

## HM Treasury Financial Services Future Regulatory Framework review Response from the Association of British Insurers 19 February 2021

### ***The UK insurance and long-term savings market and the ABI***

*The Association of British Insurers is the voice of the UK's world-leading insurance and long-term savings industry. A productive and inclusive sector, our industry supports towns and cities across Britain in building back a balanced and innovative economy, employing over 300,000 individuals in high-skilled, lifelong careers, two-thirds of which are outside of London.*

*The UK insurance and long-term savings industry manages investments of over £1.9 trillion, contributes over £16bn in taxes to the Government and supports communities across the UK by enabling trade, risk-taking, investment and innovation. We are also a global success story, the largest in Europe and the fourth largest in the world.*

*The ABI represents over 200 member companies, including most household names and specialist providers, giving peace of mind to customers across the UK. Please note we would be happy, and stand ready, to provide further information if this would be helpful to HM Treasury.*

*For the purposes of this response, 'insurers' refers to insurance, reinsurance and long-term savings companies.*

### **Executive Summary**

1. The ABI welcomes the opportunity to respond to HM Treasury's Phase II of the Financial Services Future Regulatory Framework review. The outcome of this review will decide how regulation is formulated, implemented and scrutinised in post-Brexit Britain. We have been pleased to see that HM Treasury, regulators and industry are embracing this opportunity with an open mind and without predetermined views to ensure the best possible outcome.
2. The departure from the EU provides an excellent opportunity for the UK to boost economic recovery post-Covid, and drive investment to level-up and create long-term economic advantage in communities across the country. We can keep consumers safe and eradicate the idiosyncrasies of a system which were designed for a single market of 28 countries and therefore are too often not fit for purpose. And we can press our already significant advantage in financial services on the world-stage, maintaining the UK's position as a leader in a modern, global economy.
3. These are the objectives which should drive the Government's approach as we reclaim and reform the rules and regulations governing financial services post-Brexit. With this in mind, the ABI welcomes the Minister's foreword reference to the intention of the proposed approach "to ensure that our regulatory regime has the agility and flexibility needed to respond quickly and effectively to emerging challenges and to help UK firms seize new business opportunities in a rapidly changing global economy". Much of the consultation focuses on securing flexibility and agility for the regime but remains quieter about how the new regime will identify effective measures to support firms and ensure a vibrant and successful financial services sector.
4. HM Treasury's model proposes a radical change, moving away from the EU rules-based model that the industry is familiar with, towards a principles-based framework with less oversight and a substantial transfer of powers and responsibilities to regulators. The aim would be to build flexibility and agility into the framework.
5. A principles-based approach can deliver these objectives, including the boost to our economic recovery and substantial increase in long-term investment. However, what we want to achieve as

a country must be enshrined in the new system to ensure that every regulator stays focused on these shared goals and that the framework provides stability and certainty to enable financial services firms to take the decisions to invest for the longer term. A system that gives our regulators too much scope for constant change will undermine the attractiveness of the UK. That is why we are calling for:

- 5.1. Regulators to be given a new statutory objective of supporting economic growth in line with other jurisdictions commonly recognised as having a thriving global financial services industry, such as Hong Kong, the US, Singapore and Australia.
  - 5.2. A regulatory framework that balances the proposed substantial transfer of responsibilities to regulators with enhanced regulatory accountability, scrutiny and transparency. This needs to be achieved by empowering Parliament and Treasury with explicit additional powers and resources, alongside strengthening stakeholder participation.
  - 5.3. The right balance to be struck between legislation and regulation, acknowledging the benefits of a principles-based framework but recognising the need to include certain elements in legislation, going beyond the level of detail initially suggested in HM Treasury's proposal.
6. The absence of these elements could still deliver a more flexible framework. However, it would jeopardise a number of objectives for this review such as (1) appropriate policy input by democratic institutions; (2) effective accountability; (3) a coherent and user-friendly framework; (4) international confidence; and (5) a framework that facilitates stakeholder engagement.
  7. This flexibility, without appropriate measures in place, could easily turn into uncertainty and unpredictability and eventually unwanted consequences, including an unbalanced regulatory output that would jeopardise industry's chances to better serve consumers, support the real economy, remain competitive and thrive while supporting the UK's position as a global financial centre.
  8. The ABI's response below develops some key initiatives aimed at achieving the above elements. For instance, in order to enhance accountability and scrutiny, we recommend the establishment of a Joint Committee of the Parliament, supported by a panel of experts, to scrutinise financial services legislation and rules and look in depth at areas to improve regulatory effectiveness (further developed in Questions 2 and 7). From the stakeholder engagement perspective, we recommend a function that would allow regulated firms to challenge regulatory decisions or decision-making processes without the need to have to go to court. Other regulators' processes in place, such as the Pensions Regulator's determinations panel, could be worth considering (further details in Question 9).
  9. These and other proposals developed in this response would also contribute to a new regulatory culture that would embrace a closer relationship with the industry built on mutual trust and respect. This would substantially help to avoid regulatory approaches that have been seen in the past such as gold-plating or the use of an inadequately evidence-based approach, including poor quality or rushed cost benefit analysis.
  10. Finally, we recognise that the outcome of the Framework review will require changes in legislation that will take time to implement. It is important that this does not delay the implementation of the outcome of other relevant reviews currently taking place such as the Solvency II review. Otherwise, we would be unnecessarily delaying important benefits to consumers as well as to the wider economy at a time when HM Treasury, and the country, is looking ahead to post-Covid economic recovery and to making the UK more internationally competitive post-Brexit.

## Questions

### 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?

- 1.1. The FSMA model has broadly operated well over the last 20 years and there would be a need after two decades for changes to be made to ensure the future regulatory framework is fit for purpose. With regulation-making now residing with the UK regulators and HM Treasury proposing to move away from the EU's more prescriptive approach, there is a rare opportunity to improve the UK financial services regulatory framework in a way that has not been seen for many decades.
- 1.2. The government's proposal, which envisages substantial new responsibilities and discretion for regulators, allocates smaller legislative, policymaking as well as oversight roles to Parliament and government than those of the European Parliament and the European Commission. It proposes that Parliament and government mainly focus on setting the policy framework for financial services regulation, having little say on regulatory requirements affecting firms.
- 1.3. Although HMT's blueprint advocates for enhanced accountability, we see these enhancements as falling short of what would be needed to ensure an appropriate democratic input and a balanced and proportionate regulatory output. We make suggestions on how this could be delivered further down in this section as well as in responses to Questions 2, 6 and 9.
- 1.4. The ABI understands and shares the proposal's aims to (1) ensure a more agile and flexible regime, more capable to respond to challenges and to do so quickly; and (2) support UK firms to seize new business opportunities in the global economy. However, the government's blueprint concentrates significant responsibilities and discretion in the hands of regulators to meet the first of these aims while remaining quieter about tackling the second goal.
- 1.5. The ABI believes that, for the proposed framework to fulfil the above goals and support some of its key objectives such as (1) policy input by democratic institutions; (2) effective scrutiny; (3) coherent and user-friendly framework; (4) international confidence; and (5) facilitating stakeholder engagement, it needs to embed a series of measures including, but not limited to:
  - 1.5.1. Widening the regulators' statutory objectives to support economic growth;
  - 1.5.2. Enhancing accountability, improving scrutiny and promoting further transparency; and
  - 1.5.3. An appropriate balance between legislation and regulation.

#### Widening the regulators' statutory objectives to support economic growth

- 1.6. The aims of the current regulatory framework can be broadly summarised as the totality of the statutory objectives of the two main financial services and markets regulators, the FCA and the PRA, as given by FSMA.
- 1.7. The regulators' objectives were established when the UK was part of the EU. Changed circumstances due to Brexit should require a reassessment of those objectives and decisions on whether they remain 'fit for purpose' or require some revision. In particular, they need to ensure that a healthy financial services industry continues to play a major role in the post-Brexit economy.
- 1.8. Under the new framework, with regulators' decision-making responsibilities significantly expanded, regulators need a primary objective that supports economic growth to provide an explicit balance to their other statutory objectives. The lack of such an economic growth objective would mean that, for instance, the PRA's main objectives would continue to be focused on removing risk from the system. Other jurisdictions such as Hong Kong, the US, Australia and Singapore already include wider objectives for their regulators, including to "*facilitate the sustainable market development of the insurance industry*", "*enable American companies to be competitive with foreign firms*", "*the efficiency and development of the*

economy” and “develop Singapore as an international financial centre”, respectively. In Canada, the Office of the Superintendent of Financial Institutions’ (OSFI) mandate, as directed by parliament, states<sup>1</sup> “the need to allow financial institutions to compete effectively and take reasonable risks.”. This is developed further in our responses to Questions 4 and 5. A secondary objective will not be effective in balancing out primary objectives that are mainly focused on risk, as the former is subordinated to the latter. There is a need for this new objective to be on equal footing with other statutory objectives.

#### Enhancing accountability, scrutiny and transparency

- 1.9. We welcome that HM Treasury’s proposal recognises there is a need to enhance accountability, scrutiny and transparency to reflect regulators’ expanded responsibilities. A failure to embed the measures mentioned above would result in a new framework that, although potentially agile and flexible in principle, would generate an onerous and unbalanced regulatory regime. Such a framework would not be fit for purpose, would struggle to support UK firms to seize new business opportunities and reduce the industry’s ability to accept risks from UK businesses, thus exposing them to greater uncertainty. It would also negatively impact the offering and affordability of financial products available to UK consumers. Both of these would limit the investments that the industry can make to the economy and damage the UK’s status as a global financial hub. This is further developed in Questions 2 and 7.
- 1.10. Strong accountability will be essential within the new framework. Both Parliament and HM Treasury should be provided with explicit additional powers and resources to allow for a higher degree of oversight of the regulators. Enhanced accountability should also be given to stakeholders who are impacted by the decisions of the regulators.
- 1.11. The SM&CR places personal responsibility on senior managers within financial services. Regulators claim, quite rightly, that this drives behaviours and culture within organisations as senior managers are made clearly accountable for decisions. We would like to see the same in our regulators. Government and regulators should consider learnings from SM&CR and how accountability and personal responsibility of senior managers within the regulator can be strengthened. This, in combination with the inclusion of an objective for regulators to take account of economic growth, should significantly help achieve a more coherent, agile regulatory framework that is better equipped to meet the specific regulatory needs of UK firms, markets and consumers. We further develop our vision for enhanced accountability in our responses to Questions 2, 6 and 9.
- 1.12. In respect of scrutiny, regulators need to be subject to enhanced scrutiny from Parliament, government and from independent statutory panels. Therefore, there is a need for new mechanisms and contents to improve the quality and quantity of scrutiny. For instance, we have previously proposed an advisory panel capable of detailed investigation and reporting to Parliament to support Parliamentary Committees in holding the regulators to account. This is not an audit of processes and controls but scrutiny of the form and reasonableness of decisions made which can drive firms out of markets, or stop them coming into being in the first place. We develop this proposal further in response to Question 7. HM Treasury and Statutory panels can also contribute to enhance the scrutiny function; however, they would need their roles to be strengthened, as we detail further in response to Questions 8 and 9.
- 1.13. Transparency should be enhanced for firms but also for Parliament and government. At the firm level, communication should be transparent in intent and the standard needed. By way of example, the PRA’s requirements are sometimes so opaque to firms that consultants are paid significant sums to interpret letters from supervisors. Other consultants are then engaged to find out what standard the PRA has asked other firms to meet when a letter requesting change arrives. Clearly this is ideal for neither firms nor regulators.

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<sup>1</sup> <https://www.osfi-bsif.gc.ca/Eng/osfi-bsif/Pages/so-sf.aspx>

1.14. Regulation is most effective when regulators are transparent as to their concerns and the problems they see, and honest about the difficulties of finding proportionate solutions across a range of firms with different risk profiles. In addition, the process of consultation should be demonstrably transparent, with a requirement to show the detailed reasoning which leads the regulator to conclude its original views stand unaltered or are modified. The lack of such detailed reasoning lacks transparency, as well as modifying regulation with changes not subject to consultation, such as the PRA changes to what became SS1/20<sup>2</sup>.

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

- **What are your views on the proposed division of responsibilities between Parliament, HM Treasury and the financial services regulators?**

Policy framework legislation

- 2.1. The division of responsibilities proposed by HM Treasury is mainly based on FSMA's model. Government and Parliament would set the regulatory framework through legislation, meaning high-level general objectives and principles, while the financial regulators would be responsible for setting the requirements that apply to financial services firms and markets.
- 2.2. The government blueprint's new contribution is a new policy framework legislation that would allow Parliament and government to set the policy approach for specific areas of regulation. The policy framework legislation would set out activity-specific regulatory principles that regulators should take into consideration when developing policy and designing regulatory requirements for that particular activity.
- 2.3. The ABI recognises the value of providing Parliament and government with the mechanism to increase policy input into the regulation making process. However, the blueprint recognises that these activity-specific regulatory principles would be subordinated to the regulators' statutory objectives, relegating the public policy input to a tier two objective status, only to be taken into account when supporting regulators' prime objectives.
- 2.4. Given regulators' independence and the fact that the activity-specific principles are subordinated to regulators' overarching objectives, regulators could decide, implicitly if not explicitly, to reduce focus on these principles as long as they were understood not to be supportive of, or clashing with, regulators' statutory objectives. In this case, not even enhanced accountability could prevent this from happening as regulators would be acting within their powers and remit. To avoid this, there is a need for a new statutory objective for regulators to support economic growth, ensuring an appropriate input by the democratic institutions while, at the same time, preserving the independence of the regulators.

The role of Parliament

- 2.5. Besides passing legislation, Parliament must play a key role in holding regulators to account, scrutinising their work and ensuring they are acting within their statutory objectives and in line with policy objectives set out in legislation. We propose a Joint Committee of both Houses of Parliament to scrutinise financial services legislation and rules and look in depth at areas to improve regulatory effectiveness. The Joint Committee would be supported by a panel of experts who have experience in financial services law, policy and consumer advocacy. Ultimately, this proposal would be aiming at ensuring that (i) regulator policy meets intended policy objectives; (ii) performance is measured against the statutory objectives / principles; and (iii) supervisory effectiveness. This is further developed in Question 7.
- 2.6. Parliament also has a role to play in ensuring coordination between different regulatory authorities, with a focus on identifying areas of alignment and tensions in regulatory proposals, in order to ensure they are enacted in a coordinated and efficient manner.

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<sup>2</sup> <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2020/ss120.pdf>

- 2.7. There is also an important oversight role for Parliament in the preparation, negotiation and implementation of Free Trade Agreements, and other bilateral agreements with third countries. While this clearly goes beyond just regulation, 'trade' agreements can have regulatory implications. For example, in the form of setting a framework for ongoing regulatory cooperation, agreeing mutual market access, and/or (as in the case of the Bilateral Agreement between the United States of America and the United Kingdom on Prudential Measures Regarding Insurance and Reinsurance – the UK-US Covered Agreement) address specific prudential matters on a reciprocal basis.
- 2.8. Carrying out this level of enhanced accountability and scrutiny of the regulators, Financial Services regulation and legislation, as well as Free Trade Agreements, will require Parliament to have access to greater resources than it currently has at its disposal. Staffing with independent technical expertise would be necessary. Sufficient funding to carry out these enhanced functions as well as sufficient time to ensure that the financial services market works effectively would also be required.
- 2.9. The ABI has previously proposed a model, similar to that of the Social Security Advisory Panel, with an advisory panel made up of regulatory and industry experts who are best placed to support the scrutiny of regulation. Our proposal, which is further developed in Question 7, highlights the importance for both Houses of Parliament being involved. Members of Parliament would bring elected legitimacy, promote the democratic input and align wider public objectives and priorities. The Lords, more politically neutral, would contribute with their substantial expertise and long-term vision. This combination should ensure that Financial Services legislation and regulators are better scrutinised.

#### The role of HM Treasury

- 2.10. The review reminds us that Treasury Ministers have overall responsibility for the UK's financial services regulatory framework. Therefore, they have a constitutional duty to scrutinise the work of the regulators and to ensure that the framework is operating as intended.
- 2.11. The ABI agrees with the blueprint's proposal for an arrangement for systematic engagement between regulators and HM Treasury at an early stage in the policy-making process. This should be understood as a valid mechanism to enable public policy input into regulation. However, interactions between the regulators and HM Treasury and the panels should be transparent. We further develop this in Question 8.
- 2.12. With regards to the role that HM Treasury, alongside Parliament, has in deciding which financial services activities should be regulated (regulatory perimeter), the ABI supports a regular review of the appropriateness and effectiveness of the perimeter. This is particularly appropriate given the rapid pace of innovation, especially if we want to ensure consistency of consumer protections and the good functioning of competition in the market.
- 2.13. Further, we believe that HM Treasury should play a role in making some key appointments, including the members to the independent statutory panels established by FSMA to represent the interests of consumers and industry practitioners before regulators, following nominations from industry and other stakeholders when appropriate. Currently, these appointments are carried out by the regulators. We develop this further in question 9.
- 2.14. The ABI also supports HM Treasury to have an ex-post role in rule-making properly framed in the shape of an annual report to Parliament with its conclusions as to why HM Treasury is using, or not, secondary legislation updating powers. Similarly, we believe it is appropriate for a power of direction to be vested in HM Treasury to enable it to act promptly if any of the ex-post accountability mechanisms identify that changes to rules are needed quickly because, for instance, they are not operating as intended by Parliament.

#### The role of regulators

- 2.15. We support the concept of regulatory independence as this is important to foster a stable regulatory and supervisory environment. This independence must be accompanied by strong accountability. As mentioned in Question 1, government and regulators should consider

learnings from the SM&CR, which places personal responsibility on senior managers within financial services. This could be particularly useful when considering measures to strengthen accountability and personal responsibility of senior managers within the regulator.

- 2.16. Appropriate transparency would also be required, in particular over the effectiveness and efficiency of the regulatory system to support credibility and trust in regulatory decisions and processes, as noted in the OECD's guidance *The Governance of Regulators Creating a Culture of Independence*<sup>3</sup>.
- 2.17. We also believe that the Board of the FCA and the Prudential Regulation Committee, and supporting committees, should become more accountable and transparent to external members of those bodies and their role expanded to better promote the views of regulated firms via external members, especially if regulators are granted a new statutory objective to support economic growth.
- 2.18. UK regulators also have an important international role. Regulation should follow international standards where appropriate and regulators should continue to play a role in developing global standards. Whether that is taking a constructive role in the formal development of coordinated global efforts, the sharing of experience and best practice in multinational forums, and/or bilaterally through regular dialogue with regulators in other jurisdictions. The approach taken in each must be informed by a conscious decision as to what is appropriately tackled globally or domestically.
- 2.19. There are clearly a number of global challenges that are best tackled by working together with other jurisdictions—economic recovery is an obvious example. Similarly, there is merit in looking at how there can be international cooperation on prudential regulation especially where there are shared interests in supporting financial stability, as well as looking to minimise fragmentation which unnecessarily brings costs and burdens for firms.
- 2.20. This can also be achieved bilaterally with other jurisdictions and there is real value in having formal bilateral frameworks for regulators to cooperate on financial services and develop mutual understanding of their markets' regulation. In our experience, this builds trust and familiarity which in turns assists in resolving any potential bilateral concerns.
- 2.21. It is, however, also important to recognise the limits. When it comes to retail regulation and conduct issues, challenges are best addressed nationally with regard to the UK's consumers needs and expectations. The sharing of ideas and best practices is of course valuable, but it is difficult to identify an example of where coordinated action for retail would be appropriate beyond the UK's borders.
- 2.22. It is important that there is some oversight of the approach of the regulators when they are engaging internationally to ensure that it fits the overall policy objectives/strategy of government.
  - **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?**
- 2.23. HM Treasury's proposal is aligned with the overall objective of securing a more flexible and agile framework by moving away from the EU's more prescriptive approach and towards a more principles-based regime. Under the Treasury's blueprint, Parliament and government would be responsible for setting the policy framework, leaving policy discretion on how regulatory requirements should be designed, implemented and supervised to the regulators. This should result in one source of regulatory requirements for firms – the regulators' rulebooks, implying, in the case of Solvency II, a transfer of most of the legislation into the PRA's rulebook.
- 2.24. Therefore, striking the right balance between legislation and regulation is one of our main priorities, along with enhanced accountability, improved scrutiny and transparency and a new

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<sup>3</sup> <https://www.oecd.org/gov/creating-a-culture-of-independence-9789264274198-en.htm>

objective centred on supporting economic growth. The ABI believes that there is a need to recalibrate HM Treasury's proposal to guarantee a more balanced distribution of duties and responsibilities between Parliament, government and the regulators. We feel that HM Treasury's proposal is compromising too much in the name of flexibility and agility. We believe that we can help to refine the government's proposal in a way that results in a more balanced approach while still securing flexibility and agility without jeopardising high regulatory standards for the new framework.

- 2.25. For HM Treasury's proposal to work and provide industry with the levels of certainty it needs to operate, there is a need to have a more prescriptive level of legislation than that developed in the proposed blueprint. Legislation should set out all the crucial features that should remain in place in the mid and long-term. A more prescriptive legislation would also enable a better scrutiny of the regulators and their policies.
- 2.26. HM Treasury's consultation document presents Solvency II as a case study. We agree with the contents suggested to be set out in legislation. However, we strongly recommend adding at least the following:
  - 2.26.1. Conditions governing business – role of the board, system of governance, duties of auditors
  - 2.26.2. Rules relating to the valuation of assets and liabilities, technical provisions, own funds, solvency capital requirement (for standard formula or internal model), minimum capital requirement and investment rules
  - 2.26.3. Rules for operation of internal models
  - 2.26.4. Rules for firms in difficulty
  - 2.26.5. Group supervision
- 2.27. This would still deliver an agile framework, which is a priority for HM Treasury, while giving the regulators freedom to implement the technical detail and adapt their regulatory and supervisory approach to changes in the external environment.
- 2.28. For industry, this more prescriptive legislation would provide legislative certainty and confidence on what Parliament and government expect from the regulators in respect of core elements of the regime and would make it easier to hold the regulators to account. Flexibility and agility are fine for certain aspects of a regulatory regime, however for central planks of a prudential regime firms need predictability and certainty. This can only be provided by legislation rather than leaving these to regulators' rules.
- 2.29. For the above to work, it would be crucial that core legislative features, the elements of legislation that directs the regulators, are not set at a too high level as this would result in an unprecedented increase in regulatory power. Therefore, core features should be specific but still open enough for regulators to be able to operate.
- 2.30. In the particular case of Solvency II, the ABI also strongly believes that it is important for the Solvency II review to be implemented as soon as possible. We recognise that the outcome of the Framework review will require changes in legislation that will take time to implement. It is vital that this does not delay the implementation of the outcome of other relevant reviews currently taking place such as the Solvency II review. Otherwise, we would be unnecessarily delaying important benefits to consumers and the wider economy at a time when HM Treasury, and the country, is looking ahead to post-Covid economic recovery and to make the UK more internationally competitive post-Brexit.
- 2.31. Finally, and beyond the Solvency II case study, the ABI sees an additional risk in leaving to regulators too much decision-making and discretion powers. When combining individual regulations to solve individual problems the negative effects are incremental and dispersed but still real. For example, the market for financial advice is restricted by the sometimes inconsistent regulatory requirements such as those of MiFID2 and the IDD, as reflected in different rules for full advice, streamlined advice and basic advice spread across multiple



chapters of the FCA's Handbook. This complexity can prevent many people from obtaining advice. Disclosure of costs and charges is also complex, and often over-engineered and disproportionate relative to service provision and investment returns. A legislative steer could set a framework within which the FCA could simplify rules and increase competition in the advice market while reducing unnecessary or overly complex disclosures.

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

#### Transparency

- 2.32. We agree with the government's blueprint when it highlights that PRA and FCA will be subject to enhanced transparency requirements. Obliging regulators to explain how they have had regard to the public policy issues set out by Parliament in activity-specific policy framework legislation, would provide Parliament basis to improve the scrutiny of regulators.
- 2.33. Additionally, as already established in sections 138I and 138K of FSMA, the FCA and the PRA are required, before making any rules, to publish a draft accompanied by an explanation of their reasons for believing that making them is compatible with the regulatory principles in section 3B of FSMA. We urge the Government to include a similar provision in any legislation for activity-specific regulatory principles. Explaining publicly why a regulator believes its proposals are compatible with the principles and how it has balanced any tensions between them will be vital for transparency and accountability.
- 2.34. The above measures would increase transparency while better enabling Parliament, government and firms to scrutinise regulators and their work. They would also considerably contribute to better understand the rationale behind regulators' judgements and to ensure a consistency in their application, especially with regards to the treatment of firms.
- 2.35. This enhanced transparency would also support the challenge function of independent statutory panels and assist the routine reviews of regulations after 5 years to check measures in place are achieving their intended aims.

#### Cost-benefit analyses (CBA)

- 2.36. Reports from the National Audit Office have referred to the need for more robust evaluation. Often, the costs of implementing changes are underestimated in the regulators' cost benefit analyses. One of the consequences of this is that costs are being imposed on the industry with little consideration of their appropriateness and without meeting a basic Value for Money test.
- 2.37. For example, the FCA's CBA on its costs and charges disclosure proposals for workplace pensions (CP19/10<sup>4</sup>) severely understated the costs for firms associated with the forthcoming changes. It also paid little attention to the limited impact this increased disclosure would have on consumers. More recent examples would include PRA's paper on LIBOR transition (CP1/21<sup>5</sup>), from 7 January 2021, where the cost benefit analysis consists of four short paragraphs, largely descriptive of the PRA's intentions. The CBA ignored ABI's analysis about the ultimate increase of Solvency II technical provisions by between £3-4bn as a consequence of the transition to SONIA if no upward adjustment is applied.
- 2.38. Other times, the regulators' assessment of the benefits that could emerge from the proposals are not quantified, either qualitatively or quantitatively. An example of this is the FCA's recent CBA for its proposals on the publication of General Insurance Value Measures<sup>6</sup>.
- 2.39. It is often unclear how rigorously a CBA has been undertaken. There is often limited, if any, quantification of either costs or benefits, which would allow for comparisons to be made. Policy proposals are often justified by the assertion that, whatever the cost to the industry, which

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<sup>4</sup> <https://www.fca.org.uk/publication/consultation/cp19-10.pdf>

<sup>5</sup> <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/january/solvency-ii-deep-liquid-and-transparent-assessments-gbp-transition-to-sonia>

<sup>6</sup> <https://www.fca.org.uk/data/general-insurance-value-measures>

ultimately is passed on to the policyholders, the changes will lead to (even) higher policy protection.

- 2.40. Greater rigour should be applied to the regulators' cost benefits analyses so that they are consistently of better quality, contributing to an improvement of regulators', politicians' and the public's ability to scrutinise, debate and take informed positions on the proposals. Greater rigour could be achieved by:
  - 2.40.1. Not exempting the FCA and PRA from the processes that government and other regulators are required to follow and submit CBAs to the Better Regulation Committee ahead of taking forward policy changes for scrutiny;
  - 2.40.2. Requiring each CBA to state the degree and source of uncertainty in the estimates used in line with good practice the industry has adopted for the uncertainty in valuing assets;
  - 2.40.3. Establishing a public assessment of the quality of the CBA. The ABI stands ready to work with HM Treasury and regulators to develop this further; and
  - 2.40.4. Including CBAs within the scope of the systematic review of regulator's rules, which would allow to measure the accuracy of CBAs after five years and, when appropriate, the reform of any regulatory reforms derived from the original CBAs. This is further developed in question 9.

#### Early assessment and public consultations

- 2.41. Similarly, an early and comprehensive assessment of the potential regulatory implications of proposed changes would be beneficial. Often requirements remain unclear until too close to the implementation date. An early detailed assessment would enable better scrutiny at consultation stage and help to signal the regulators' intent so that industry and stakeholders are given the most time possible to engage with the proposals and to prepare for the likely changes.
- 2.42. We welcome the regulators' commitment to full public consultations for their policy proposals and the transparency with which they usually summarise the main feedback they receive in response to these, and how stakeholders' responses have informed their final position. We believe this should continue in order to maintain transparency. We would also encourage considering further consultation where feedback to a consultation leads to changes to policy proposals. For instance, the PRA made changes to what became SS1/20<sup>7</sup> between consultation and policy and those changes were not subject to consultation.
- 2.43. We have noted a varying degree of openness from regulators to amend initial proposals based on feedback received during consultations. It is not entirely clear what determines the level of openness and therefore where the consultation is aimed at receiving input from stakeholders and where it is aimed at merely informing the public on the regulators' intentions or undertaken as a procedural exercise.
- 2.44. To ensure a more meaningful consultation process, we would urge the regulators to make clearer in the consultations on which areas they are open to persuasion and on which areas the course has already been set and cannot change irrespective of the feedback received. We also call on the regulators to ensure that sufficient time is given to respond to consultations so that all stakeholders can provide meaningful responses, thus increasing the quality of the regulation and policy making process.

#### Evaluations of interventions

- 2.45. To further adapt the current regulatory framework to activity-specific regulatory principles, we would urge the regulators to invest time and resources to conduct full evaluations of their interventions that are published in full. For major areas of policy, some element of independent assessment could be involved. We believe that these evaluations should play a vital role in

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<sup>7</sup> <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2020/ss120.pdf>

demonstrating in a clear way how implemented policies or rules have had regard to the policy input from the UK's democratic institutions through the activity-specific regulatory principles.

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

- 3.1. The ABI supports FSMA's current regulatory principles and find them appropriate for the current framework. However, the ABI believes that for a more principle-based regime, as proposed in this review, principles should also underpin the following attributes:
  - 3.1.1. Operational sustainability;
  - 3.1.2. A high degree of accountability for the regulators as well as for the regulatory framework;
  - 3.1.3. A competitive framework that places the UK at the forefront of the international ecosystem and promote coordination of regulators across jurisdictions;
  - 3.1.4. A balanced distribution of duties and a clear delineation between regulators' and policymakers' remits;
  - 3.1.5. A clear delineation between the different institutions' remits;
  - 3.1.6. Cooperation between the different regulators;
  - 3.1.7. Regulatory consistency and predictability;
  - 3.1.8. A clear set of regulatory priorities;
  - 3.1.9. Space for effective revision; and
  - 3.1.10. Transparency around how trade-offs are decided.
- 3.2. The above attributes have been developed in different sections of this response and/or in the ABI's response to Phase I of the Future Regulatory Framework review.
- 3.3. A relevant point to make is more connected with the way principles are taken into account. In practice, consideration for principles have proven to be weak. For example, if the existing principle of ensuring sustainable growth in the economy had been given proper weight by regulators, this response might not need to propose the creation of a statutory objective on that subject.
- 3.4. To ensure principles are taken into account, we suggest HM Treasury introduces a structured policy evaluation approach which should prescribe how regulators must take them into account. We also recommend introducing performance indicators which would then aid ex-post scrutiny.

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

- 4.1. The ABI has been a long-standing supporter of a high-standards regulatory regime conducted by independent regulators driven by statutory objectives. We recognise their importance and do not wish for any of these to be amended or removed.
- 4.2. However, the ABI fundamentally believes that the regulators' statutory objectives should be expanded to support economic growth under the new framework where regulators concentrate new levels of responsibilities and discretion. Given the breadth of the new powers that the regulators receive under the new framework it is necessary to acknowledge the importance of these decisions in the wider context of the economy and international competitiveness.
- 4.3. We note the proposal specified in paragraph 2.44 that activity-specific regulatory principles are subordinated to the regulatory statutory objectives. This subordination means that regulatory

principles cannot provide a potential alternative to our recommendation for an economic growth input. Indeed, it reinforces the case for a statutory objective to support economic growth. The existence of such an objective would strengthen the consideration given to related activity-specific regulatory principles as they would contribute to the achievement of such an objective.

- 4.4. This would introduce an effective mechanism, on equal footing to the other operational objectives, that would guarantee public policy inputs and would allow regulators to:
  - 4.4.1. Become bigger contributors of stronger, more successful and better-managed UK financial services;
  - 4.4.2. Let firms have the opportunity to contribute further to achieving economic recovery and growth, the UK's carbon-neutral objective and transition to a green economy, as well as supporting further socially valuable investments, including social housing and infrastructure;
  - 4.4.3. Support the international competitiveness of the UK and its firms, contributing to attracting international capital and to the success of UK firms overseas; and
  - 4.4.4. Promote competition even further, contributing to increased efficiency for consumers and the effectiveness of the markets while promoting innovative solutions, including on range, affordability and access.

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

### Accountability

- 5.1. The EU process devotes more resource to the scrutiny of amendments to regulation than the government intends to devote to the amendment of the British regulatory regime. The EU process also involves a greater number of institutions, encouraging the development of differing views, conducive to an open debate. Therefore, in the context of the EU Withdrawal, similar safeguards need to be put in place to ensure there is an adequate degree of accountability.

### Regulatory statutory objectives

- 5.2. There are several jurisdictions where their financial services regulators are expected to balance financial stability, market integrity and policy holder interests with other objectives aimed at supporting the economic interest.
- 5.3. In countries commonly recognised as having a thriving global financial services industry, such as Hong Kong, the US, Australia or Singapore, the regulators are often given a specific duty to promote economic growth or competitiveness:
  - 5.3.1. Hong Kong: The legislation (the Insurance Ordinance<sup>8</sup>) establishing their insurance dedicated regulator, the Insurance Authority, places a duty on it to “*facilitate the sustainable market development of the insurance industry, and promote the competitiveness of the insurance industry in the global insurance market*”;
  - 5.3.2. The U.S.: A 2017 Presidential Executive Order<sup>9</sup> on Core Principles for Regulating the United States Financial System require federal regulators to “*enable American companies to be competitive with foreign firms*”. It also contains a reference to “*foster economic growth and vibrant financial markets*”;
  - 5.3.3. Australia: Australian Securities and Investments Commission Act 2001<sup>10</sup>, in its Part 1, section 2(b), states that in performing its functions and exercising its powers, ASIC must strive to “*maintain, facilitate and improve the performance of the financial system and the entities within that system in the interests of commercial*

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<sup>8</sup> [https://www.ia.org.hk/en/aboutus/role/statutory\\_functionse.html](https://www.ia.org.hk/en/aboutus/role/statutory_functionse.html)

<sup>9</sup> <https://www.govinfo.gov/content/pkg/DCPD-201700094/pdf/DCPD-201700094.pdf>

<sup>10</sup> <https://www.legislation.gov.au/Details/C2018C00077>

*certainty, reducing business costs, and the efficiency and development of the economy”; and*

- 5.3.4. Singapore: The ‘Monetary Authority of Singapore Act<sup>11</sup>’ in its ‘Principal objects and functions of Authority’ (Section 4(1)(b)) specifically states that the function of the authority should also be “*to develop Singapore as an international financial centre*”.
- 5.4. In some other jurisdictions, financial regulators are mandated to balance risk, as oppose to only reduce or eliminate it, understanding risk as a necessary element to do business. For instance, in Canada the Office of the Superintendent of Financial Institutions’ (OSFI) mandate, as directed by parliament, states<sup>12</sup> “*the need to allow financial institutions to compete effectively and take reasonable risks.*”
- 5.5. Finally, there is the case of New Zealand, where its Reserve Bank Act<sup>13</sup> (1989) establishes that the purpose of the Act is, among others, “*to promote the prosperity and well-being of New Zealanders and contribute to a sustainable and productive economy*”. This is followed by the economic objectives, which includes “*supporting maximum sustainable employment*”.
- 5.6. All the examples above show objectives that promote growth, employment and competitiveness of their industries and economies in a way that are not mutually exclusive of the regulators’ objectives on financial stability, market integrity and policyholder protection, and indeed can be synergetic.

**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?**

- 6.1. Judicial review is considered by many firms as the last resort for several reasons, including the impact that it can have in the relationship between firms and regulators, as well as the length of the process as a whole. Alternative mechanisms should be considered. We develop this further in Question 9.
- 6.2. As already mentioned, CBAs should be independently scrutinised by an appropriate independent panel or the Treasury.
- 6.3. For significant rule changes there should be a requirement to review the change by the regulators after five years and for the regulator to prove why and how the rule change has been of benefit and how the benefits outweigh the cost. Where there is no indication of benefit or the rules are not implemented consistently across the market due poor drafting of the rules there should be a further consultation process to amend the rules or the rules should be withdrawn. This is further developed in Question 9.
- 6.4. A senior executive within each regulator should sponsor a potential significant rule change and be accountable for explaining why the rule change is merited. The sponsor would be required to explain this in relevant select committees, particularly when market participants have highlighted that a change will not benefit consumers and/or will cost significantly more than the benefits provided.
- 6.5. There does need to be an independent review of rules particularly where there is no clear evidence that the rules provide any benefits. The Treasury could be responsible for the appointments and, as has already been highlighted, the relevant select committee would have a role in scrutinising the rules.
- 6.6. The Treasury should be given powers to actively suggest ways to improve rules particularly when market participants have highlighted significant concerns.

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<sup>11</sup> <https://sso.agc.gov.sg/Act/MASA1970#pr4->

<sup>12</sup> <https://www.osfi-bsif.gc.ca/Eng/osfi-bsif/Pages/so-sf.aspx>

<sup>13</sup> <https://www.legislation.govt.nz/act/public/1989/0157/latest/DLM1606600.html>

- 6.7. The current other mechanisms in place such as select committee inquiries, regular hearings and appointment hearings should remain. However, where there is a significant policy change then it may be appropriate that these mechanisms review policy changes before they are implemented and call relevant parties to the hearing to provide responses and input.

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

- 7.1. We propose a Joint Committee of both Houses of Parliament to scrutinise financial services SIs. This Committee could not only scrutinise legislation and rules regarding financial service but could also look in depth at areas of strategy and policy that it felt would help support a more effective Financial Services sector. They could also hold the regulators to account in terms of ensuring that processes such as consultation and cost benefit analysis had been robustly undertaken. The membership of the Joint Committee could include those with experience of financial services, and in addition it would be supported by a panel of experts who have experience in financial services law, policy and consumer advocacy. This would also help achieve detailed scrutiny of regulators' strategy and policy decisions from a continually informed basis.
- 7.2. Ultimately, it is for Parliament to decide how to adapt scrutiny measures. What we would like to recommend is the outcomes that process should achieve. These mainly being (i) whether regulator policy met intended policy objectives); (ii) performance against the statutory objectives / principles; and (iii) supervisory effectiveness.

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

- 8.1. Treasury Ministers have overall responsibility for the UK's financial services regulatory framework. Therefore, it is expected that HM Treasury and the regulators work closely together to formulate policy, prepare legislation and coordinate activities to develop the UK's regulatory framework.
- 8.2. The ABI agrees with the government's proposal for a general arrangement whereby the regulators consult HM Treasury more systematically on proposed rule changes at an early stage in the policy-making process and before proposals are published for public consultation. The ABI also believes that this practice should be extended to the appropriate independent statutory panels of the regulators, allowing their membership, who represent key stakeholders, to be part of this early-stage coordination with the regulators.
- 8.3. However, interactions between the regulators and HM Treasury and the panels should be more transparent as a matter of course. For instance, when a regulator publishes a consultation, it should set out what it proposed to HM Treasury and the panels, the comments it received in response and how it reacted. Regulators should also publish correspondence in situations where a regulator decides not to pursue a rule change following consultation. There will, of course, be specific, commercially-sensitive circumstances where full transparency is not suitable, but these should be the exception, and the expectation should be transparent publication.
- 8.4. Further, the ABI considers that for HM Treasury Ministers to carry on their duty to ensure an appropriate democratic policy input, HM Treasury should be able to go beyond just feeding in views, as this government's proposal suggests. For instance, the Treasury should be in a position to require the PRA or FCA to review specific rules where the rules as implemented do not provide any benefit to consumers and/or firms. This would not compromise the overall independence of the regulators on operational matters, but it would ensure democratically elected and accountable ministers are able to have more traction on key issues. This is appropriate given the significant range of powers onshored to the regulators from the EU where

such powers were subject to the detailed scrutiny of elected lawmakers in the European Parliament.

- 8.5. The ABI recognises that finding the right balance between public policy input and regulatory independence can sometimes be complex and challenging, especially in a framework where FSMA does not include any statutory objectives that guarantee public policy input. The ABI sees the addition of a new statutory objective to support economic growth as an effective mechanism to support public policy input while respecting the independent of the regulators.

**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?**

- 9.1. Stakeholder engagement is an important part of the regulator's policy-making processes and is vital to the development of fully considered regulation. The ABI believes that this review offers an exceptional opportunity to discuss how the new regulatory framework could improve the regulators' policy-making process and its stakeholders engagement.

Consultations

- 9.2. There is merit in more iterative consultation processes. Regulators should not always be expected to have all the answers immediately at their fingertips. By the time a formal consultation is published, it is often too short and sometimes seems like not every part of it is open for feedback and consideration, that some decisions have already been made and the consultation is part of a box-ticking exercise. We do not find this to always be a transparent or optimal process.
- 9.3. With this in mind, industry would appreciate a systematic early-stage engagement and, a more extensive use of consultation ahead of the thought process, so that consultations also ask about aims and principles, instead of limiting consultations to some particular sections where the issuer has already developed a position. There should be greater use of discussion papers to set the parameters for consultation rather than simply consulting directly on draft rules. By doing this, we would also be improving the efficiency of the consultation process itself, allowing a faster implementation of the outcomes for the benefit of consumers.
- 9.4. The ABI also believes that there would be a need to consult on the evaluations of the effectiveness of regulatory interventions. This would contribute to improving the quality of these evaluations. This measure could be accompanied by a requirement for regulators, or independent parties, to evaluate their interventions after a particular length of time after rules of guidance come into force.
- 9.5. Another simple but effective change that would help the industry to adapt to new regulations would be to make sure that firms have enough time to prepare for the implementation, ideally after a determined time after the finalisation of relevant secondary legislation.

Statutory panels

- 9.6. Independent statutory panels play a key role and industry welcomes the interest of the review in how the independent challenge function of the panels might be enhanced.
- 9.7. Regulators currently seek and have regard to the views of these panels, mainly during the early stages of the policy-making process and through public consultation at the formal proposal stage. However, we believe that panels could play a more relevant role in feeding in views and contribute to improving the levels of scrutiny and transparency of regulators and the work they do. For instance, we believe that independent statutory panels should scrutinise existing regulators' rules, new proposals, the evidence (including cost-benefit analyses) and the understanding of those rules. Panels should also become an alternative appeal mechanism, providing firms with a timely independent view on processes and clarification of rules. This would offer a valid alternative to the judicial review, which is only used by firms as a last resort.
- 9.8. To achieve this, HM Treasury should consider the following recommendations:

- 9.8.1. Panel memberships: If panels are to have an enhanced challenge function, the knowledge and expertise of their members should be such that panels are in a position to challenge regulators in the required different areas of the financial services. Panels should not concentrate expertise for each area of activity in just one member but more. Additionally, if panels are to remain independent, members should not be appointed by the regulators. Instead we propose that relevant trade associations/stakeholders nominate members and these are appointed by HM Treasury.
- 9.8.2. Independent secretariat: To guarantee their independence, panels should have their own secretariat or, alternatively, HM Treasury should provide secretariat support to the panels, instead of the regulators providing this support.
- 9.8.3. Legislation: Panels should be established by legislation, which should also set out the terms of reference for the membership, appointments, nomination of the chair and deputy chair, role, purpose, structure, resources, accountability and transparency measures.
- 9.8.4. Scrutiny of the regulators: Parliament should consider giving greater weight to the work of the panels in its scrutiny of the regulators, including inviting chairs of the panels to give evidence when scrutinising regulators.
- 9.8.5. Transparency:
- 9.8.5.1. Panels should contribute to improve regulators' transparency by strengthening the coordination and interaction between the two of them. More systematic consultation between regulators and panels at an early stage in the policymaking process would allow panels to consider regulator rule proposals and feed in views to the regulators' policy development process before proposals are finalised for consultation. This would complement HM Treasury views with those of key stakeholders, providing regulators with a wider range of considerations to take into account.
- 9.8.5.2. In addition, the chairs of the panels should be required to give account for their scrutiny and contribution to policy and rulemaking. The effectiveness of the panels should also be regularly scrutinised, not just in the work that they have produced but in their effectiveness in ensuring that the framework works in the manner outlined in the Call for Evidence.

Regulators' consultation obligations or practices (i.e. cost-benefit analysis)

- 9.9. As explained in our response to question 2, the ABI believes that cost benefit analyses (CBA) play a vital role in the regulatory policy making process and we encourage improving the quality of these analyses to ensure they are as robust as possible. This could be achieved by different means, including increasing the level of engagement with industry to understand better the real costs. CBAs should also be object of check and balances, in the next sub-section we suggest a mechanism to review CBAs, evaluate their accuracy and reform any derived regulatory measures when appropriate.

A more systematic review of regulator rules

- 9.10. New legislation now routinely includes a requirement for measures to be reviewed after 5 years to check those measures are achieving their intended aims.
- 9.11. Although we recognise that making this a matter of routine introduces more bureaucracy and cost, we believe that evaluation of regulatory rules is a vitally important pillar of the policy making process. We would welcome a routine, regular procedure on the rules as well as an analysis of the accuracy of the regulators original CBAs. Further, this should be a meaningful exercise, involving engagement with industry and with an effective way to implement the outcome and not just a 'box-ticking' exercise.



- 9.12. Making ex-post rule reviews a more routine part of the regulators' rule-making functions would also be essential to avoid regulators keeping rules on the books 'because they are there'.

#### Independent review of regulator rules

- 9.13. The ABI believes that a framework that carries out independent reviews is more fit for purpose. With this in mind, we support the government's suggestion about making use of independent, expert reviewers to carry out more significant reviews. These reviews should focus on existing regulators' rules and the evidence attached to them (including cost-benefit analyses).
- 9.14. With regard to the power to appoint an independent reviewer, we would recommend HM Treasury be responsible for appointments instead of the regulators, and would encourage the relevant Parliamentary select committee to have a role in scrutinising the review of regulator rules. These measures combined would help to keep a better and more balanced regulatory framework.
- 9.15. In the past, we have called for an independent review of the FCA handbook, which is currently extremely complex and unwieldy. We suggest that a temporary independent arms' length body is put in place by HM Treasury to carry out a review with the aim of streamlining the Handbook.

#### An appeal process

- 9.16. The ABI would support and encourage a function that would allow regulated firms to challenge regulatory decisions or decision-making processes without the need to have to go to court. This would be a valuable counterweight to the significant extra powers regulators have accumulated as a result of Brexit. Other regulators' processes in place, such as the Pensions Regulator's determinations panel, could be worth considering. Such an additional and alternative appeal mechanism to the judicial review would be particularly welcomed if it:
- 9.16.1. Offered firms a mechanism to clarify the interpretation of new and existing rules in a prompt manner, avoiding lengthy delays which can have a substantial negative impact on firms.
  - 9.16.2. Helped firms, especially those that often do not have the time or resource to give to the current consultation process, to develop and put forward effective arguments.
  - 9.16.3. Offered an independent view on the way processes are conducted.