A New Approach to Financial Regulation

The ABI’s Response to HM Treasury’s consultation paper ‘the blueprint for reform’

Introduction

1. The ABI is the voice of insurance, representing the general insurance, investment and long-term savings industry. It was formed in 1985 to represent the whole of the industry and today has over 300 members, accounting for some 90% of premiums in the UK. The ABI’s role is to:

   - Be the voice of the UK insurance industry, leading debate and speaking up for insurers.
   - Represent the UK insurance industry to government, regulators and policy makers in the UK, EU and internationally, driving effective public policy and regulation.
   - Advocate high standards of customer service within the industry and provide useful information to the public about insurance.
   - Promote the benefits of insurance to the government, regulators, policy makers and the public.

2. The ABI welcomes the opportunity to respond to HM Treasury’s consultation paper ‘A New Approach to Financial Regulation: The Blueprint for Reform’.

Overall Comments

3. The ABI welcomes many of the Government’s proposals in the draft Financial Services Bill but we do have some substantial concerns about how the system will operate.

   - Close co-ordination between the PRA and FCA will be necessary to ensure that the new regulatory structure operates in an efficient and effective manner. It is vital that the PRA and FCA do not duplicate each others’ activities. It is particularly important for dual regulated firms that there is effective co-ordination in order to ensure a consistent and proportionate approach to regulation.

   - Overall accountability arrangements need to be better defined to make clear who is ultimately responsible for decision-making within the system and to ensure clarity and transparency of responsibility between and within the different institutions within the system.
The proposed **timetable** is very ambitious. The financial sector is facing other substantial regulatory developments, for example RDR and Solvency II. Both firms and the regulatory authorities are stretched responding to these developments and have limited capacity to absorb further changes. The current timetable does not appear to make provision for any transitional arrangements – firms will require time to make changes to documentation and review and implement changes arising from the new rulebooks.

We think there is a clear risk that fees will increase under dual-regulation. It is therefore important that there is greater transparency to help ensure additional overheads or any rises in regulatory fees looked at across both regulatory bodies (together with FOS, FSCS and MAS) are proportionate and represent value for money for customers who, ultimately, finance regulatory costs. We believe that there also needs to be a stronger commitment by the regulatory authorities over future cost control as there has been a marked increase in regulatory fees for insurance firms over recent years.

The proposed UK architecture does not fit well with the EU structures. The **European Supervisory Authorities** (ESAs) are based on a sectoral approach (banking, insurance, securities) rather than the functional (prudential and conduct) approach being pursued by the UK Government. This will mean that there will be an onus on the UK authorities to ensure proper co-ordination to ensure that UK interests are fully represented on the ESAs by the appropriate authority. The ESAs are becoming the main source of detailed regulatory requirements for UK financial services firms for both prudential and conduct issues. In order to retain their influence the UK authorities will have to do more to guide the process of setting EU rules. This is likely to require new skills on the part of UK representatives on the ESAs – negotiating and influencing skills and a higher level of political awareness will be needed in addition to a high degree of technical skill. This needs to be taken into account in selecting UK representatives on the ESAs and more generally in the recruitment of staff to the UK regulatory bodies and the setting of work priorities and allocation of resources. The UK authorities should also work closely with industry to ensure wherever possible that a unified UK approach is taken.

We are concerned that some of the powers proposed for the new bodies may go beyond what is permissible under EU law. For example, it is by no means clear that all of the intrusive product regulation powers proposed for the FCA are permitted under the terms of MiFID or the Life and Non-life Framework Directives. Equally, it is not clear that the proposed PRA powers over branches of foreign domiciled providers of financial services are compatible with the usual split of responsibilities between home and host regulators in EU legislation. We get the impression that compatibility with EU law was a rather late consideration when the Government was formulating its proposal, and that it has been grafted on after the main ideas were fixed. Clearly it is essential for legal certainty that the Government goes back and checks that all the proposed powers are indeed compatible with EU legislation.
4. We agree with the decision of the Government to set up a Financial Policy Committee (FPC) to oversee the Bank of England’s financial stability remit and are content with most of the proposals in the Bill concerning the FPC. However, we continue to have concerns in a number of areas:

- The current proposals give the Bank of England wide powers over aspects of economic as well as regulatory and monetary policy. The Government must ensure that it retains overall control of economic management and has powers to ensure that the Bank of England complies with its priorities.

- The FPC needs to ensure that it draws on a wide variety of experience (including from the insurance sector) and we are concerned that as presently constituted the FPC is overly weighted towards Bank of England insiders.

5. We welcome the setting up of the PRA and in particular the recognition by the Government that insurers need to be considered separately and be subject to sector specific regulation.

- The proposed general objective clearly sets a micro-prudential remit for the PRA (which we believe is the correct focus) whereas the PRA seems to be required to meet this objective by focusing on financial stability issues (a macro-prudential objective). We believe that the focus of the PRA should be on its micro-prudential remit of ensuring the prudential soundness of individual institutions while macro-prudential policy is a matter for the FPC.

- We agree with the focus of the insurance objective being on policyholder protection. However, we are unclear about the implications of extending the objective to cover those who ‘may become policyholders’. While both the firm and the regulators have a clear responsibility for ensuring adequate protection of policyholders it is not clear that any such duty extends to the as yet undefined category of those who may become policyholders or what the regulatory implications of ensuring adequate protection for this class of person would entail.

- We remain unclear about how the proposed judgement-led approach will operate alongside UK regulatory requirements which will have to comply with relevant EU directives (such as CRD and Solvency II) which contain many detailed, technical rules. The UK regulatory regime sits within the EU level regulatory regime, and EU level rules and decisions take precedence over rules and decisions generated domestically. The UK regime needs to be transparently situated in its EU context if regulated companies are to avoid double jeopardy. To avoid regulatory uncertainty and supervisory confusion for regulated companies, it is essential that judgement-led decisions are communicated transparently in their EU context, and cleared prior to promulgation with the necessary EU authorities where this is necessary.
• The requirements for the PRA to consult are much improved since the initial consultations but remain less secure than those for the FCA. Many of the requirements to consult are to be developed by PRA rather than being set out in legislation.

Financial Conduct Authority (consumer)

6. The ABI welcomes the opportunity for a fresh start in conduct regulation. We need a regulatory framework that commands consumer and industry confidence and allows a competitive market to deliver positive outcomes for consumers.

• We are broadly content with the FCA’s proposed objectives and the statutory duty to promote competition. However, there should be a specific requirement on the FCA to increase access to financial products. This will ensure that FCA places due weight on the value of consumers accessing products that meet their needs, and does not act as a barrier to more saving and a resilient society.

• More clarity is needed from Government and the FSA about the FCA’s enhanced role in influencing the products that are available in the market. Regulators should not be involved in designing or approving financial products. Instead, the focus should be on effective, proactive and consistent supervision and enforcement of the existing requirements on firms to treat customers fairly, including when developing products.

• We are very concerned by the proposal that FCA could publish a warning notice indicating that it has commenced an enforcement action. This could cause lasting reputational damage to the firm (and indeed the regulator) before the facts have been fully determined, and before the case has been proven.

• We support the Financial Ombudsman Service (FOS) in its important role as an independent and free service for resolving individual disputes. However, the respective responsibilities of the FCA, FOS and the courts should be set out in statute. For example, novel points of law should be referred to the courts and broader regulatory matters determined by the FCA. In addition, new measures are needed to ensure that the FOS is properly transparent and accountable.

• We have reservations about the proposed new requirement on the FOS to publish reports of their determinations (unless the ombudsman concerned considers it ‘inappropriate’ to do so). This is a significant change in policy, particularly combined with recently enhanced FSA rules/guidance requiring firms to take account of ombudsman decisions. There is a danger that the stock of ombudsman determinations will unintentionally be interpreted by firms and consumers as a second rulebook. It may also deter firms from appealing an adjudicator’s decision to an ombudsman, even if they regard the adjudicator’s decision to be a poor one. We believe open debate and consultation is needed about the implications of this new power, led by the FCA when it is established. In the meantime, we suggest the FOS should have the statutory option (rather than statutory obligation) to publish determinations, and this should be balanced by safeguards for a firm to challenge publication which it considers would be inappropriate.
We should be wary of a 'compensation culture' being fuelled by the rapid expansion of Claims Management Companies (CMCs). CMCs are involved in nearly half of all cases that go to FOS, even though the FOS has pointed out that they do not deliver better outcomes for consumers, and they take a considerable proportion of redress payments. The current regulatory framework for CMCs (low key and under-resourced Ministry of Justice regulation) is inadequate so the Government should consider inclusion of CMCs within the regulatory scope of the FCA.

Financial Conduct Authority (markets)

7. We agree that responsibility for markets regulation should be within the FCA but have some concerns with the Government’s proposals:

- The approach of the FCA with its strong consumer focus creates a considerable risk that wholesale market conduct will be viewed through a retail lens. The output from the FCA Approach to Regulation document concedes that there may be differences between the retail and wholesale markets, but envisages greater emphasis in future on wholesale conduct, both for its knock-on effect on retail markets and for its systemic impact. More thinking is needed on this including the way in which UK approaches will interface at European level with a MiFID regime which is currently subject to review.

- As investors we are concerned that responsibility for regulation of clearing and settlement will rest wholly with the Bank of England. It is well-understood that the Bank should be closely interested in the effective and safe operation of systemically important infrastructure. However this is ancillary architecture that supports the operation of markets and needs a close working relationship to be established with the FCA as markets regulator. We believe an appropriate specification of shared responsibility, which has precedents in other jurisdictions applying similar twin peaks regulatory model, is needed for the UK.

8. The attached annex sets out our comments in more detail including comments on specific provisions in the draft Bill.
Questions for Consultation

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

We agree with the decision of the Government to set up a Financial Policy Committee (FPC) to oversee the Bank of England’s financial stability remit and are content with most of the proposals in the Bill concerning the FPC. However, we continue to have concerns in a number of areas:

- The current proposals give the Bank of England, through the FPC, wide powers over macro-prudential policy – decisions taken by the FPC could have significant impacts on the real economy. The Government must ensure that it retains overall control of economic management and has powers to ensure that the Bank of England complies with its priorities. We are not convinced that the requirement (in draft section 9C(4)) for the FPC to ensure that its actions do not have a significant adverse impact on the financial sector provides adequate checks and balances.

- The FPC needs to ensure that it draws on a wide variety of experience (including from the insurance sector) and we are concerned that as presently constituted (draft section 9B(1)) the FPC is overly weighted towards Bank of England executives.

- It would considerably aid debate about how the FPC will operate if information about the proposed range of potential macro-prudential tools was available for the pre-legislative scrutiny phase rather, than as currently proposed, only for the introduction of the Bill.

- We are concerned that the power in draft section 9H(2) will enable new rules to be imposed on firms without proper consultation. We believe that the regulatory authorities should only make rules to implement a FPC direction without consultation where this would meet the requirements of draft section 138M of FSMA. This would still enable directions to be implemented speedily where necessary but would preserve the normal procedures that apply to rulemaking by the regulatory authorities – as it stands the power in section 9H(2) will enable the normal procedures to be by-passed at the whim of the FPC.

- We are unclear about the purpose of draft section 9P. This allows the FPC to make recommendations to any person (other than the Treasury, Bank, PRA and FCA which are specifically covered by other sections of the Bill). It is unclear under what circumstances the FPC may give such recommendations, whom they may be made to, what action the recipient of such recommendations is expected to
take or what the consequences of rejecting such a recommendation might be.

It is clear that most of the thinking in relation to the work of the FPC and the macro-prudential tools that it might adopt has been focused on the banking sector. We agree that this is the correct focus given the much greater risks to financial stability posed by banks compared to insurers. However, we understand that the FPC will, quite rightly, include insurance within its remit. Therefore, there will be a need for the FPC to consider the need for macro-prudential tools to tackle problems that might arise in the insurance sector. As the Treasury and FSA have acknowledged, insurers operate different business models from banks and so it will not be appropriate for macro-prudential tools designed for banks to be applied to insurers. The FPC needs to give separate consideration to insurers and should ensure that it has access to relevant expertise within its membership in order to undertake this work.

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

We still have serious reservations about the arrangements for regulation of systemically-important infrastructure. As referred to in the Summary of Responses to the February 2011 consultation on ‘A new approach to financial regulation’ there was considerable emphasis on the need to ensure effective co-operation between the Bank of England and the FCA in an area of key concern to the markets regulator. We suggested in our response that the need for such co-operation needed to be clearly referenced in the legislation through a duty on the bank to consult the FCA and share relevant information. However, no means of promoting this co-operation has been provided under the legislative proposals.

We agree that the Bank, in its role as guardian of financial stability, needs to be closely interested in the effective and safe operation of systemically important infrastructure. The resilience of the payments system is of particular importance to the effective operation of the banking sector. However, the scope of the Bank’s regulatory and supervisory remit is now to run well beyond this and into territory that is of primary concern to the markets regulator. Just as the boundaries of banking activity have expanded and become blurred so has the definition of ancillary services and infrastructure such as central clearing houses that support banking as opposed to market activity. This is an argument for shared responsibility for supervision between banking and market regulators which we now believe needs to be enshrined in the Bill. This would also greatly enhance the ability of the UK through the FCA to engage credibly at the European level where ESMA rightly has responsibility for the relevant activities.

3 Do you have any comments on:
• the proposed crisis management arrangements; and
• the proposals for minor and technical changes to the Special Resolution Regime as described in paragraphs 2.41 to 2.44 and in Chapters 3 and 4?

We welcome the proposals in the draft Bill in relation to crisis management. However, whether the arrangements work in a crisis will be dependent on the
working relationships between the parties rather than on the legal requirements. We do not, therefore, think that we can comment further until the draft MoU on crisis management is available for comment.

There is considerable work being undertaken internationally on crisis management (for example, we understand that EU proposals on crisis management are expected in the autumn) and it is essential that any UK measures are compatible with international developments.

In relation to the wording of draft clause 43 we are concerned that 43(5)(c) could, at least in theory, allow EU authorities (notably the ESAs) to be parties to the proposed MoU on crisis management. While it is clearly important that the UK authorities maintain close relationships with the EU authorities during a crisis it is not clear that it would be appropriate for them to be party to the proposed MoU.

More generally we are concerned that almost all the thinking about crisis management, whether in the UK or at EU and international level, has been focused on banks. The very different nature of insurers means that solutions which may be appropriate in a banking context will not be relevant to insurers. In particular we would note that where an insurer fails its liabilities will fall due over an extended period which allows time for regulatory intervention and enables insolvent insurers to be resolved under ordinary insolvency laws. For these reasons we do not believe that insurers need to be subject to the equivalent of the SRR process that applies to banks.

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

We agree with the proposed scope of the PRA.

We are grateful for the recognition in the draft Bill of the need for the PRA to have a specific objective for insurers. We also welcome the proposal in draft section 2H that the PRA must give guidance on how it intends to advance its objectives and will provide specific guidance on each sector. However, we believe that further thought needs to be given to the proposed objectives of the PRA:

- We agree with the general objective as set out in draft section 2B(2). However, it is not clear to us that this is consistent with subsection (3). The general objective clearly sets a micro-prudential remit for the PRA (which we believe is the correct focus) whereas subsection (3) seems to require the PRA to meet this objective by focusing on financial stability issues (a macro-prudential objective). We believe that the focus of the PRA should be on its micro-prudential remit of ensuring the prudential soundness of individual institutions while macro-prudential policy is a matter for the FPC.

- We agree with the focus of the insurance objective (in draft section 2C(2)) being on policyholder protection. However, we are unclear about the implications of extending the objective to cover those who ‘may become policyholders’. While both the firm and the regulators have a clear responsibility for ensuring adequate protection of policyholders it is not clear that any such duty extends to the as yet undefined category of those who
may become policyholders or what the regulatory implications of ensuring adequate protection for this class of person would entail.

- We agree that provision along the lines of draft section 3F (with-profits policies) is needed and that it is correct for the PRA to be responsible for matters related to policyholders’ reasonable expectations. We will, however, consider further the drafting of the section to be sure that it is appropriate and adequate, particularly in relation to the definition of ‘surplus’.

The ABI considers that the regulatory principles should include a requirement on the PRA (and the FCA) to take account of the competitiveness of the UK financial services industry in setting its rules. The FSA is subject to a similar requirement. The UK financial services industry is a world leader and this provides substantial benefits to the wider UK economy through creating many skilled jobs, its impact on the balance of payments and on tax receipts. An effective regulatory environment is a competitive advantage for UK firms but it is essential that regulation does not damage the UK’s attraction as a centre for financial services or add burdensome costs for UK wholesale and retail consumers.

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

We remain unclear about how the proposed judgement-led approach will operate alongside UK regulatory requirements which will have to comply with relevant EU directives (such as CRD and Solvency II) which contain many detailed, technical rules. The UK regulatory regime sits within the EU level regulatory regime, and EU level rules and decisions take precedence over rules and decisions generated domestically. The UK regime needs to be transparently situated in its EU context if regulated companies are to avoid double jeopardy. To avoid regulatory uncertainty and supervisory confusion for regulated companies, it is essential that judgement-led decisions are communicated transparently in their EU context, and cleared prior to promulgation with the necessary EU authorities where this is necessary.

The requirements for the PRA to consult are much improved since the initial consultations but remain less secure than those for the FCA as many of the requirements to consult are to be developed by PRA rather than being set out in legislation. In particular, we believe that requirements for practitioner panels (similar to those currently existing for the FSA and proposed for FCA) should be included on the face of the Bill.

Paragraph 2.68 of the paper notes that the insurance industry was keen that there should be insurance expertise on the PRA Board but there is no requirement in the legislation for any of the members of the Board to have insurance (or any other relevant) expertise. We believe that the legislation should make clear that Board members will be chosen on the basis of having relevant expertise – this could take the form of a requirement similar to that proposed for FPC members in section 9B(3)(a) of the Bank of England Act 1998.

Other than this we are largely content with the detailed arrangements proposed for the PRA.
6 Do you have any views on the FCA’s objectives – including its competition remit - as set out in paragraphs 2.80 to 2.90 and in Chapters 3 and 4?

As stated in our response to the previous consultation on regulatory reform, the ABI considers that the proposed strategic and operational objectives are a sensible balance. However, the FCA should be explicitly required to facilitate consumer ‘access’ to financial services. The FSA often points out that it is not statutorily required to put weight on the potential benefits from more consumers having access to financial products that meet their basic financial needs. If the Government wants to ensure that the FCA does not act as a barrier to additional saving and a resilient society, we suggest a reference to access should be added to the efficiency/choice objective.

We support the proposed FCA free standing duty to have regard to the need to minimise the extent to which firms may be used for purposes connected with financial crime. But the FSA’s consultation on the FCA’s approach to regulation did not specify any new measures or strategy with regard to financial crime. We suggest that this is an area that requires further thought during the transition to the new regulatory framework and we urge the FSA to prioritise the development of a clear strategy for combating fraud. The FCA will need to exercise judgement on the extent to which firms should have controls in place to prevent financial crime (e.g. on anti-money laundering) given that this might adversely impact on access to insurance.

The ABI welcomes a greater regulatory focus on effective competition given its importance in delivering good outcomes for consumers. However, we agree that pursuit of competition should not be the exclusive objective of the FCA, given the other important considerations such as consumer protection and market integrity.

As stated in our response to question 4 above, we believe the FCA should be subject to a regulatory principle requiring it to take account of the competitiveness of the UK industry.

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

The ABI stresses we need a regulatory framework that commands consumer and industry confidence and allows a competitive market to deliver positive outcomes for consumers. So we support a more proactive approach to regulation but this should be risk-based, focusing on retail markets where there is evidence of consumer detriment and market failure. We can see little need to add to the FSA’s extensive rulebook and instead suggest the FCA should focus on effective, proactive and consistent supervision and enforcement of the existing requirements on firms to treat customers fairly, including when developing products. To that end, we do not support the FSA’s suggestion that the FCA will significantly reduce its investment in individual supervision of firms, as we have made clear in our response to the consultation on FCA’s regulatory approach.

We are concerned about the proposed additional product intervention powers proposed in the draft Bill and, in particular, the right to make temporary product intervention rules without consultation and cost-benefit analysis (CBA). Although we are somewhat reassured that the FCA will be required to publish a statement of policy on the use of this power, we are not persuaded that the suspension of basic
regulatory safeguards is justified. Legislative safeguards are needed to ensure that any such power is used as a last resort rather than on a regular basis.

We also remain strongly opposed to the early publication of disciplinary action against firms and we are disappointed that the Government has maintained its commitment to a power which appears contrary to natural justice. There is a risk it will cause lasting reputational damage to firms before the facts have been fully determined, and before the case has been proven. At the very least, we propose there should be stronger statutory safeguards on the use of the power, such as requirements on FCA to consider the impact of the disclosure upon the firm, and to publicise discontinuation of the enforcement action.

The FCA should be encouraged to work with the Money Advice Service to build consumer confidence about financial products so that consumers become more confident in taking responsibility for their financial decisions.

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

We are not clear why a new statutory process is needed in order for the FCA to deal with any future issues that are causing mass detriment. Given the FCA’s proposed objectives, powers (including the FSA’s recently enhanced consumer redress powers) and considerable resources it might reasonably be expected that the FCA would be in a position to take responsibility for addressing such issues, without requiring external parties to alert them. Furthermore, granting such a power to FOS may compromise their role as an independent alternative dispute resolution service, and create a public perception that they are a consumer body. However, if a process of this sort is established, consumer bodies should be required to meet clear criteria to become a nominated party, and they should be expected to submit clear evidence of detriment if they are to put an issue on the FCA’s agenda.

More generally, we do believe there is a need for more clarity about the respective roles of the FOS and the FCA. We agree with the Government that the FOS should be able to focus on processing individual complaints on a case-by-case basis rather than having to deal with mass issues. We hope that there will be few, if any, cases of mass detriment in the future, given the FCA’s commitment to early intervention and the work of the insurance industry and others to address risks of consumer detriment. But if there are future cases on the scale of PPI we agree it would be better for the regulator to take the lead in resolving the matter rather than FOS.

More broadly, we suggest that it is not the role of individual ombudsmen to privately make final decisions on precedent-setting cases, which could have wider implications for potentially thousands of similar cases. The small minority of cases that fit into this category ought to be referred to the FCA or the courts.

We believe the legislation and FCA rules should set out a clear process for decision-making on cases requiring regulatory or legal clarification, perhaps building on the recently established FOS, FSA and OFT Co-ordination Committee. This might include giving trade associations and other stakeholders the right to refer such cases to the appropriate body. The legislation should also require FOS to take account of the relevant regulation at the relevant time when making determinations.
9 What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?

In the event that the Government does provide statutory powers for FOS and other nominated parties to refer potential causes of mass detriment to the FCA, we agree the FCA should set out its response in a timely manner. It will, however, need time to consult with the industry and other parties, and to properly assess the costs and benefits of alternative approaches.

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

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

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

The approach of the FCA with its strong consumer focus creates a considerable risk that wholesale market conduct will be viewed through a retail lens. The output from the FCA Approach to Regulation document concedes that there may be differences between the retail and wholesale markets, but envisages greater emphasis in future on wholesale conduct, both for its knock-on effect on retail markets and for its systemic impact. More thinking is needed on this including the way in which UK approaches will interface at European level with a MiFID regime which is currently subject to review.

We are largely supportive of the legislative proposals as regards wholesale and markets regulation and in respect of the FCA’s role as the UK Listing Authority. As regards the latter we firmly support the Government’s decision to retain the Listing Authority role within the markets regulator.

We share the concerns, acknowledged in the consultation document, over the powers of the FCA as Listing Authority to require issuers and others to commission skilled person reports. The scope of such reports would therefore be extended to those companies who list their shares but who are in a quite different position from companies who properly come within the scope of regulatory jurisdiction as financial services companies. We are not convinced that this is a proportionate provision, or that it could with any confidence be expected to help strengthen the listing regime and maintain London’s reputation as a leading centre for capital raising and primary
markets without compromising the ability of UK businesses to obtain the financing they need.

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

The ABI is generally content with the proposed arrangements for the governance and accountability of the FCA and we particularly welcome the provision for the National Audit Office (NAO) to launch value for money investigations into the FCA.

We do, however, have serious concerns about the erosion of ‘due process’, in various parts of the Bill. In a more interventionist and judgement-based regulatory environment, the ability to challenge the regulator’s decisions should be strengthened not weakened. For example, we are surprised by the proposal that the Upper Tribunal should no longer be able express an opinion about the appropriate cause of regulatory action in the event that it does not uphold the FCA’s original regulatory decision.

As outlined in more detail in our response to Q7, we are also concerned by the planned suspension of requirements to consult and conduct a CBA when the FCA makes use of its product intervention powers, and the proposals around early warning notices.

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

Close co-ordination between the PRA and FCA will be necessary to ensure that the new regulatory structure operates in an efficient and effective manner. It is vital that the PRA and FCA do not duplicate each others’ activities. It is particularly important for dual regulated firms that there is effective co-ordination in order to ensure a consistent and proportionate approach to regulation. We, therefore, welcome the proposed statutory duty of co-operation.

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

We are generally content with draft section 3D setting out the duty to co-operate. However, we are concerned that the exemptions in section 3D(2) could, if interpreted widely, significantly limit the requirement to co-operate. We would propose that additional guidance should be given making clear the extent to which these exemptions might be used to disapply the duty to co-operate in particular circumstances.

The list of issues to be covered in the MoU in draft section 3E(2) seems comprehensive but more detailed comments are not possible until the draft MoU becomes available. However, whether the arrangements work in practice will be dependent on the working relationships between the parties rather than on the legal
requirements. It will, therefore, be important for the FSA and Bank of England to ensure that close working relationships between the units that will become the PRA and FCA are built up and maintained during the period of 'internal twin peaks' which is currently being introduced and will last until the revised legislation comes into force. These close working relationships will need to be formed at all levels of the respective organisations. We will look to the FSA and the Bank of England to keep the industry informed of its progress in developing the 'shadow' PRA and FCA and to consult where appropriate.

In relation to the proposed legislation on the MoU we have the following comments:

- Draft section 3E(4) to 3E(7) requires that the MoU is regularly reviewed and published. We welcome these requirements. However, there is no requirement for the PRA and FCA to consult on changes – we believe that the authorities should be required to consult. How the authorities work together will impact directly on regulated firms and it is important that they are able to comment on proposed changes which may impact on them.

- Draft section 3E(8)(b) allows technical or operational issues relating to co-operation between the authorities to be left out of the MoU. We are concerned that this will allow issues which have a direct and material impact on firms to be omitted and we believe that any agreements covering such issues should be made public.

From the point of view of dual-regulated firms a single point of contact and a single rulebook would provide greater clarity in their dealings with the regulators and would help to ensure that overlaps and inconsistencies were avoided. However, requiring such an arrangement on a legal basis would not be in keeping with the underlying intention of the proposed reforms. However, it would make sense for the PRA and FCA to undertake joint working wherever possible to minimise the burden on firms. It is also essential that where both the PRA and FCA have an interest in a particular section of the rule book that any rules and subsequent changes are made jointly in order to ensure that differences do not arise between the requirements of the two regulators.

We think there is a clear risk that fees will increase under dual-regulation. It is therefore important that there is greater transparency to help ensure additional overheads or any rises in regulatory fees looked at across both regulatory bodies (together with FOS, FSCS and MAS) are proportionate and represent value for money for customers who, ultimately, finance regulatory costs. We believe that there also needs to be a stronger commitment by the regulatory authorities over future cost control as there has been a marked increase in regulatory fees for insurance firms over recent years.

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

We note the Government is proposing (in draft section 55A) that authorisations should be carried out by the PRA (in consultation with the FCA) for PRA authorised firms and otherwise by the FCA. We welcome the Government’s move towards a more unified approach in comparison with its proposals in its earlier consultations.
However, the proposed approach will still require both the PRA and the FCA to have teams to undertake authorisations which could give rise to additional costs for firms. We continue to believe that the most appropriate approach would be for all authorisations to be carried out by the FCA (subject where appropriate to agreement by the PRA).

We are concerned that the proposed process for approving holders of controlled functions (clause 11) appears unnecessarily complex and is not yet fully thought through. It is unclear from the drafting which regulator will be responsible for designating and approving some functions. We would continue to suggest that it would be more appropriate for there to be a joint responsibility on the part of PRA and FCA to approve holders of significant influence functions for dual-regulated firms. Whatever system is put in place it is important that it is run as efficiently as possible to ensure that the approval process is undertaken quickly and with the minimum of overlap. Candidates should only have to put forward one application and attend a joint interview. In order to ensure this it would be appropriate, as with authorisations, for either PRA or FCA to take the lead in processing applications consulting the other as necessary.

Our members are already concerned by the length of time which it can take for the FSA to agree authorisations and approve candidates for significant influence functions and by how onerous these processes can be – we are particularly concerned that many potential candidates for roles within financial services firms (particularly non-executive directors) will be unwilling to undergo these processes thereby reducing the number of available candidates. These delays are inefficient and potentially costly. We are concerned that the current proposals will exacerbate this situation.

We are also concerned by the planned halving (from 28 to 14 days) of the minimum period that firms have to make representations before warning notices are issued, which exacerbates our concerns about early publication.

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

The ABI supports what we understand to be the Government’s main objectives in relation to FOS:

- Retaining an independent alternative dispute resolution body
- Making the respective roles of the regulator and the ombudsman service clear and distinct
- Strengthening the accountability of FOS

We therefore welcome some of the specific legislative changes included in the draft Bill, such as requiring FOS to publish an annual plan and making it subject to NAO audit.

However, we suggest additional statutory measures are needed in order to achieve the Government’s stated objectives. As set out in response to Q8 above, we believe clarity is needed about the respective roles of the regulator and the ombudsman
service in the rare occasions where individual complaints raise matters which require regulatory accountability.

To strengthen the accountability of FOS, we suggest FCA should conduct regular reviews of its overall operations, policies and procedures. This would not, and should not, compromise the operational independence of ombudsmen when adjudicating on individual cases.

We also suggest that the ombudsman service should be required to exercise its functions in a manner which is consistent with the FCA’s strategic and operational objectives and the regulatory principles. The Legal Services Ombudsman is subject to a similar high-level requirement to operate within the regulatory framework for legal services, and we consider this to be a reasonable discipline on FOS. The FOS should also be required to consult with stakeholders before it issues guidance (or ‘technical notes’) about its procedures and its approach to handling common categories of cases.

We have reservations about the proposed new requirement on the FOS to publish reports of their determinations (unless the ombudsman concerned considers it ‘inappropriate’ to do so). This is a significant change in policy, particularly combined with recently enhanced FSA rules/guidance requiring firms to take account of ombudsman decisions. There is a danger that the stock of ombudsmen determinations will unintentionally be interpreted by firms and consumers as a second rulebook. It may also deter firms from appealing an adjudicator’s decision to an ombudsman, even if they regard the adjudicator’s decision to be a poor one. We believe open debate and consultation is needed about the implications of this new power, led by the FCA when it is established. In the meantime, we suggest the FOS should have the statutory option (rather than statutory obligation) to publish determinations, and this should be balanced by safeguards for a firm to challenge publication which it considers would be inappropriate.

The ABI continues to believe that responsibility for regulation of Claims Management Companies (CMCs) should be transferred from the Ministry of Justice to the FCA, given the large number of CMCs that get involved in financial services complaints. Stronger regulation is needed to address consumer detriment associated with some CMCs, including high fees for poor service, misleading communications, unsolicited advertising and fraudulent activity.

We are content with the accountability and governance proposals in relation to the FSCS. However, there will be a need for the future funding structure of the FSCS to be determined under the new regime - FSCS funding policy is currently set by the FSA and it is unclear what will be the respective responsibilities of the PRA and the FCA. The ABI remains strongly opposed to cross-subsidy between sectors and believe that the existing arrangements should be dismantled as part of any revised policy.