

AFME consultation response

The Financial Services Future Regulatory Framework Review: Proposals for Reform (November 2021)

February 2022

Introduction

The Association for Financial Markets in Europe (AFME) is grateful for the opportunity to respond to HM Treasury's *Financial Services Future Regulatory Framework Review: Proposals for Reform*¹ (November 2021).

Executive Summary

AFME is fully supportive of the government's vision as set out in *A new chapter for financial services*² for an open, green, and technologically advanced financial services sector that is globally competitive and acts in the interests of communities and citizens, creating jobs, supporting businesses, and powering growth across all of the UK.

AFME broadly welcomes the *Financial Services Future Regulatory Framework Review: Proposals for Reform* (the proposals) which will deliver meaningful change to the financial services sector in line with the government's vision. The proposals are in line with and complementary to AFME's long standing position in support of high regulatory standards, financial stability, competitive markets, sustainable growth, appropriate levels of investor protection and responsive legislation for financial services.

We support the continuation of the Financial Services and Markets Act 2000 (FSMA) model of independent regulators acting to advance objectives set for them by Parliament as the most appropriate legislative framework. We endorse the proposed addition of secondary objectives for sustainable growth and international competitiveness to the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). We share HM Treasury's perspective that there should be a clear allocation of responsibilities in the future regulatory framework between parliament, the government and regulators. We welcome the proposals to strengthen the requirements governing how the PRA and the FCA conduct cost benefit analyses (CBAs) and review existing rules. Furthermore, AFME members would support a further strengthening the scrutiny of regulators' policy proposals.

AFME's position

UK's financial services regulatory landscape

Despite recent fundamental changes in the European financial services landscape, AFME considers that the current structure of the UK's financial services regulatory landscape remains an appropriate framework, with certain amendments, to deliver on the government's vision.

AFME strongly supports the proposal that the current structure and roles of the FCA and PRA remain the best way to deliver the financial services regulatory framework in the UK, and that the overarching model in FSMA 2000 remains the appropriate basis for regulation.

¹ Future Regulatory Framework (FRF) Review: Proposals for Reform, HM Treasury, November 2021, <https://www.gov.uk/government/consultations/future-regulatory-framework-frf-review-proposals-for-reform>

² A new chapter for financial services, HM Treasury, July 2021, <https://www.gov.uk/government/publications/a-new-chapter-for-financial-services>.

Statutory objectives and principles

The proposals introduce a new statutory objective for both the FCA and PRA requiring them to act in a way which facilitates the long-term growth and international competitiveness of the UK economy (including the financial services sector). The new objective is “secondary” meaning that it would not require the regulators to act inconsistently with their primary objectives.

Under the proposals, as well as their statutory objectives, regulators must consider certain principles when discharging their functions. One of these regulatory principles is the desirability of sustainable growth in the UK economy in the medium or long term. The consultation proposes changing this principle to clarify that such growth should happen in a sustainable way that is consistent with the UK’s net zero commitments.

AFME agrees that, as the regulators take on responsibility for setting detailed rules in areas currently covered by retained EU law, it is right that the regulators’ objectives reflect the need to support the long-term growth and international competitiveness of the UK economy, including the financial services sector. This can be done in a way that does not detract from the regulators’ existing objectives of ensuring that UK firms remain safe and sound, that the UK’s markets function well, and that consumers and users of financial services receive an appropriate degree of protection.

AFME members are strongly supportive of retaining the current structure of the UK FS regulatory landscape and of the proposals pertaining to statutory objectives and principles including a competitiveness secondary objective and sustainable growth regulatory principle consistent with the UK’s net zero commitments.

Oversight

As regulators take on more powers and responsibilities, Parliament must take on an enhanced oversight and scrutiny role.

HM Treasury proposals strengthen the engagement mechanisms between HM Treasury, Parliament and the regulators. For example, the HM Treasury plans to set up a new statutory panel dedicated to supporting the development of the regulators’ cost benefit analyses (CBAs). AFME fully supports a facts-based approach to policy making. Provided it has the requisite resources and expertise, the panel would be a principal source of independent challenge to the regulators’ CBAs. High-quality CBAs would introduce further analytical rigour in the policy-making process as the analysis would require regulators to gather and appraise data and forecast the likely impact of a proposed intervention. This ultimately would improve the quality of regulation and minimises the likelihood of unintended consequences and regulatory failure.

The consultation asks for views on whether it would be more appropriate for this panel to assess and challenge the regulator’s analysis on a pre- or post-publication basis. Whilst we recognise the requirement to balance timely intervention with analytical rigour in policy making, we support the general position that the panel’s role should be to comment on a CBA before publication. This would afford regulators the opportunity to revise their CBA and, if necessary, their proposals in light of the panel’s feedback. Indeed, if the panel were to comment only ex post, the opportunity to provide feedback and effect positive change in the timeliest manner would be lost.

Rule proposals which are broad in nature, expected to be high impact, extend rules to new products or market participants, or for which either the cost or benefit cannot accurately be assessed or is based on broad assumptions, should be subject to a pre-publication CBA panel review. Rule proposals which are narrow in focus, or limited to minor technical matters, such as the correction of handbook references or the removal of redundant rules, should not require a pre-publication review, though regulators should have the option to seek one.

The consultation proposes requiring the FCA and PRA to publish and maintain a public version of their CBA framework and rule review framework, which we welcome.

AFME members are strongly supportive of regulation based on cost benefit analyses (CBAs) and considers that a new statutory panel dedicated to assisting in the process on an ex ante basis would be beneficial.

At least once a Parliament, the proposals suggest, the HM Treasury should write to the PRA's Prudential Regulation Committee and FCA to make recommendations on issues related to matters of economic policy. The consultation proposes requiring the PRC and FCA to respond to these recommendations letters on an annual basis, covering their activity in the previous year.

It is also proposed for HM Treasury to require the regulators to review their rules where the government considers that this is in the public interest. AFME members are broadly supportive of the proposals with respect to enhanced Parliamentary scrutiny.

Additionally, AFME notes the UKFinance response to the proposals and agrees with the principles expressed in that response with respect to the desirability of strengthening the scrutiny of regulators' policy-making further still beyond the proposed power for HM Treasury to require the regulators to review their rules when necessary. Specifically by enabling designated representative bodies to require a financial services regulator to review a rule it has made and respond within 90 days with its proposed reaction. Such a mechanism would address some concerns about the limitations of the judicial review process.

AFME members are broadly supportive of the proposals with respect to enhanced Parliamentary scrutiny. AFME members recommend further strengthening measures for the scrutiny of regulators' policy proposals.

Overseas arrangements and agreements

HM Treasury also suggests requiring the regulators to consider the potential impact on deference arrangements (including equivalence) and assess compliance with trade agreements when making rules and setting supervisory approaches.

With respect to resolving the interaction between the regulators' responsibilities under FSMA and the government's overseas arrangements and agreements, we agree with the proposed approach. The consultation proposes new accountability mechanisms requiring the regulators to consider the impact of exercising their powers to make rules and set general approaches on supervision, and to assess compliance with relevant trade agreements with overseas jurisdictions. The UK's adoption of international regulatory standards is key to facilitating cross-border trade and activity. Indeed, as the consultation notes, the UK is a global leader in shaping and setting such standards in international fora.

AFME would support introducing new requirements for the regulators to consult on the positions they propose to adopt and to conduct CBAs on them before pursuing them in negotiations in international standard-setting fora. This would help to ensure that the usual rigours of domestic policy-making are applied in formulating positions that will ultimately impact domestic regulation. AFME members highlight the importance of industry dialogue alongside formal consultation as critical for successful outcomes in all aspects of policy-making.

AFME members are broadly supportive of the proposals with respect to enhanced Parliamentary consideration of overseas arrangements and agreements including deference arrangements when making rules and setting supervisory approaches. Furthermore, AFME members would support the introduction of new requirements for the regulators to be required to consult on the positions they propose to adopt in international standard-setting fora

Statutory footing

The FCA's Listing Authority Advisory Panel and the PRA Practitioner Panel's insurance sub-committee are proposed to be placed on a statutory footing, in line with the PRA's and FCA's other panels.

AFME members are broadly supportive of the proposals with respect to the FCA's Listing Authority Advisory Panel and the PRA Practitioner Panel's insurance sub-committee statutory footing.

Retained EU law

One outcome of Brexit and the onshoring process which retained much of EU legislation in UK law is that FS regulations are now distributed between the statute books and rulebooks.

We agree with the proposal for HMT to take a power to repeal parts of retained EU law, including the direct regulatory requirements that apply to firms. As with the proposed power to require the regulators to make rules in relation to specific areas of regulation, such a power is justified by the sheer volume of retained EU law to be domesticated.

AFME members point out there is a careful balancing act to be achieved between effecting appropriate policy change at a manageable pace and the costs associated with absorbing a high volume of policy changes overall. The prioritisation, sequencing and pace of policy change elements is of critical importance to the overall success of the proposals for reform. An environment of constant flux in financial services regulations is inefficient, costly and ultimately undermines competitiveness.

AFME members do not support a complete review of all UK financial services policy in parallel with the proposals for reform put forward in this review. Rather, we would support prioritising the domestication of the body of retained EU law in the first instance. With respect to the most desirable pace of the process of domestication we are looking forward to engaging with the Government.

AFME members support the government's proposal for HM Treasury to have the ability to apply "have regards" and to place obligations on the regulators to make rules in relation to specific areas of regulation. Furthermore, we believe it should apply equally across all areas of regulation – not only those which have their origins in EU law. The approach taken in the Financial Services Act 2021 to the implementation of Basel III standards provides a suitable model for how this can work in a balanced and transparent manner.

**AFME members agree with the proposal for HMT to take a power to repeal parts of retained EU law, including the direct regulatory requirements that apply to firms.
AFME members support the government's proposal for HM Treasury to have the ability to apply "have regards" and to place obligations on the regulators to make rules in relation to specific areas of regulation.**

A Designated Activities Regime (DAR) would be created, under the proposals, mirroring the current approach under the Regulated Activities Order (RAO), which would empower the regulators to make rules to replace retained EU law for specified activities (e.g. short selling and issuing securities) and potentially other activities in the future. The DAR would provide the government with an alternative mechanism to the RAO for placing activities within the regulatory perimeter. Decisions about the perimeter are critical to financial markets participants, and it therefore important that any proposals to designate an activity under the DAR be subject to appropriate Parliamentary scrutiny and approval.

The scope of any regulatory powers granted in relation to the DAR should be clearly set out. This should include, in particular, their territorial scope. There should be a clear process for establishing how questions relating to interpretation of the scope of DAR should be addressed

AFME members support collating the existing provisions into a single coherent framework. As a result of the process of onshoring EU law there are no consolidated versions of the rules, which makes them a challenge for market participants to consume.

AFME members would be supportive if HM Treasury's proposals for changes to legislation would include (as an annex) full marked up text, in the same way as the FCA typically present clear mark-ups to their handbook text. This would improve accessibility of the rules, make reviews of proposed changes more focused and efficient, enhance clarity and certainty around what is proposed, enable industry to better focus its energy, and could streamline the overall change process and compress timelines.

This will promote a more consistent approach to regulation of these activities. However, it will be important to ensure consistency of treatment for authorised and unauthorised firms carrying on the same designated activity in order to avoid the risk of divergence between the rules that apply to authorised firms and those applying to unauthorised firms.

AFME members agree with the DAR proposals and would support increased governance thereof. AFME members would support the collation of existing and future provisions into a single coherent framework.

Further Information

The Association for Financial Markets in Europe (AFME) is the voice of all Europe's wholesale financial markets, providing expertise across a broad range of regulatory and capital markets issues. We represent the leading global and European banks and other significant capital market players. We advocate for deep and integrated European capital markets which serve the needs of companies and investors, supporting economic growth and benefiting society. We aim to act as a bridge between market participants and policy makers across Europe, drawing on our strong and long-standing relationships, our technical knowledge and fact-based work.

AFME Contacts

Julian Allen-Ellis
Director, UK Coverage and Capital Markets
julian.allen-ellis@afme.eu
+44 (0)203 828 2690