the establishment of an external body to conduct reviews into regulator rules, and a new external appeals mechanism allowing firms to challenge regulator decisions. This latter mechanism was proposed as potentially being a less expensive and resource intensive alternative to Judicial Review for firms to challenge regulatory decision making. Respondents noted the value of regular rule reviews and made a number of suggestions for how to increase their frequency, including more systematic reviews conducted by the regulators of entire regimes or sectors, enabling HM Treasury to appoint independent

reviewers to conduct reviews into rules, and the introduction of timeframes for when rule reviews should be conducted.

- 2.20 Further discussion of consultation responses on specific aspects of the regulatory framework is included in subsequent chapters where relevant.

Chapter 3

Objectives and principles

- 3.1 This chapter outlines the government’s approach to updating the regulators’ objectives and principles. It sets out the priority the government gives to maintaining the safety and soundness of the UK’s financial sector, considers the balance between long-term economic growth, international competitiveness and the regulators’ current objectives. It then sets out the government’s intention to provide for a greater focus on growth and international competitiveness through the introduction of new secondary objectives for the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA).
- 3.2 It also sets out the proposals for updating the regulatory principles, including by revising the existing sustainable growth principle to incorporate climate targets.

The Statutory Objectives and Principles

- 3.3 As the government considers the UK’s new position outside the EU, it is appropriate to evaluate the regulators’ objectives and principles and assess whether they continue to set the right strategic considerations for the regulators. In the previous consultation, the government invited views on whether the regulators’ objectives should be changed or added to, and whether their principles should be updated.
- 3.4 The government considers that the FCA’s current strategic objective to ensure that relevant markets function well is the right strategic focus, and that its operational objectives are an effective way of protecting the integrity of the UK’s financial services market, safeguarding consumer protection, and promoting effective and healthy competition in consumers’ interests. The FCA also has an important role to play in combating financial crime. The PRA’s present statutory objective of promoting safety and soundness among PRA-authorized persons is vital to the ongoing stability of the financial services sector. Its objective to contribute to securing an appropriate degree of protection for those who are or may become insurance policy holders, and its secondary objective to promote effective competition, are important priorities for the government. The policy aims encapsulated by the current regulatory objectives are vital to ensuring a stable and fair financial system in which the UK public and international stakeholders can have confidence. Responses to the previous consultation demonstrated that the majority of stakeholders recognise the importance of these objectives to the UK’s financial services sector.

- 3.5 As set out in the strategy document published alongside the Chancellor’s Mansion House speech in July 2021, *A new chapter for financial services*,¹ the UK will continue to remain a global leader in promoting high international standards. Alongside this commitment, the government stated its intention to ensure that the financial services sector is delivering for businesses and consumers across the UK. The government considers that the regulators’ current objectives are each important in helping to deliver these outcomes. Robust regulatory standards encouraged by these objectives are the cornerstone of the UK market’s attractiveness, and the stability and soundness of the UK’s market remains an important priority for the government.
- 3.6 Similarly, the government considers that the 8 existing regulatory principles broadly capture the key considerations the regulators should take into account when carrying out their general functions. There was little support from respondents to the consultation to remove any of the existing regulatory principles. The government agrees that there is no need to remove any of them from the regulatory framework.
- 3.7 However, there are some additional policy areas that consultation respondents suggested should be included in the regulators’ objectives and principles.

Long-term economic growth and international competitiveness

- 3.8 The government recognises that the financial services sector is not just an industry in its own right but an engine of growth for the wider economy. The Mansion House document, *A new chapter for financial services*,² set out the government’s vision for a sector that is globally competitive and acts in the interests of communities and citizens, creating jobs, supporting businesses, and powering growth across the UK.
- 3.9 In recent years, including during the passage of the Financial Services Act 2021 (FS Act 2021), there has been significant debate in Parliament and among industry stakeholders about whether the regulators should have a specific objective to require them to advance the growth of the UK economy and the competitiveness of the UK financial sector. This debate was also reflected in Lord Hill’s report on the UK Listings Regime, published in March 2021, which recommended that the government consider the case for amending the FCA’s statutory objectives to include a ‘competitiveness’ or ‘growth’ requirement.³
- 3.10 Many stakeholders responding to the previous consultation argued that, given the importance of a thriving financial services sector for UK economic growth and prosperity, the regulators should have a statutory duty to support the economic viability of financial services and the ability of the sector to compete internationally. By contrast, respondents opposed to the

¹ *A new chapter for financial services*, HM Treasury, July 2021.

² *A new chapter for financial services*, HM Treasury, July 2021.

³ *UK Listing Review*, Lord Hill, March 2021.

proposition argued that a new objective could distract from or dilute the regulators' existing objectives. As explained above, the government continues to agree that the current objectives set broadly the right strategic considerations, and has carefully considered the many representations it has received on this issue, as well as the ongoing public debate.

- 3.11 Supporters of action on growth and competitiveness noted that comparable jurisdictions have various mechanisms that seek to balance regulator objectives for financial stability and consumer protection with objectives related to growth or competitiveness. As noted by Lord Hill,⁴ other financial services regulators – for example in Australia, Singapore, Hong Kong, and Japan – have growth or competitiveness embedded in their frameworks. Although these regulators have different structures and powers, the focus on growth or competitiveness tends to function either as a specific objective, or as a balance to stability objectives. In addition, Switzerland's independent financial markets regulator (FINMA) has its contribution to sustaining the reputation and competitiveness of the Swiss financial marketplace set out in statute. The government's view is that the successes of these jurisdictions demonstrate the feasibility of embedding competitiveness and growth considerations within a regulatory framework without harming financial stability.
- 3.12 As the government considers the UK's new circumstances outside the EU, it is appropriate to evaluate the effectiveness of the regulators' existing objectives in contributing to the UK's long-term economic growth and international competitiveness. For example, the EU's approach to financial services regulation was not constrained by any particular objectives. This meant that it was possible to consider the competitiveness of the EU as a financial centre during the legislative process. When the European Commission brought forward legislative proposals, and when these were considered by the European Council and European Parliament, each could weigh the impact of new regulation on the growth and competitiveness of the EU, and balance that against the other aims of the legislation.⁵
- 3.13 As the regulators take on responsibility for setting detailed rules in areas currently covered by retained EU law, the government considers that it is right that the regulators' objectives reflect the need to support the long-term growth and international competitiveness of the UK economy, including the financial services sector. This can be done in a way that does not detract from the regulators' existing objectives of ensuring that UK firms remain safe and sound, that the UK's markets function well, and that consumers and users of financial services receive an appropriate degree of protection.
- 3.14 Some consultation respondents advocated for a new objective that would require the regulators to make direct trade-offs between growth and competitiveness on the one hand, and the PRA's existing primary objective and the FCA's existing strategic and operational objectives on the other. The

⁴ *UK Listing Review*, Lord Hill, March 2021

⁵ For example, Article 89 of the Fourth Capital Requirements Directive (2013/36/EU) required the Commission to conduct "a general assessment as regards potential negative economic consequences of [the public disclosure requirements in CRD IV] including the impact on competitiveness..." and, if the report identifies significant negative effects, to consider a legislative proposal to amend the disclosure requirements.

government has considered such proposals carefully, but has concluded that there are potential disadvantages to such an approach. For example, if it inhibited the ability of the regulators to make effective prudential regulation, this could potentially reduce the UK's financial stability and the ability of the regulators to conform to international standards, which is incompatible with the government's commitment to global leadership. Furthermore, significantly compromising the standards that underpin our regime and the UK's international reputation could have the effect of undermining the UK's competitiveness by reducing confidence in the safety and stability of the UK's market, or the level of protection for consumers and other market users – meaning that such an approach would not achieve the intended outcome.

- 3.15 Other respondents suggested that an alternative method for increasing the regulators' focus on competitiveness would be the introduction of a new regulatory principle focused on competitiveness. However, the regulators are not required to act to advance their regulatory principles; instead they must take them into account when pursuing their statutory objectives. While a regulatory principle would likely have some effect in increasing the regulators' focus on competitiveness, the government considers that it would not provide the regulators with the appropriate statutory basis required to act to support competitiveness in line with the government's vision for the sector.

Measure 1: New growth and international competitiveness objectives

- 3.16 The government intends to provide for a greater focus on growth and international competitiveness through the introduction of new secondary objectives for the PRA and the FCA.
- 3.17 In crafting the new objectives, the government has taken into consideration the wide range of views expressed in the responses to the consultation. Respecting the need for the regulators to maintain high regulatory standards in the UK and align with international standards, the government will make provision for the regulators to facilitate the long-term growth of the UK economy, including through the lens of international competitiveness.
- 3.18 For the PRA, the government intends to introduce the new growth and international competitiveness objective as a secondary objective to sit alongside the PRA's existing secondary objective to facilitate effective competition in the markets for services provided by PRA-authorised persons. This will mean that, as the PRA advances its general objective to promote the safety and soundness of PRA-authorised persons and its insurance specific objective on policyholder protection, the PRA will be required to act in a way that, subject to aligning with international standards and so far as is reasonably possible, facilitates the long-term growth and international competitiveness of the UK economy, including the financial services sector. As with the PRA's competition objective, this would not require or authorise the PRA to take any action inconsistent with its primary objectives.

- 3.19 For the FCA, the government similarly intends to introduce the new growth and international competitiveness objective as a secondary objective. This will mean that the new objective will complement the FCA's three existing operational objectives of consumer protection, market integrity and competition, all of which sit underneath the FCA's single strategic objective to ensure that relevant markets function well. As will be the case for the PRA, as the FCA advances its operational objectives, the FCA will be required to act in a way that, subject to aligning with international standards and so far as is reasonably possible, facilitates the long-term growth and international competitiveness of the UK economy, including the financial services sector. In line with the way the PRA's competition objective works at present, this would not require or authorise the FCA to take any action inconsistent with its strategic or operational objectives. This new objective would also not change the FCA's competition duty which requires it to promote effective competition in the interests of consumers so far as is compatible with meeting its objectives to protect consumers and enhance market integrity.
- 3.20 The government will also require both regulators to report on their performance against their growth and competitiveness objective on an annual basis.

Question 1: Do you agree with the government's approach to add new growth and international competitiveness secondary objectives for the PRA and the FCA?

Alternative proposals

- 3.21 In response to the previous consultation, the government received a number of alternative proposals. For example, consultation respondents suggested that a strengthened regulatory principle on proportionality would encourage the removal of unnecessary burdens on industry. The government considers that proportionality is already sufficiently embedded in the regulators' statutory principles, requiring the regulators to ensure that any burden or restriction is proportionate to the expected benefits, taking into account costs to firms and consumers. As part of the regulators' accountability mechanisms, including their annual reports, regulators are required to set out how they have considered their principles. The government is therefore not persuaded that this principle should be amended.
- 3.22 Consultation respondents also highlighted that increased innovation may be a benefit of proposed new objectives or regulatory principles focused on proportionality, economic growth, or competitiveness. Some respondents argued for a standalone regulatory principle to increase innovation in the financial services system. The regulators' current set of objectives (particularly those in relation to competition) have allowed the FCA to establish Project Innovate, resulting in the creation of an Innovation Hub and the Regulatory Sandbox, both of which are now held up as examples of global best practice in increasing innovation in financial services and other sectors. The government is therefore not persuaded by the need for an additional regulatory principle focused on innovation alone, and is confident that the balance of objectives and regulatory principles allows the regulators to act to

encourage innovation. The government also asked the regulators to consider the desire ‘to see innovation in the financial services sector’ in the most recent recommendations letters published in March 2021.

- 3.23 A number of respondents argued for one or both of a financial inclusion objective or principle for regulators, and a duty of care for regulated firms. The government’s view is that the FCA’s current and ongoing initiatives in the financial inclusion space, including those relating to access to cash and vulnerable consumers, demonstrates that it can already effectively support the government’s leadership on this agenda through the present operational objectives and regulatory principles. The government has already legislated to require the FCA to consult on the introduction of a duty of care owed by firms to consumers through the FS Act 2021. This was in response to calls from Parliamentarians to introduce such a duty in order to reduce levels of harm in the financial services sector. The FCA has since consulted on the introduction of a new ‘Consumer Duty’, which seeks to set higher and clearer expectations for the standard of care firms should provide to consumers. The FCA intends to publish a further consultation by 31 December 2021 and is required to make any new rules it considers appropriate by August 2022.

Climate change

- 3.24 The government is committed to tackling climate change and has made a series of commitments to advance environmental and climate goals. In 2019, the UK became the first major economy to write into law its commitment to reach net zero greenhouse gas emissions by 2050. In 2021 the government went further, setting out the world’s most ambitious climate change target to cut emissions by 78% by 2035. The financial services sector needs to support these challenging targets if they are to be met. Action has already been announced through the policy frameworks outlined in the Prime Minister’s Ten Point Plan for a Green Industrial Revolution⁶ and the Chancellor’s Mansion House speech.⁷
- 3.25 The UK’s approach to embedding climate considerations within the actions of its financial services regulators is already world leading. The recommendations letters, which allow the government to make recommendations to the regulators on matters of economic policy, were updated in 2021 with new economic policy objectives including the ‘transition to an environmentally sustainable and resilient net zero economy’ and set out specific aspects of this policy that they should take into account; this included climate change for the first time. Alongside this change, the FS Act 2021 requires the PRA and the FCA, from 1 January 2022, to ‘have regard’ to the 2050 Net Zero target when making rules to implement the latest Basel standards, and making rules as part of the Investment Firms Prudential Regime. Throughout the passage of this Act, the government was clear that the FRF Review presents an opportunity to consider action beyond

⁶ *The ten point plan for a green industrial revolution*, HM Government, November 2020.

⁷ *Mansion House Speech 2021 – Rishi Sunak*, HM Treasury, July 2021.

these changes. As set out in Chapter 2, several respondents to the consultation noted the specific need for a new regulatory objective or principle relating to green or climate change issues.

Measure 2: Incorporation of climate change into the regulatory principles

3.26 The government considers there to be an opportunity to further strengthen the UK's regulatory regime relating to climate. Embedding climate change into the regulatory principles would demonstrate the government's long-term commitment to transform the economy. The PRA and the FCA are already subject to a regulatory principle which requires them to take into account the desirability of sustainable growth in the economy in the UK in the medium or long term. Alongside the new secondary objective to facilitate growth and international competitiveness, the government therefore proposes to amend the existing regulatory principles to be clear that such growth should occur in a sustainable way that is consistent with the government's commitment to achieve a net zero economy by 2050 to meet the obligation set out in section 1 of the Climate Change Act 2008.

Question 2: Do you agree that the regulatory principle for sustainable growth should be updated to reference climate change and a net zero economy?

Chapter 4

Relationship with HM Treasury

- 4.1 This chapter provides an overview of the government’s proposed approach to strengthening the existing mechanisms underpinning the regulators’ relationship with HM Treasury. It sets out an overview of the responses provided to the previous consultation and outlines the considerations the government considers key in proposing changes to accountability. The chapter then sets out the government’s proposals in this area.
- 4.2 As the authorities responsible for UK financial services regulation, the relationship between HM Treasury and the regulators involves wide-ranging collaboration and coordination. Effective coordination between regulatory bodies is vital for the smooth and successful operation of our regulatory regime. The first stage of the Future Regulatory Framework (FRF) Review in 2019 examined coordination between the UK authorities that have responsibility for the regulation of the financial services sector. This resulted in the creation of the Financial Services Regulatory Initiatives Grid and Forum. This provides a clear picture of expected regulatory activity to help regulators, firms and consumer stakeholders plan ahead and improve proportionality, co-ordination and transparency across the regulatory landscape for financial services, reducing the operational burden on industry.
- 4.3 The government considers that the greater responsibility being given to the regulators, following the UK’s departure from the EU and the implementation of the FRF Review, should be balanced with effective policy input and appropriate accountability to government. This view is supported by responses to the previous consultation.
- 4.4 In the previous consultation, the government suggested some initial proposals and principles for providing this balance. Responses to these suggestions were largely positive, though respondents noted the importance of ensuring that new accountability mechanisms do not undermine the regulators’ independence, a point reiterated by the Treasury Select Committee (TSC) in their 6 July 2021 report into *The Future Framework for Regulation of Financial Services*.¹ Many respondents also touched on the importance of greater transparency under the new arrangements.
- 4.5 The existing mechanisms governing the regulators’ relationship with HM Treasury, both formal and informal, have been outlined earlier (see Chapter 1), and the government considers that they are largely effective. However, the government considers that it would be appropriate to bring forward a number of targeted proposals which build on these existing mechanisms.

¹ *The Future Framework for Regulation of Financial Services*, Treasury Select Committee, July 2021.

Importantly, while the regulators' expanded responsibilities require strengthened engagement and relationship mechanisms, the government agrees that it is vital not to compromise the regulators' independence, and these measures should not constitute a veto or power of direction for HM Treasury over policy which is properly a matter for our independent regulators.

- 4.6 The government considers that the specific area of regulators' responsibilities where the relationship with HM Treasury requires strengthening is rulemaking. While it is important to maintain the regulators' independence and respect their expertise, the government has a justifiable interest in the policymaking that informs the regulators' rules. The regulators' other functions, including enforcement and supervision, are not areas in which increased accountability to HM Treasury would be useful or desirable.
- 4.7 With the above considerations in mind, and taking into account the views of consultation respondents, the government proposes the following measures to strengthen the regulators' relationship with HM Treasury.

HM Treasury recommendations

- 4.8 As noted earlier, the Financial Services and Markets Act (FSMA) 2000 and the Bank of England Act 1998 provide that HM Treasury may at any time make recommendations to the Prudential Regulation Committee (PRC), the governing committee of the Prudential Regulation Authority (PRA), and the Financial Conduct Authority (FCA) on issues related to matters of economic policy through recommendations letters (also known as remit letters).² These recommendations to the PRA and the FCA must be made at least once a Parliament, and must be published by HM Treasury and a copy laid before Parliament. The recommendations letters serve the valuable purpose of providing an opportunity for government to make recommendations related to particularly topical issues or aspects of the government's economic policy.
- 4.9 HM Treasury may at any time make similar recommendations to the Bank of England's Financial Policy Committee (FPC),³ though the scope of these recommendations is wider, going beyond matters the FPC should 'have regard' to while exercising its functions.⁴ The FPC must respond to the recommendations, explaining how they have taken action, intend to take action, or reasoning for not intending to act in accordance with HM Treasury's recommendations.⁵

² FSMA, section 1JA (FCA) and Bank of England Act 1998, section 30B.

³ Bank of England Act 1998, section 9E.

⁴ For example, HM Treasury may make recommendations to the FPC recommendations about "the responsibility of the [Financial Policy] Committee in relation to support for the economic policy of Her Majesty's Government, including its objectives for growth and employment." For the PRC and FCA, HM Treasury may only make recommendations about what the regulator should 'have regard' to.

⁵ Bank of England Act 1998, section 9E, subsection 3.

Measure 3: Requirement for regulators to respond to HM Treasury recommendations letters

- 4.10 In the previous consultation, the government suggested that increasing the frequency of recommendations letters was an option for strengthening the regulators' accountability to HM Treasury.
- 4.11 As noted above, the current requirement sets out that HM Treasury must make recommendations 'at least' once per Parliament. This means that the government already has the option to make additional recommendations, where necessary, to reflect changing government priorities.
- 4.12 Consultation respondents raised some concerns over the proposal to mandate an increased frequency for recommendations letters. This was on the basis that increasing the frequency to more than once per Parliament (for example, annually or even biannually) runs the risk of creating uncertainty for the regulators – and industry and consumers – through regularly changing the public policy matters that need to be considered by the PRC and the FCA.
- 4.13 The government therefore considers that the current requirement to make recommendations to the PRC and FCA at least once in each Parliament remains appropriate, given that the government has the option to make them more regularly if doing so is necessary to reflect changing government priorities.
- 4.14 However, the government has considered the fact that there is currently no requirement for the PRC and the FCA to respond to the government's recommendations. Some consultation respondents suggested that the regulators could be required to publish a response. Imposing this requirement to respond would increase HM Treasury and wider stakeholders' ability to see how the regulators have taken into account the recommendations.
- 4.15 The government therefore intends to introduce a new statutory requirement for the PRC and the FCA to respond to HM Treasury recommendations, bringing them into line with the FPC. As the regulators take on more policy responsibility following the UK's exit from the EU, this will increase transparency around how the regulators take into account these recommendations, and increase their effectiveness as a mechanism for setting out which aspects of the government's economic policy the regulators should take into account when exercising their functions.
- 4.16 The government intends that the obligations on the PRC and the FCA should broadly align with those which apply to the FPC, while recognising the different nature of FPC letters (as noted earlier in this section). Within the response, the regulators should provide an overview of:
- how they have taken account of each recommendation in the letter
 - any impact on policy that has resulted from recommendations
- 4.17 In line with the requirement for HM Treasury to publish FPC responses and lay them before Parliament, the government intends that HM Treasury

should be required to publish the PRC and the FCA responses and lay them before Parliament.

- 4.18 The government intends to require that the PRA and the FCA provide a response on an annual basis, covering their activity in the previous year.

Measure 4: Power for HM Treasury to require the regulator to conduct a rule review

- 4.19 At present, how and when the regulators review their rules to assess whether they function as intended is largely at the discretion of the regulators. There is no formal mechanism for HM Treasury, or anyone else, to require the regulators to conduct reviews of their existing rules. As the regulators take on increased policymaking responsibilities following the implementation of the FRF Review, there may be areas where the government considers it is in the public interest for the regulators to review their rules to assess whether they are appropriate.
- 4.20 Respondents to the previous consultation raised concerns regarding the current avenues for ongoing challenge of regulator rules. In particular, some respondents noted that judicial review is not frequently used by firms and that there were few other avenues to challenge regulator rules. Some respondents suggested that a new external review body should be set up to review regulators' rules, while others argued for the creation of a new external appeals mechanism allowing firms to challenge regulatory decision making. There was a further suggestion that a designated group of industry bodies could be given a power to trigger rule reviews.
- 4.21 The government has considered the consultation responses carefully and sought to strike the appropriate balance between the regulators' independence and ensuring that there is appropriate ongoing scrutiny of regulators' rules.
- 4.22 The government therefore intends to introduce a new power for HM Treasury to be able to require the regulators to review their rules where the government considers that it is in the public interest. This would allow, where appropriate, for an independent person to be appointed to conduct the review.
- 4.23 The government expects the proposed power would only be used in exceptional circumstances. For example, where there has been a significant change in market conditions, or other evidence suggests that the relevant rules are no longer acting as intended.
- 4.24 The government expects that, alongside such a power, provisions would be made setting out how it would be operationalised. These may include:
- HM Treasury powers of direction on scope, conduct, timing, and making of reports
 - a requirement for the regulator to report the outcome of the review to HM Treasury

- a requirement for HM Treasury to lay directions and reports before Parliament and publish them, unless this would be considered not in the public interest
- a requirement for the regulators to each maintain a statement of policy on how they will conduct reviews under the power

4.25 The government considers that this proposal offers a new avenue for challenge of the regulators' rulemaking, while still maintaining the operational independence of the regulators as set out in FSMA and relevant provisions in other financial services legislation.

Question 3: Do you agree that the proposed power for HM Treasury to require the regulators to review their rules offers an appropriate mechanism to review rules when necessary?

Overseas deference arrangements and trade agreements

Deference arrangements

- 4.26 While a member of the EU, the UK was subject to the equivalence decisions made at an EU level, rather than independently setting its own policy. Therefore, the current FSMA framework does not require the regulators to consider the impact of their activities on HM Treasury's deference arrangements, including equivalence, as these impacts did not arise during membership of the EU.⁶
- 4.27 The government currently has extensive deference arrangements with overseas jurisdictions (which include incorporating nearly all of the existing EU equivalence determinations for overseas jurisdictions at the end of the transition period into UK law), as well as deference afforded to the UK by overseas jurisdictions. In utilising its new deference tools, the government also intends to enter into Mutual Recognition Agreements with our overseas partners
- 4.28 In his speech at Mansion House, the Chancellor outlined his vision for using the UK's strengths as a global financial hub to establish and enhance strong relationships with jurisdictions all around the world, attracting investment and increasing opportunities for cross-border trade and supporting openness through consistently high standards. The vision also emphasised using HM Treasury's deference mechanisms, including equivalence decisions and Mutual Recognition Agreements, to deliver the government's ambition.
- 4.29 The government recognises that different combinations of rules and supervisory practices can achieve equivalent outcomes to the corresponding UK framework. Therefore, assessments of other jurisdictions for the purposes of deference focus on whether they achieve an equivalent outcome to the relevant UK regime. The UK's approach to deference is therefore flexible

⁶ Regulatory deference, including the issuing of equivalence decisions, is a process endorsed by the G20 where jurisdictions and regulators defer to each other when it is justified by the quality of their respective regulatory, supervisory and enforcement regimes.

enough to allow for both jurisdictions to change and adapt their rules, with the UK still being able to maintain deference arrangements with the overseas jurisdiction. The financial services sector is not static, and regulatory regimes will necessarily evolve over time. As rules evolve this could create material deviations with regard to the corresponding rules used by international partners with whom the UK has deference arrangements.

Trade agreements

- 4.30 In addition to using HM Treasury's deference mechanisms to establish and enhance strong relationships specifically on financial services, the government is also pursuing an ambitious free trade agenda, setting a new global standard for financial services in trade agreements. These agreements, covering free trade agreements, bilateral investment treaties and the WTO agreements, will create obligations on UK authorities that will need to be considered when setting rules that apply to firms.
- 4.31 The FRF Review will significantly increase the regulators' responsibilities, including in areas where the UK may have taken obligations under trade agreements with overseas jurisdictions. Actions taken by regulators in these areas, including by amending their rules, could be challenged under the dispute settlement mechanisms of a free trade agreement if they breach these obligations. To help mitigate this risk, it is appropriate to ensure that the regulators' accountability framework appropriately covers the trade obligations that the UK is subject to.

Measure 5: New overseas deference arrangements and trade agreements accountability mechanisms

- 4.32 Under the FSMA model, and following the implementation of the FRF Review, the regulators will generally have responsibility for setting the rules that apply to firms. The government considers that there is now a case for ensuring that the regulators consider the potential impacts on deference arrangements and assess compliance with relevant trade agreements as a matter of course when making rules and when setting general approaches on supervision, where relevant and proportionate. The government therefore proposes introducing new accountability mechanisms requiring the regulators to consider the impact of exercising their powers to make rules and set general approaches on supervision, and to assess compliance with relevant trade agreements with overseas jurisdictions.
- 4.33 This would consider the possible impact on relevant deference arrangements afforded to the UK by overseas jurisdictions, where proportionate and relevant, as well as where the UK has provided deference to overseas jurisdictions (including equivalence decisions and Mutual Recognition Agreements). When making rules and when setting general approaches on supervision where appropriate and proportionate, the government proposes that the regulators would be required to consult HM Treasury on the general anticipated impact on these areas, providing the opportunity for further

dialogue to assist the government with the management of the UK's deference arrangements. For trade agreements, this would require the regulators to assess, where proportionate and relevant, whether the exercise of their powers to set rules and general approaches on supervision is in compliance with the UK's obligations under our trade agreements.

Question 4: Do you agree with the proposed approach to resolve the interaction between the regulators' responsibilities under FSMA and the government's overseas arrangements and agreements?

Alternative proposals

- 4.34** As noted previously, in the years since FSMA was introduced, and in particular following the global financial crisis and the growth of the Single Market in the EU, EU financial services regulation has expanded into new areas and become significantly more detailed. EU legislation was proposed by the European Commission and negotiated with Member State governments and the European Parliament. HM Treasury, which led the UK's negotiations on EU financial services legislation, therefore took on responsibility for key areas of regulatory policy. While the UK regulators supported HM Treasury on the technical detail, the government was directly responsible for negotiating areas of detailed regulatory requirements that would otherwise have sat with UK regulators under the FSMA model. This allowed ministers to reflect wider public policy considerations in our approach to negotiations; for example, ensuring proposals on the regulation of mortgages didn't adversely affect the ability for borrowers to attain home ownership in the UK.
- 4.35** As the regulators take on additional responsibility for determining the direct regulatory requirements that apply to firms in these areas, the scrutiny and input provided by the EU level of policymaking – including that provided by HM Treasury as part of it – will no longer be in place. The government is of the view that it is appropriate for the detailed rules to be determined by the independent, expert regulators, and so is not proposing to replicate the EU process.
- 4.36** In the previous consultation, the government suggested some form of general arrangement whereby the regulators would consult HM Treasury more systematically on proposed rule changes at an early stage in the policymaking process and before proposals were published for public consultation.
- 4.37** Given the detailed measures proposed in this consultation, the government is continuing to consider whether any further arrangements for how the regulators may be required to consult HM Treasury are necessary.

Chapter 5

Accountability to Parliament

- 5.1 This chapter sets out the role of Parliament in the scrutiny of the regulators under the UK's regulatory framework and the government's proposals to strengthen the existing mechanisms which Parliament uses to hold the regulators to account and scrutinise their work.
- 5.2 It sets out proposals for clearer requirements on when and how information should be provided to Parliament. These measures have been designed to support more effective accountability to, and scrutiny, of the regulators by Parliament.

Current arrangements and proposed approach

- 5.3 As set out in Chapter 1, Parliament sets the regulatory framework in the UK through the legislation under which the financial services regulators operate. This framework includes the regulators' objectives and the powers that they are given to pursue those objectives. As Parliament determines the roles and powers of the regulators, it has an interest in knowing how this framework operates and how the powers are being used. Parliament therefore rightly has a unique and special role in relation to the scrutiny and oversight of the financial services regulators. Effective Parliamentary scrutiny provides a valuable service for consumers, firms and the regulators. It can help to ensure that the regulators' resources are appropriately targeted to consider appropriate democratic policy input from Parliament and bring important public policy considerations into focus.
- 5.4 The Future Regulatory Framework (FRF) Review will see the regulators take on increased responsibility for direct regulatory requirements which apply to firms. The government considers that Parliament's focus should continue to be on setting the strategic framework and objectives for financial services regulation, and holding the regulators to account for their actions to further their statutory objectives.
- 5.5 This approach aligns with the Treasury Select Committee (TSC)'s report on *The Future Framework for Regulation of Financial Services*,¹ in which the committee suggests that a targeted approach to scrutiny through the select committee system focused on the current framework, with some ex-ante scrutiny, is preferable to 'line-by-line' scrutiny of all regulator proposals. Respondents to the previous consultation also felt that it would not be

¹ *The Future Framework for Regulation of Financial Services*, House of Commons Treasury Committee, July 2021.

appropriate or feasible for Parliament to seek to adopt a model of line-by-line scrutiny of regulator proposals, similar to that of the Economic and Monetary Affairs (ECON) Committee of the European Parliament.

- 5.6 The All-Party Parliamentary Group on Financial Markets and Services' report on *The Role of Parliament in the Future Regulatory Framework for Financial Services* also suggested that Parliament's key focus should be on setting the framework for regulating financial services and scrutinising the delivery of regulation within that framework.²
- 5.7 The government's view is that the existing Parliamentary scrutiny mechanisms – including the targeted scrutiny provided by select committees – are appropriate and flexible and should continue to be the principal ways in which Parliament holds the regulators to account.
- 5.8 Respondents to the previous consultation strongly agreed with the importance and value of Parliamentary accountability and scrutiny of the regulators. The select committee system was considered robust and effective, and respondents felt the TSC performed an important and valuable function in holding the regulators to account. Given the regulators' wide-ranging powers, which they exercise independently of government, it is vital that Parliament is able to continue to effectively scrutinise and hold the regulators to account following the implementation of the FRF Review.
- 5.9 The debates during the passage of the FS Act 2021 demonstrated Parliament's keen interest in ensuring that appropriate mechanisms are in place to allow it to effectively scrutinise financial services policymaking and the activities of the regulators. In particular, participants in the debate highlighted the importance of the regulators having sufficient regard to the conclusions of Parliamentary scrutiny, and the importance of parliamentarians receiving sufficient information from the regulators to facilitate their scrutiny and ensure it is effective.
- 5.10 Throughout the passage of the Act, several parliamentarians commented that the current legislation does not set specific requirements on regulators to provide Parliament with the information it requires to scrutinise financial services policy effectively. They called for an explicit requirement for the regulators to provide Parliament with relevant information, tabling amendments to this effect. The government recognised these concerns, and welcomed the commitments from the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) in March 2021 to an open and transparent relationship with Parliament, and the reassurance that the PRA and the FCA would have due regard to the conclusions of any Parliamentary scrutiny.³ The government has therefore considered this issue carefully, including the proposals noted above from respondents and Parliamentarians designed to address the concerns raised, and reflecting the commitments made by the regulators during the passage of the FS Act 2021.

² *The Role of Parliament in the Future Regulatory Framework for Financial Services*, All-Party Parliamentary Group on Financial Markets & Services, February 2021.

³ *FCA accountability to Parliament and approach to sustainable finance*, Financial Conduct Authority, March 2021.

Financial Services (FS) Bill 2019-2021, Prudential Regulation Authority, March 2021.

- 5.11 The government is also aware of the lively debate in Parliament regarding the appropriate committee structure for scrutinising financial services, and the views shared in response to our first consultation. However, Parliament is responsible for determining the best structure for its ongoing scrutiny of the regulators. The government will therefore not be making recommendations to Parliament on this matter.
- 5.12 Some respondents to the previous consultation also noted the importance of Parliament and select committees having access to appropriate financial services technical expertise. The government's view, in line with that set out by the TSC in their recent report,⁴ is that Parliament already has the ability to draw on expertise. Further, as noted by respondents to the previous consultation, Parliament can also use industry and regulator secondments to further enhance technical expertise where required. Therefore, the government will not be making recommendations to Parliament on this matter.
- 5.13 The government's proposals aim to ensure that select committees continue to have access to the information needed to best scrutinise the work of the regulators and set expectations for how the regulators must respond to any representations from Parliamentary committees. These requirements should be sufficiently flexible to ensure that regulation can be made in a dynamic and agile way, including by ensuring that regulators can move quickly in an emergency.

Measure 6: Requirement to notify the relevant committee of a consultation

- 5.14 In order to ensure that the relevant Parliamentary committee has the information it requires to be able to carry out effective scrutiny, the government intends to bring forward a new statutory requirement for the PRA and the FCA to notify the relevant Parliamentary committee when they publish a consultation on any matter. This should draw attention to the section of the consultation dealing with how the proposals advance the regulators' objectives and how they have considered their regulatory principles and any other relevant considerations. Although the regulators regularly bring consultation papers to the attention of the TSC, as noted by parliamentarians through the passage of the FS Act 2021, there is currently no statutory basis for this action. The government considers that there is value in ensuring that parliamentarians continue to receive the right information to conduct their scrutiny following the implementation of the FRF Review, and believes that this measure responds to the clear calls for action in this area throughout the passage of the FS Act 2021.

⁴ *The Future Framework for Regulation of Financial Services*, House of Commons Treasury Committee, July 2021.

Measure 7: Requirement for the regulators to respond to Parliament

5.15 At present, although both the PRA and the FCA engage with Parliament regularly and respond to letters and parliamentary questions from parliamentarians, there is no statutory requirement to respond to formal responses to consultations from select committees. Given the important role of select committees in the structure of Parliamentary scrutiny, and to ensure that the regulators have due regard to the conclusions of this scrutiny, the government intends to bring forward a new statutory requirement for the regulators to respond in writing to formal responses to statutory consultations from Parliamentary committees. This proposal will allow Parliament to understand how the regulators have considered the committee's views and any changes that have been made to the approach, drawing on (or cross-referring to) the policy statement issued by regulators where relevant.

Question 5: Do you agree that these measures require the regulators to provide the necessary information on a statutory basis for Parliament to conduct its scrutiny?

Chapter 6

Stakeholder engagement and the policymaking process

6.1 This chapter sets out the government's views on the importance of stakeholder engagement in the regulatory policymaking process. It summarises respondents' support for the current arrangements, and goes on to outline the government's proposals on stakeholder engagement, which focus on three distinct areas: the regulators' statutory panels, the production of cost-benefit analysis (CBA), and how the regulators review their rules.

Stakeholder engagement

6.2 As set out in the previous consultation, the opportunity for relevant stakeholders to engage with and scrutinise the development of policy proposals is essential for two main reasons. First, policymaking is at its most effective when it draws on the views, experience, and expertise of those who may be impacted by regulation. Good policymaking should, as far as possible, be based on evidence, and so should take into account evidence that external stakeholders may be able to provide. Second, meaningful engagement by stakeholders helps support the policymaking process, making it more likely that final proposals are effective, understood, and accepted as fair and reasonable by stakeholders.

6.3 The current requirements on the regulators to consult stakeholders are set out in Chapter 1. Respondents to the consultation noted that the regulators already conduct extensive stakeholder engagement and research on their proposed policies, and that the consultation requirement works well. They also noted that the regulators' current engagement in many cases goes beyond their statutory requirement to consult. Suggestions for improvements tended to be related to strengthening and enhancing these practices and the statutory underpinning, rather than an overhaul of the consultation process.

6.4 The government recognises that some consultation respondents raised concerns about specific aspects of the regulators' stakeholder engagement. This included concerns about aspects of the operation of the regulators' statutory panels, a lack of clarity on the regulators' approach to reviewing their rules, and the rigour, scope, and external challenge of the regulators' CBA. The following proposals are intended to reflect existing best practice by the regulators while addressing these concerns.

Strengthening the role of the statutory panels

- 6.5 As set out in Chapter 1, following the implementation of the Future Regulatory Framework (FRF) Review, the regulators will take responsibility for determining the direct regulatory requirements that apply to firms that were previously set by the EU. This is likely to result in the regulators making more rules across a broader range of topics. This will in turn increase the opportunities for the regulators to consult their statutory panels from the outset of policy and regulatory development, which was not possible to the same extent while the UK was a member of the EU.
- 6.6 The government and the regulators believe this will strengthen the panels' important ability to provide stakeholder input into the development of policy and regulation. As set out in Chapter 1, the government considers that it is appropriate to build on the strengths of the existing arrangements. The government intends to introduce a number of measures to ensure that there is consistency in the panels' status, that the panels represent a diverse range of stakeholders, and that the regulators are transparent about where they have engaged the panels, maintaining the crucial 'critical friend' role.
- 6.7 The government believes that the strengthened role of the statutory panels, alongside these new measures, will address the concerns of some respondents to the previous consultation about the panels' functions. These included a lack of clarity around how and when the regulators consulted the panels on particular proposals; whether the panels were consulted early enough to affect policy development; and whether the regulators took panels' views adequately into consideration.

Measure 8: Placing the FCA's Listing Authority Advisory Panel (LAAP) and the PRA Practitioner Panel's insurance sub-committee on a statutory footing

- 6.8 As set out in Chapter 1, the regulators currently maintain two panels voluntarily: the Financial Conduct Authority (FCA)'s Listing Authority Advisory Panel (LAAP) and the Prudential Regulation Authority (PRA)'s insurance sub-committee. These have been in operation since the establishment of the FCA in 2013 and the first sub-committee meeting in 2018, respectively. They have proven value; for example, the insurance sub-committee discussed insurance supervision in the context of the PRA consultation on operational resilience in the last year,¹ and the LAAP replied in its own right to the Lord Hill Review.²
- 6.9 Given the important contribution that the panels make as a channel for stakeholder engagement with the regulators' policy development, the government considers that there should be consistency across the panels' statutory underpinning, and consistency concerning what is expected of the regulators in terms of engaging and operating the panels. The government

¹ PS6/21 CP29/19 DP1/18 *Operational Resilience: Impact tolerances for important business services*, PRA, March 2021.

² *FCA Listing Authority Advisory Panel (LAAP) response to the Call for Evidence by Lord Hill's Listings Review*, FCA LAAP, January 2021

therefore proposes that the LAAP and PRA Practitioner Panel's insurance sub-committee be placed on a statutory footing. The government proposes that this would be broadly the same as the existing statutory panels under the Financial Services and Markets Act (FSMA) 2000, and will provide confidence to stakeholders that they are permanent and that the regulators have a duty to consult them where appropriate.

Measure 9: Statutory requirement for the regulators to publish information on their engagement with the panels

- 6.10 The regulators already provide some information on panel engagement as part of their Annual Reports, and in the FCA's responses to the panels' Annual Reports. Depending on the issue, the regulators also note engagement in consultation papers. Where panels have responded directly to a consultation, the FCA list them among the respondents. In order to increase the transparency of where and when panels have been consulted, the government proposes introducing a new statutory requirement to systematise this existing practice and ensure clear and consistent communication by regulators on their engagement with panels across all of their work. The statutory requirement would require the regulators:
- to provide information in their annual reports on their engagement with panels over the reporting period
 - to provide, as part of public consultation, information on pre-consultation engagement with panels
- 6.11 The government does not propose to specify the form and detail of the information provided. This is to ensure that the regulators (working with the panels as appropriate) can find the appropriate balance between transparency and the confidentiality crucial to ensure an open exchange of views as part of the policymaking process, which is fundamental to the panels' role as a 'critical friend'.

Measure 10: Statutory requirement for the regulators to maintain a statement on appointment processes for the panels

- 6.12 Ensuring the right membership of the panels is crucial to their success in providing challenge, a range of expertise, and differing perspectives. Panels that have diverse backgrounds, expertise, and thought will be better placed to ensure the regulators receive the most comprehensive appraisal of their policy. In order to ensure that the membership of panels represents the full diversity of stakeholders, both amongst practitioners and amongst consumers, there should be a clear and transparent process for appointing members.
- 6.13 The FCA has recognised the importance of improving diversity in the membership of the panels and is already undertaking a review to identify ways to boost diversity so their composition appropriately reflects the range of practitioners and stakeholders in financial services. The government

welcomes the work the regulators are doing to move recruitment to the panels in this direction, and expects the regulators will take this opportunity to commit to open and fair recruitment practices to ensure a diverse range of qualified candidates are appointed to panels.

- 6.14 Building on this work, and to improve transparency, the government proposes to introduce a requirement for the regulators to each maintain statements on their processes for appointing members to panels. This statement would need to be approved by HM Treasury before it is published.
- 6.15 The government also recognises that consultation respondents raised concerns regarding the composition of panel membership. These included suggestions that there may be a bias towards large firms and established sectors, and suggestions that there may be a lack of representation for some groups; for example, vulnerable consumers.
- 6.16 As part of their ongoing work to improve the diversity of panels, the regulators should also continue to consider the diversity of the sectoral composition of membership. In the context of emerging technologies, changing business models, and evolving consumer choices (for example, the transition towards digital payments), it is particularly important that a representative balance of stakeholder types and views are included. While this is a matter for the regulators, given that the number of panel members is not set out in legislation, one way of achieving this may be an expansion of the number of panel members.

Question 6: Do you agree with the proposals to strengthen the role of the panels in providing important and diverse stakeholder input into the development of policy and regulation?

The regulators' cost-benefit analysis (CBA) processes

- 6.17 Respondents to the consultation noted that conducting CBA is a useful practice, and welcomed the regular inclusion of CBA in the regulators' consultations. However, some respondents also expressed concerns that it is not clear when and how regulators decide to conduct CBA (e.g. which rules and guidance they apply to), and what the process involves. Some industry respondents expressed concerns that the regulators' analysis focuses overly on the expected benefits of intervention and underplays the costs to individual firms and the wider market. Some consumer groups, on the other hand, felt that CBA was overly concerned with the cost to firms, and disregarded quantifying benefits.
- 6.18 There were also concerns expressed regarding the rigour and scope of the regulators' CBAs. Some consultation respondents suggested that CBA should include an assessment of behavioural changes that would result from the introduction of the proposed rule, the wider effect on markets rather than just individual firms, and for assessment of alternate options for intervention, rather than only a comparison between the proposed rule and 'do nothing'.
- 6.19 The government recognises the significant concerns around CBA that respondents have expressed, and the following proposals are intended to

address them through increased transparency and improved consistency of the CBA process. The government also recognises that the proposed measures may increase the costs of regulation and require additional data collection from stakeholders and firms.

Measure 11: Statutory requirement for the regulators to publish a framework for CBA

- 6.20 In order to increase transparency regarding when stakeholders can expect a CBA to be conducted, and what that CBA will consist of, the government proposes a new statutory requirement for the regulators to publish and maintain a public version of their framework for conducting CBA.
- 6.21 The FCA already publishes its framework for conducting CBA which contains the FCA's approach to many of the suggestions made by consultation respondents, such as consideration of effects on the wider market and CBA of other options.³ This proposal is intended to increase transparency by setting out that both regulators should publish and maintain these frameworks. This will allow stakeholders to be confident that regulators' CBA practices are based on a consistent, publicly available approach.
- 6.22 Though legislation will not specify the content of the framework in detail, to allow regulators flexibility in their operations, the government expects that it would specify that frameworks include clear explanations of the following:
- the criteria establishing when CBA is necessary (including an explanation of existing exemptions)
 - the methodology involved in different aspects of CBA
 - how representations at consultation are considered
- 6.23 The government proposes that under this new statutory requirement the PRA and the FCA should be required to explain any criteria they have for determining when to conduct CBA beyond their existing statutory obligations under FSMA (such as for guidance). This requirement is intended to ensure there is a clear explanation for all of the CBA conducted by the regulators.
- 6.24 The publication, and maintenance of, new frameworks in relation to the regulators' approach to CBA will provide transparency going forward and support robust regulatory policymaking. Clear and publicly available CBA processes should provide further assurance to stakeholders that the regulators are seeking to understand the effect of their regulatory policymaking. This should also support stakeholders in considering effectively whether the regulators' assessments through their CBA are correct.

Question 7: Do you agree that the proposed requirement for regulators to publish and maintain frameworks for CBA provides improved transparency to stakeholders?

³ *How we analyse the costs and benefits of our policies*, Financial Conduct Authority, July 2018.

Measure 12: Establish a statutory panel to support development of regulators' approach to CBA

- 6.25 Several respondents expressed support for enhanced external challenge as a way to improve the quality of the regulators' CBA. The regulators' existing panels can be, and are, asked for early, qualitative comment on CBA. However, given the technical nature of CBA and the existing panels' role of strategic input, the government proposes the creation of a new statutory panel dedicated to supporting the development of the regulators' CBAs.
- 6.26 There are a number of different options for how this panel could operate. The government is therefore considering whether it would be most effective for the panel to provide its input "pre-publication" as part of the development of CBA for individual consultations, or for the panel to provide its input "post-publication" and scrutinise the approach post-implementation, at a more aggregate level, to consider more systematically the regulators' approach and methodology in approaching CBAs.
- 6.27 In the "pre-publication" role, the new panel would perform a similar role for the regulator as the Regulatory Policy Committee (RPC) performs for the government.⁴ The panel would therefore assess and challenge the quality of evidence and analysis used to produce CBA for rule proposals, and provide advice on whether CBA has been conducted according to best practice and is likely to accurately capture the effect of the proposed change. The government's view is that regular, in-depth comment on CBAs pre-consultation could improve both individual CBA and the overall approach.
- 6.28 The government recognises that the proposed CBA panel providing detailed comments on all of the regulators' CBA could cause delays to the policymaking process. To avoid harmful delays or an overly burdensome process for minor rule changes, there would have to be carefully considered thresholds for when the CBA panel is asked to comment, and exemptions for emergency rulemaking. It may also be appropriate to consider whether expedited mechanisms need to be established for specific circumstances. A further consideration is that this approach may require more data from firms in advance of consultations, placing a greater cost on firms and regulators.
- 6.29 The alternative approach is for the new CBA panel to have a "post-publication" role and so would therefore review CBA following implementation of a rule change. Under this option rather than scrutinising the CBA for individual rules, the panel would periodically review a number of CBA produced by the regulators. At the conclusion of this review, the panel would provide the regulators with public recommendations for how they can improve their overall methodology and approach to CBA. Where appropriate, these recommendations may form the basis for updating the regulators' CBA frameworks (measure 12; proposed above). Such recommendations could cover: how the regulators identify and quantify cost and benefit, how they take into account possible market-wide effects, and

⁴ Where required, the RPC also performs a somewhat similar role for regulators. The FCA is required by the Small Business, Enterprise and Employment Act 2015, as amended by the Enterprise Act 2016, to conduct Impact Assessments (IAs) on Qualifying Regulatory Provisions (QRPs), which are reviewed by the RPC. However, these IAs are distinct from the CBA required by FSMA, and the high threshold for QRPs means that relatively few are produced in any given year.

how they account for behavioural change resulting from interventions. This could enable the CBA panel to provide more holistic comments on the regulators' CBAs. It would also avoid the possibility of delays to rulemaking. The government's view is that a "post-publication" panel would provide long-term improvement to the regulators' overall approach to CBA.

- 6.30 The government considers that the proposed CBA panel can play an important role in improving the production of regulators' CBA. The government also considers that it can increase stakeholders' confidence that there is regular, independent input into the regulators' CBA. These two outcomes should be achievable with either of the possible roles of the panel, pre- or post-publication, and the government recognises the value of both proposals. The government would be grateful for stakeholder views on which of the possible roles of the panel would be preferable.

Question 8: Should the role of the new CBA Panel be to provide pre-publication comment on CBA, or to provide review of CBA post-publication?

Regulators' review of their rules

- 6.31 It is important to review policy interventions after implementation to ensure they remain appropriate and have had the desired effect. This can range from monitoring to wider evaluation of the impact of a rule after a certain period. In recent years the principle of reviewing regulation after it has been in operation has been embedded in government legislative initiatives. The government's approach to post-legislative scrutiny, published in 2008, contains a commitment for departments to produce memoranda on appropriate Acts, so that Parliamentary select committees may decide whether to conduct further post-legislative scrutiny.⁵ The government's consultation on 'Reforming the framework for better regulation' (which closed on 1 October 2021) is also considering how the reviews conducted under requirements to review legislation - contained in the Small Business, Enterprise, and Employment Act 2015 - might be strengthened.⁶
- 6.32 The regulators already make use of similar reviews in a number of areas. In the previous consultation for the FRF Review, the government set out that more routine use of reviews by the regulators might be expected to help ensure that regulatory rules remain appropriate and have had the desired effect. At the same time, the government recognised that more regular reviews will have resource implications and could divert the regulators' attention from other important tasks, as well as potentially introducing greater burden for industry, for example if additional data is required from industry to conduct these reviews.
- 6.33 The benefits of an established review process are that it will:
- contribute to managing risk and uncertainty (of the intervention and its implementation)

⁵ *Post-legislative Scrutiny – The Government's Approach*, Office of the Leader of the House of Commons, March 2008.

⁶ *Reforming the framework for better regulation*, Department for Business, Energy, and Industrial Strategy, July 2021.

- improve current interventions by providing the evidence to make better decisions
- develop a better understanding of what works, for whom and when, and generate evidence for future policymaking
- make the timing and conduct of reviews more predictable for stakeholders

6.34 Undertaking regular and predictable reviews of regulations is important for building confidence amongst stakeholders, who can see that the regulators are actively working to understand the effects of, and improve, regulation. As noted earlier in this chapter, the regulators do review their regulatory policies and the FCA publishes its framework for *Ex post impact evaluation*,⁷ which focuses on quantifying the impact of significant or novel measures after implementation. However, there are no public frameworks outlining other forms of review, such as monitoring. This leaves the review process potentially opaque to stakeholders and, as evidenced by some consultation responses, the result is that stakeholders are unsure of when to expect reviews and what to expect of the review process.

Measure 13: Requirement for the regulators to publish and maintain a framework for reviewing their rules

6.35 The government proposes a new statutory requirement for the PRA and the FCA to publish and maintain a framework for how they conduct rule reviews. The government expects this would cover all approaches to assessing the effect of rules, from monitoring to wider evaluation of the impact. This will allow stakeholders to be more confident that regulators' review of rules is based on consistent, publicly available standards. It will also incentivise the regulators to clearly systematise their review process as a part of setting it out.

6.36 The government proposes that the content of the framework would be left for the regulators to develop, given their expertise, and to ensure flexibility in their operations. However, the government proposes requiring that the framework includes:

- any differences in the purpose of reviews, and what different types of review entail
- criteria for deciding which type of review is used
- criteria for deciding when each type of review will be conducted

6.37 The main purpose of the framework is to encourage systematisation of regulators' review of rules and provide clarity and transparency for stakeholders on how and when rules are reviewed. This will allow stakeholders to be confident that reviews are happening regularly and in a consistent manner, increasing confidence in regulation.

⁷ *Ex post impact evaluation framework*, Financial Conduct Authority, December 2018.

Question 9: Do you agree that the proposed requirement for regulators to publish and maintain frameworks for how the regulators review their rules provides improved transparency for stakeholders?

Alternative proposals

- 6.38** Some respondents recommended the creation of an external body to provide additional independent challenge to the regulators and scrutiny of final rules. Proposals differed on whether this would be a body explicitly supporting the relevant Parliamentary committee, or an entirely stand-alone body. In both cases it was suggested this body could enhance Parliamentary scrutiny of proposals by issuing independent reports (at public consultation stage) on whether the regulators' proposals are likely to advance their objectives. The practical obstacles to be overcome in making such a body operate effectively are substantial, and there would be significant cost and resource burdens. Such a body would also duplicate existing functions and potentially undermine the regulators' operational independence.
- 6.39** The government considers that the existing avenues for stakeholders to provide input, feedback, and challenge through public consultation, as well as the role of HM Treasury and Parliament in assessing whether the regulators are advancing their objectives, remain the appropriate accountability mechanisms. This position is supported by the Treasury Select Committee (TSC) report on *The Future Framework for Regulation of Financial Services*, which said 'the creation of a new independent body to assess whether regulators were fulfilling their statutory objectives would not remove the responsibility of [the TSC] to hold the regulators to account, and it would also add a further body to the financial services regulatory regime which [the TSC] would need to scrutinise'.⁸ Therefore, the government does not propose the creation of an external scrutiny body.
- 6.40** Some respondents also noted that judicial review is not frequently utilised by firms, and that an alternate dispute resolution mechanism should be established to provide firms a route to challenge decision making. The government considers that there is a risk that such a mechanism could undermine the regulators' independence if a non-judicial body could mandate them to change their rules. The creation of a new dedicated dispute resolution body would require significant resourcing and would duplicate many of the functions of judicial review, which remains open to industry participants where they wish to challenge regulator decision-making.
- 6.41** As set out earlier, in Chapter 4, the government's proposed power for HM Treasury to order a rule review is intended to offer a mechanism for mandating a review of regulator rules when it is in the public interest, while maintaining the operational independence of the regulators. Along with the proposed framework for rule review to be published by regulators, the government considers these proposals address these concerns.

⁸ *The Future Framework for Regulation of Financial Services*, House of Commons Treasury Committee, July 2021, page 28.

Chapter 7

A comprehensive FSMA model

- 7.1 This chapter describes the set of changes which will be necessary to move to a comprehensive FSMA model of regulation in areas which are currently covered by retained EU law. This aims to establish a more agile regulatory framework for the future, with the expert and independent regulators able to determine the direct regulatory requirements that apply to firms.
- 7.2 In a statement in the House of Lords on 16 September 2021, Lord Frost announced a review into retained EU law, to consider both its status in UK law, and its practical effect. HM Treasury is working closely with the Cabinet Office to ensure the Future Regulatory Framework (FRF) Review is consistent with this wider review.

Revoking retained EU law

- 7.3 Direct regulatory requirements are the obligations that firms must follow, for example a requirement to hold a certain level of capital; to act in a particular way, such as provide certain information to a customer; or refrain from acting in a certain way or from undertaking a particular activity. In order to move to a comprehensive FSMA model of financial services regulation, the government intends to ensure that the financial services regulators have the ability to determine the direct regulatory requirements which are currently set out in retained EU law, just as they already do in other areas not covered by retained EU law.
- 7.4 Conferring this responsibility on the financial services regulators will ensure that there is a consistent approach taken to financial services regulation across UK markets, allowing the development of coherent and user-friendly rulebooks. It will allow regulation to be agile and responsive to future developments and technologies, while maintaining the UK's high standards of regulation.
- 7.5 In order to confer this responsibility on the regulators, it will be necessary to repeal a significant amount of retained EU law that currently contain many of these direct regulatory requirements.
- 7.6 The government will ensure that the deletion of retained EU law happens in a way that maintains continuity. Any particular piece of retained EU law will not cease to have effect until the regulator rules which replace it are in place – or it has been determined that it is appropriate. The government is committed to high regulatory standards, while making the most of this opportunity to do things differently and better. In many cases, it may be

appropriate for the regulators to ensure continuity with the current provisions in retained EU law. However, there will also be instances where it is appropriate for the regulators to take the opportunity to tailor the rules to reflect the specifics of UK markets, and to make targeted improvements, in line with their objectives.

Measure 14: A power to repeal parts of retained EU law, including the direct regulatory requirements that apply to firms

- 7.7 The government intends, as a general approach, to take a power to repeal retained EU law, which it will use to repeal the direct regulatory requirements which apply to firms. This repeal will enable the appropriate regulator to replace those provisions with their own rules. The repeal will take effect at the same time as the regulators' new rules come into force, to avoid any "gap" in regulation.
- 7.8 This process – of repealing the relevant retained EU law and concurrently replacing it with the appropriate regulator rules – will take place over a number of years. The government and the regulators will work together closely on this, to ensure that there is a clear and transparent approach to transition, that provides continuity and stability and appropriately manages any impact on firms or consumers that would result from the changes.
- 7.9 At a minimum, the government proposes that the ability to repeal retained EU law should extend to:
- all EU Regulations and decisions related to financial services which are retained EU law by virtue of section 3 of the EUWA
 - all statutory instruments made under the European Union Communities Act 1972 (ECA) which are relevant to financial services, and statutory instruments made under other empowerments which implemented EU obligations relating to financial services
 - all EUWA statutory instruments relevant to financial services
 - all instruments made under specific empowerments contained in legislation of the type specified above
- 7.10 A number of responses to the previous consultation stressed the extent to which FSMA itself has been increasingly altered in order to implement EU law, and suggested that this will require some changes to the parts of FSMA that have been affected by this. For example, Part 18 of FSMA was substantially reformed following the adoption of EU legislation. Where retained EU law is set out in elements of domestic primary legislation related to financial services, the government proposes that it should also have the ability to amend or repeal the relevant provisions, in order to deliver a coherent regulatory framework.
- 7.11 There may be other elements of retained EU law that are not direct regulatory requirements, but which nevertheless should be repealed in order to facilitate regulator rulemaking. These include:

- areas which duplicate existing domestic requirements
- areas which set out unnecessary process, which may unduly restrict the scope that the regulators have for independent action
- areas in retained EU law which give the regulators narrowly defined powers, where these are already covered by the rulemaking powers that FSMA gives to the regulators.

Designated Activities Regime

- 7.12** Many activities covered by retained EU law are also regulated activities under the RAO. This means that the full FSMA framework already applies, including a general rulemaking power for the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) in relation to authorised persons, unless a firm is exempt.¹ The regulators already have sufficient powers to establish direct regulatory requirements for firms, where they are authorised persons, and they act within the established FSMA framework. This framework gives the regulators the power to make rules, but also sets the wider regulatory architecture such as supervision, enforcement, and consultation.
- 7.13** As a result, in those areas already covered by the core FSMA authorisation regime, no significant additional rulemaking powers will be required to allow the regulators to replace retained EU law that is to be repealed. The government considers that the regulated activities arrangements, and the RAO process, work well. Accordingly, the government does not propose amending these arrangements in any substantive way.
- 7.14** However, there are many pieces of retained EU law which set the rules for a kind of activity, product, or conduct which are not FSMA regulated activities, and which apply to a broader range of entities than FSMA authorised persons. As a result, the general rulemaking powers of the PRA and the FCA in relation to authorised persons does not currently apply.
- 7.15** Some examples include the Short Selling Regulation, which sets out the rules which apply to the activity of short selling, or margin rules that apply to certain types of derivative transactions, which set out how firms engaged in this activity should mitigate the risk posed by these type of contracts.
- 7.16** Many of these activities came to be subject to EU law as a response to the global financial crisis, when policy makers sought to introduce standardised rules across a number of different activities, even where those activities may be carried out by some firms which may not consider themselves to be “financial services” firms at all. It is right that these activities continue to be subject to regulation by the financial services regulators, as activities outside the core financial services perimeter can often have an impact on financial markets and consumers.

¹ In some instances, a firm can be exempted from the requirement to become an authorised person in order to carry out a regulated activity.

- 7.17 Including all these activities within the perimeter set by the RAO, and making them subject to the general prohibition in section 19 of FSMA, would have the effect of requiring every person who carries out these activities and who is not an exempt person to become an authorised person. This would not be a proportionate approach.
- 7.18 For example, a large number and wide range of businesses across the economy enter into derivatives contracts. They are often used by firms to manage the risk of price fluctuations. These firms can be complex financial services firms or non-financial businesses operating in the real economy. For example, a car manufacturer may enter into metal derivative contracts as a way of protecting itself against a rise in the price of the metals that it needs to purchase. In most instances under retained EU law, firms that enter into derivative contracts which are not cleared in a central counterparty (CCP) must exchange a certain amount of “margin” or collateral in order to reduce the impact if one party is not able to meet its obligations in that contract. The government agrees that such activities should remain subject to an appropriate level of regulation. However, it would not be proportionate to make entering into these derivative contracts a regulated activity, because it would require all entities that wish to use these contracts to apply for authorisation from the FCA, with all of the additional obligations that would entail.

Measure 15: To create a new Designated Activities Regime, to enable to the regulators to make rules for such activities

- 7.19 To ensure that these activities can continue to be regulated in a proportionate manner that is consistent with the existing FSMA framework, the government proposes to create a new Designated Activities Regime (DAR).
- 7.20 The DAR will be a mechanism to allow the regulation of certain activities outside the FSMA authorisation process. This will mirror the existing approach for the RAO: the government will determine the activities that are in scope via secondary legislation (within a framework established in primary legislation) and this will empower the regulators to determine the rules that will regulate these activities.
- 7.21 However, the DAR would be subject to a more limited rulemaking power than the general rulemaking powers in relation to authorised persons. It would allow the relevant regulator to make rules relating to the designated activity only, and not other unrelated activities of the firm. This reflects the fact that this is designed to be a more limited regime, relating to the designated activities only (and not the wider activities of those who carry out designated activities). This reflects the risk that activities outside the core financial services perimeter can often have on financial markets and consumers.
- 7.22 Persons carrying out a specific activity would be required to follow the regulators’ rules relating to that activity, and there would be appropriate

enforcement mechanisms and penalties for failure to comply with the relevant rules.

7.23 The government proposes that the framework within which the regulators must operate when establishing these rules should be closely based on the provisions in FSMA, which already has well established provisions to address information gathering, enforcement, supervision, consultation etc. These provisions are currently spread out across different instruments and regimes, and bringing them into a coherent framework under FSMA will simplify the procedures and powers available to the regulators to administer the DAR.

7.24 Each set of regulations currently set out in retained EU law performs a different function. As a result there should be a means for HM Treasury to modify the application of the core DAR framework for certain activities, or to add additional elements, in order to ensure that this regime is capable of recreating the core elements of the existing EU regimes, at a minimum. For example, it may be appropriate to require one regulator to consult another in particular circumstances.

Box 7.A: The RAO and the DAR

	Regulated Activities	Designated Activities
How is framework set?	FSMA sets regulators' objectives; regulatory principles; consultation requirements etc.	
How is activity specified?	HMT specifies regulated activities by SI (the RAO), e.g. activities related to banking, insurance	HMT would specify designated activities by SI, e.g. short selling, issuing securities
What rule-making powers are available?	General rulemaking – the relevant regulator makes rules applicable to the authorised firm	Specific rulemaking – the relevant regulator would make about how the designated activity must be carried out
Who can carry out the activity?	FSMA general prohibition – only authorised persons can carry out regulated activities	Any firms carrying out a designated activity would be required to follow the relevant rules
What requirements are placed on firms?	Firms must apply for authorisation, and meet threshold conditions on an ongoing basis	<div style="border: 1px solid black; border-radius: 50%; padding: 5px; display: inline-block;"> <i>This includes authorised firms, who will also be required to follow the rules for any designated activities they perform</i> </div>
	Firms must follow the regulators' rules in relation to the regulated activity, and in addition any rules in relation to activities which are not regulated	
What sanctions are available?	Range of sanctions and offences apply if firms do not follow the relevant rules, or are not appropriately authorised to carry out the activity	Range of sanctions and offences may apply if firms carry out a designated activity without following the relevant rules

7.25 The government intends to use the DAR, where appropriate, to replicate the existing scope of regulation, and therefore bring the activities currently covered by retained EU law into this new kind of FSMA regulation. However, the government does not intend to restrict the DAR to retained EU law only. It will be possible to designate, in the future, other activities if necessary. This will ensure that the framework can adapt to future developments – for example, new types of activity, or where the risks associated with a particular activity change in a way that merits bringing it within scope of regulation.

Question 10: Do you agree with the government's proposal to establish a new Designated Activities Regime to regulate certain activities outside the RAO?

Bringing FMIs covered by retained EU law into FSMA regulation

- 7.26** The DAR will not be an appropriate approach to all areas of retained EU law that currently sit outside the core FSMA authorisation framework. There are a small number of areas where retained EU law applies to entities which are systemic to the financial system, or which play a unique or essential role in markets, but which currently sit outside of the core FSMA authorisation regime. In particular, this includes certain types of Financial Market Infrastructure (FMI).²
- 7.27** The government does not believe that the DAR, described above, would be suitable for such firms. This is because the regimes which have been established to regulate these entities typically require a firm to go through a recognition process or otherwise become registered with the relevant regulator in order to carry out certain activities. While the exact processes differ in each regime, these recognition regimes have similarities (both in purpose and process) to the authorisation process that firms must go through in order to carry out regulated activities under FSMA.
- 7.28** When incorporating these regimes into UK law, the UK kept these regimes outside the core FSMA authorisation framework. There may be some cases where it would be appropriate for HM Treasury to specify that FMIs' activities are regulated activities, bringing them within the core FSMA framework. However, this is unlikely to be an appropriate approach in all cases and may require complicated amendments to the core FSMA authorisation regime.
- 7.29** The reason for this is that many FMIs provide a very wide range of activities as part of their unique function, but they often perform these activities for different reasons than other types of financial services firm. For example, a central counterparty may undertake some investment services simply in order to manage the risk it faces as a result of offering clearing services, not because it wishes to offer investment services to clients. And so the general requirements in FSMA may not be the most appropriate framework for regulating these firms effectively. As a result, a number of FMIs have previously been exempted from the FSMA authorisation framework even when they are carrying out regulated activities. This is the case for Recognised Investment Exchanges, for example.
- 7.30** In all instances, the government must ensure that the regulators are given sufficient rulemaking powers to enable them to make rules replacing the direct regulatory requirements which currently apply to firms under retained EU law. However, due to the systemic and unique nature of these firms, and the wide variety of different EU regimes that underpin them, this is likely to require more detailed solutions in order to give the regulators appropriate

² There is no universally agreed definition of an FMI, but the term is used here to mean: recognised investment exchanges (RIEs); various entities offering payment services; payment systems; trade repositories (TRs); credit rating agencies (CRAs); central counterparties (CCPs); and central securities depositories (CSDs).

rulemaking powers, and set the appropriate frameworks within which the rules might operate. For example:

- trade repositories (TRs) and credit rating agencies (CRAs): The FCA has a general rulemaking power in relation to Trade Repositories and another general rulemaking power in relation to CRAs, which were both created using powers in the EUWA,³ in order to prepare for EU exit. These currently sit separately from the general rulemaking power in FSMA. The government considers that these powers will be needed on an ongoing basis, to ensure the effective regulation of these important firms. The government therefore intends to put these general rulemaking powers on an appropriate statutory footing
- recognised investment exchanges (RIEs): The FCA already has specific rulemaking powers over RIEs, and has established a robust recognition regime. Where needed, the government will ensure that the FCA has the necessary additional powers to replace the direct regulatory requirements in retained EU law
- various entities related to payments and e-money: there are various types of entity performing payment or e-money services, and the supervisors have a number of regulatory powers in relation to them. Where these existing powers are not sufficient, the government will ensure that they have the necessary additional powers to replace the direct regulatory requirements in retained EU law.

Central counterparties and central securities depositories

7.31 The Bank of England is responsible for the regulation and supervision of CCPs and central securities depositories (CSDs), due to the fact that these FMI are essential to the stability of the financial system.⁴ The Bank of England carries out this responsibility as part of its overall statutory objective to protect and enhance the stability of the UK financial system.

7.32 However, the Bank of England has very limited rulemaking powers over CCPs and CSDs, since prior to EU exit the regulations relating to them were largely set at EU level through the European Market Infrastructure Regulation⁵ and the Central Securities Depositories Regulation,⁶ with the Bank of England responsible for supervision and enforcement of the EU regulations in the UK. At a minimum, the government must ensure that the Bank of England has the relevant powers to replace all these provisions in retained EU law relating to the regulation of CCPs and CSDs.

³ Regulation 3, the Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019; and regulation 74, the Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2019.

⁴ The Bank of England is also responsible for regulating recognised clearing houses (RCHs). However, there are currently no RCHs which are not also CCPs in the UK.

⁵ Regulation (EU) No 648/2012

⁶ Regulation (EU) No 909/2014

- 7.33 But it is also important that the Bank of England has an effective way to uphold and enhance standards for CCP and CSD regulation, including a means to make new rules for these firms, to address emerging risks and keep pace with international standards.
- 7.34 The government is therefore considering granting the Bank of England a general rulemaking power in relation to CCPs and CSDs so that it can set appropriate rules for these firms. Such a new power, and the associated broader responsibility, will be accompanied by appropriate enhancements or additions to the Bank of England's current framework of objectives and accountability in relation to the regulation and supervision of these entities.
- 7.35 The UK is home to a global clearing market used by market participants from around the world. Any enhancements to the existing framework governing the way the Bank of England exercises its responsibilities over CCPs and CSDs would need to reflect not only the vital domestic importance of these firms, but also the effect they can have on the global financial system as well as the role they play in safeguarding global financial and monetary stability. The government will set out further details in due course.

Activity-specific have regards and obligations

- 7.36 The previous consultation for the FRF Review considered 'Activity-Specific Legislation' to provide additional public policy input into regulators' rulemaking in specific areas. This proposal was designed to enable the government to set out specific duties and policy considerations that the regulators should have regard to when making rules in a specific area.

Measure 16: The ability to establish activity-specific 'have regards' and obligations

- 7.37 In some instances, it may be necessary to require the regulators to consider specific aspects of public policy which are not generally applicable and so are not captured by the objectives and principles which the regulators already have. Some of the detailed rules in retained EU law were specifically drafted to address certain public policy points which are still relevant. If these rules are updated in the regulators' rulebooks in the future, it is right that the regulators should continue to have those public policy priorities in mind.
- 7.38 The Financial Services Act 2021 included a small number of considerations which the PRA is required to "have regard" to when making its rules to implement the Basel standards, and a similar but separate list to which the FCA must have regard to when making rules to introduce an Investment Firms Prudential Regime. For example, the PRA is required to have regard to relevant standards recommended by the Basel Committee on Banking Supervision. The government considers that this model could have benefits when applied more widely to some parts of the regulatory framework.
- 7.39 However, the government is mindful that it is important to maintain a sensible balance between cross-cutting and activity-specific regulatory

principles. Where policy considerations are relevant to many areas of regulation, these will be reflected in cross-cutting regulatory principles, in line with Chapter 3 of this consultation. The regulators' must have regard to these considerations across the full range of their responsibilities.

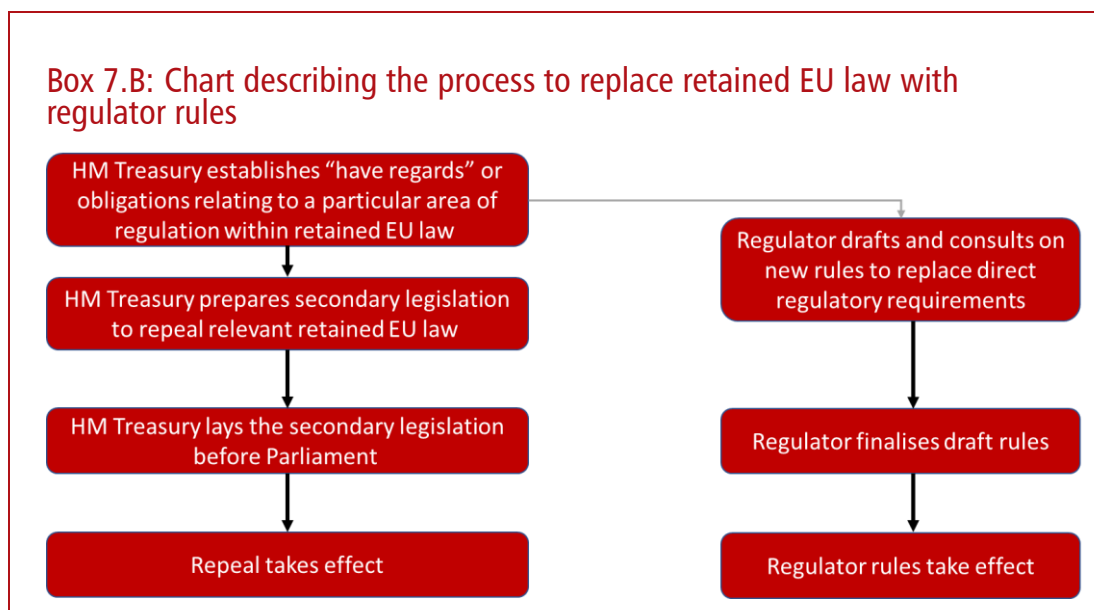
- 7.40 Therefore the government proposes to have an ability to set specific "have regards" which the regulators must consider when exercising their rules in specific areas of regulation. For example, the government may set "have regards" for the FCA when it is making rules in relation to uncleared derivatives.
- 7.41 When making rules, the regulators must act in a way that advances their statutory objectives. The government believes that it is generally appropriate for the regulators to make their own judgement about what rules are required, based on their objectives and on the regulatory perimeter established by HM Treasury. However, in response to the previous consultation, some stakeholders suggested that there should be a means for government and Parliament to require the regulators to make rules covering certain matters, to ensure important wider public policy concerns are addressed.
- 7.42 The government agrees that there are some areas where it is appropriate to put an obligation on the regulators to exercise their rulemaking powers in a way that imposes certain types of requirements on firms. Section 143C of FSMA, inserted by Schedule 2 to the Financial Services Act 2021, provides an example of this: it requires that the FCA "must make rules applying to FCA investment firms" that impose certain types of prudential requirements.
- 7.43 The government therefore proposes to take a power to place obligations on the regulators to make rules in relation to specific areas of regulation. This could be necessary in areas where retained EU law will be repealed and the government believes it is essential that there are similar provisions in the regulators' rulebooks. This would mean, for example, that HM Treasury could put an obligation on the FCA to use their rulemaking power to make rules relating to the reporting of financial transactions.
- 7.44 It would not be possible to use this power to impinge on the regulators' independence by seeking to influence what those rules should be. The regulators could not be required to act in a way that is inconsistent with their objectives.
- 7.45 The government expects that the ability to set "have regards" and to put an obligation on the regulators to make rules in relation to specific areas should at a minimum extend to any areas currently covered by retained EU law. As retained EU law is deleted from the UK statute book, the government is committed to ensuring a coherent approach. This means avoiding creating a distinction between regulations that were once part of retained EU law, and regulations that weren't. The government will therefore continue to consider the appropriate scope of the powers to make "have regards".

Question 11: Do you agree with the government's proposal for HM Treasury to have the ability to apply "have regards" and to place obligations on the regulators to make rules in relation to specific areas of regulation?

Revocation and amending retained EU law for purposes other than regulator rulemaking

- 7.46 As set out above, the government intends to take a power to repeal the direct regulatory requirements that apply to firms in retained EU law, so that the regulators can determine the direct regulatory requirements on firms in their rulebooks.
- 7.47 However, there are also a number of provisions in retained EU law which do not set direct regulatory requirements on firms. These provisions form the wider “regulatory architecture” that establishes the regulatory regimes. For example, these provisions set out how certain rules should be supervised or enforced, and the powers that the regulators may have to do so.
- 7.48 Deleting significant parts of retained EU law is a complex task, and is likely to require a number of other changes in order to keep this regulatory architecture functioning effectively.
- 7.49 In some instances, the government will require the ability to amend retained EU law directly in order to bring it into alignment with the FSMA framework and ensure that it can be kept up to date. This is particularly the case where retained EU law has been incorporated into existing domestic legislation. This ability will be needed to ensure that the legislation can be kept up to date, especially where retained EU law does not contain many direct regulatory requirements but instead relates to the actions of the regulators – for example, the legislation establishing the bank resolution regime.
- 7.50 The government will therefore ensure that the legislation that will be brought forward enables the necessary amendments to be made to retained EU law, and to allow for consequential changes to ensure coherence and the continued effective operation of FSMA and other relevant legislation, which will enable the deletion of direct regulatory requirements.

Process for moving to a comprehensive FSMA model



- 7.51 The process of moving from retained EU law to a comprehensive FSMA model of regulation will be a significant undertaking, and will take a number of years. There are hundreds of pieces of retained EU law relating to financial services, and some of the most detailed pieces can be several hundred pages long. Following the delivery of the powers proposed in this chapter, a subsequent programme of secondary legislation will be required to give effect to the changes. This means that Parliament will have the opportunity to scrutinise the legislation which enables these changes, and subsequently, the statutory instruments giving effect to these changes. The government and the regulators will work together closely on this, to ensure that there is a clear and transparent approach to transition, that provides continuity and stability and appropriately manages any impact on firms or consumers that would result from the changes.
- 7.52 This process will involve government identifying the areas of retained EU law which need to be repealed, and putting in place any necessary “have regards” and obligations through secondary legislation.
- 7.53 The government and the regulators will ensure that there is sufficient time for HM Treasury and the regulators to consult where necessary, and that there is a sufficient time for firms to adapt to any rule changes before they are applied.
- 7.54 In many instances, the government would expect the regulators to initially replace the repealed provisions with rules that are similar to those which are already in place. However, this approach will allow the regulators to ensure that the rules are properly tailored for the UK markets, and appropriately reflect their objectives. It will also mean that the rules can be more efficiently updated in the future, for example in response to new global standards, or to take account of new business models. The government and the regulators recognise the importance of providing stability and continuity for firms and their customers by avoiding unnecessary changes.

Chapter 8

Responding to this consultation and next steps

- 8.1 This consultation will remain open for three months, closing on 9 February 2022. HM Treasury are inviting stakeholders to provide responses to the questions set out below and share their views on the proposals for how the government intends to take forward its approach to the FRF Review.

Box 8.A: Questions for consultation respondents

1. Do you agree with the government's approach to add new growth and international competitiveness secondary objectives for the PRA and the FCA?
2. Do you agree that the regulatory principle for sustainable growth should be updated to reference climate change and a net zero economy?
3. Do you agree that the proposed power for HM Treasury to require the regulators to review their rules offers an appropriate mechanism to review rules when necessary?
4. Do you agree with the proposed approach to resolve the interaction between the regulators' responsibilities under FSMA and the government's overseas arrangements and agreements?
5. Do you agree that these measures require the regulators to provide the necessary information to Parliament on an appropriate statutory basis to conduct its scrutiny?
6. Do you agree with the proposals to strengthen the role of the panels in providing important and diverse stakeholder input into the development of policy and regulation?
7. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for CBA provides improved transparency for stakeholders?
8. Should the role of the new CBA Panel be to provide pre-publication comment on CBA, or to provide review of CBA post-publication?
9. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for how the regulators review their rules provides improved transparency to stakeholders?

10. Do you agree with the government's proposal to establish a new Designated Activities Regime to regulate certain activities outside the RAO?
11. Do you agree with the government's proposal for HM Treasury to have the ability to apply "have regards" and to place obligations on the regulators to make rules in relation to specific areas of regulation?

Who should respond?

- 8.2 A wide range of stakeholders will be interested in the important issues presented in this document. Responses are welcome from all stakeholders, including:
- financial services institutions and firms
 - other businesses impacted by financial services regulation
 - trade associations and representative bodies
 - consumer groups

How to submit responses

- 8.3 Please submit your responses to FRF.Review@hmtreasury.gov.uk, or post to:
- Future Regulatory Framework Review
Financial Services Strategy
HM Treasury
1 Horse Guards Road
SW1A 2HQ

Next steps

- 8.4 This document sets out the government's response to the feedback received in response to the previous consultation and a series of proposals for how the government intends to take forward its approach to the FRF Review, including:
- the changes needed to the regulators' statutory objectives and principles to ensure the government's priorities and objectives for the sector are fully reflected across the breadth of the regulators' responsibilities

- the proposals for ensuring that accountability, scrutiny and engagement arrangements with HM Treasury, Parliament, and stakeholders are appropriate given the regulators' responsibilities, and;
- The proposed approach to returning responsibility for designing and implementing the direct requirements that apply to firms in certain areas of retained EU law to the regulators within a system established by government and Parliament

8.5 The government will take into account stakeholder views and respond to this consultation in due course.

HM Treasury Future Regulatory Framework (FRF) Review 2021 Consultation: Processing of Personal Data

8.6 This notice sets out how HM Treasury will use your personal data for the purposes of the Future Regulatory Framework Review 2021 consultation and explains your rights under the UK General Data Protection Regulation (UK GDPR) and the Data Protection Act 2018 (DPA).

Your data (Data Subject Categories)

8.7 The personal information relates to you as either a member of the public, a parliamentarian, or a representative of an organisations or company.

The data HM Treasury collect (Data Categories)

8.8 Information may include your name, address, email address, job title, and employer, as well as your opinions. It is possible that you will volunteer additional identifying information about yourself or third parties.

Legal basis of processing

8.9 The processing is necessary for the performance of a task carried out in the public interest or in the exercise of official authority vested in HM Treasury. For the purpose of this consultation the task is consulting on departmental policies or proposals or obtaining opinion data in order to develop good effective government policies.

Special categories data

8.10 Any of the categories of special category data may be processed if such data is volunteered by the respondent.

Legal basis for processing special category data

- 8.11 Where special category data is volunteered by you (the data subject), the legal basis relied upon for processing it is: the processing is necessary for reasons of substantial public interest for the exercise of a function of the Crown, a minister of the Crown, or a government department.
- 8.12 This function is consulting on departmental policies or proposals, or obtaining opinion data, to develop good effective policies.

Purpose

- 8.13 Personal information is processed for the purpose of obtaining the opinions of members of the public and representatives of organisations and companies, about departmental policies, proposals, or generally to obtain public opinion data on an issue of public interest.

Who HM Treasury share your responses with

- 8.14 As part of policy development, HM Treasury may share full responses to this consultation, including any personal data provided (such as your name and email address) with the Financial Conduct Authority (FCA), Prudential Regulation Authority (PRA) and Bank of England.
- 8.15 Information provided in response to a consultation may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 2018 (DPA) and the Environmental Information Regulations 2004 (EIR).
- 8.16 If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory code of practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence.
- 8.17 In view of this it would be helpful if you could explain to HM Treasury why you regard the information you have provided as confidential. If HM Treasury receive a request for disclosure of the information HM Treasury will take full account of your explanation, but HM Treasury cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury.
- 8.18 Where someone submits special category personal data or personal data about third parties, HM Treasury will endeavour to delete that data before publication takes place.
- 8.19 Where information about respondents is not published, it may be shared with officials within other public bodies involved in this consultation process to assist HM Treasury in developing the policies to which it relates. Examples of these public bodies appear at:
<https://www.gov.uk/government/organisations>.

- 8.20 As the personal information is stored on HM Treasury's IT infrastructure, it will be accessible to HM Treasury's IT contractor, NTT. NTT will only process this data for HM Treasury's purposes and in fulfilment with the contractual obligations they have with HM Treasury.
- 8.21 At a future date, HM Treasury may decide to publish summarised and/or anonymised versions of responses to this consultation document as part of a second consultation.

How long HM Treasury will hold your data (retention)

- 8.22 Personal information in responses to consultations will generally be published and therefore retained indefinitely as a historic record under the Public Records Act 1958.
- 8.23 Personal information in responses that is not published will be retained for 3 calendar years after the consultation has concluded.

Your rights

- 8.24 You have the right to request information about how your personal data are processed and to request a copy of that personal data.
- 8.25 You have the right to request that any inaccuracies in your personal data are rectified without delay.
- 8.26 You have the right to request that your personal data are erased if there is no longer a justification for them to be processed.
- 8.27 You have the right, in certain circumstances (for example, where accuracy is contested), to request that the processing of your personal data is restricted.
- 8.28 You have the right to object to the processing of your personal data where it is processed for direct marketing purposes.
- 8.29 You have the right to data portability, which allows your data to be copied or transferred from one IT environment to another.

How to submit a Data Subject Access Request (DSAR)

- 8.30 To request access to personal data that HM Treasury holds about you, contact:

HM Treasury Data Protection Unit

G11 Orange

1 Horse Guards Road

London

SW1A 2HQ

dsar@hmtreasury.gov.uk

Complaints

- 8.31 If you have any concerns about the use of your personal data, please contact HM Treasury via this mailbox: privacy@hmtreasury.gov.uk.

- 8.32 If HM Treasury is unable to address your concerns to your satisfaction, you can make a complaint to the Information Commissioner, the UK's independent regulator for data protection. The Information Commissioner can be contacted at:

Information Commissioner's Office

Wycliffe House

Water Lane

Wilmslow

Cheshire

SK9 5AF

0303 123 1113

casework@ico.org.uk

- 8.33 Any complaint to the Information Commissioner is without prejudice to your right to seek redress through the courts.

Contact details

8.34 The data controller for any personal data collected as part of this consultation is HM Treasury, the contact details for which are:

HM Treasury

1 Horse Guards Road

London

SW1A 2HQ

London

020 7270 5000

public.enquiries@hmtreasury.gov.uk

The contact details for HM Treasury's Data Protection Officer (DPO) are:

The Data Protection Officer

Corporate Governance and Risk Assurance Team

Area 2/15

1 Horse Guards Road

London

SW1A 2HQ

London

privacy@hmtreasury.gov.uk

HM Treasury contacts

This document can be downloaded from www.gov.uk

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

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

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gov.uk

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